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THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION. If you are in any doubt as to any aspect of this proposal or as to the action you should take, you should consult your insurance broker, solicitor, accountant or other professional adviser without delay.

In an endeavour to ensure that insurance brokers are in a position to advise their clients, a copy of this document has been sent to all brokers known to have placed business with or on behalf of Municipal Mutual Insurance Limited. Further copies of this document and the enclosed Voting and Proxy Form can be obtained by contacting the Company at 22 Old Queen Street, Westminster, London SW1H 9HW.

PROPOSAL IN RELATION TO

A SCHEME OF ARRANGEMENT

(under section 425 of the Companies Act 1985)
(the "Scheme")

between

MUNICIPAL MUTUAL INSURANCE LIMITED

and its

SCHEME CREDITORS

(as defined in the Scheme)

Your attention is drawn to the letter from the Chairman of the Company set out on pages 11 to 18 of this document which contains the recommendation of the Directors of the Company that you vote in favour of the proposal.

The action required to be taken by you is set out on pages 16 to 18. Whether or not you intend to attend the meeting of Scheme Creditors, you are requested to complete and return the Voting and Proxy Form enclosed with this document in accordance with the instructions printed thereon as soon as possible.

The meeting of Scheme Creditors to consider the Scheme will be held on Wednesday, 5th January, 1994 at 2.00 p.m. at Central Hall, Storey's Gate, Westminster, London SW1. Notice of the meeting is set out on pages 153 and 154.

The statements contained herein are made as at the date hereof, unless another time is specified in relation to them, and service of this document shall not give rise to any implication that there has been no change in the facts set forth herein since such date.

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Nothing contained herein shall constitute any admission of any fact or liability on the part of the Company with respect to any asset to which the Company may be entitled or any claim against the Company. No estimate of the value of a claim against the Company included in the Claims Table contained in the Voting and Proxy Form returned to the Company or otherwise notified for voting purposes shall be admissible against the Company or the Policyholders Protection Board (the "PPB") or be taken into account in calculating payments under the Scheme. Any such estimate shall be used solely at the meeting of Scheme Creditors to consider the Scheme for voting purposes only.

The summary of the principal provisions of the Scheme contained herein is qualified in its entirety by reference to the Scheme itself, the full text of which is set out on pages 105 to 151 of this document. You are advised to read and to consider carefully the text of the Scheme itself.

No person has been authorised by the Directors of the Company to make any representations concerning the Scheme which are inconsistent with the statements contained herein and, if made, such representations may not be relied upon as having been so authorised.

The PPB is not responsible for any of the contents of this document.

You should not construe the contents of this document as legal, tax or financial advice. You should consult your own professional adviser as to the legal, tax, financial or other matters relevant to the action you should take in connection with the Scheme.

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Introduction

This summary provides a broad overview of the proposed Municipal Mutual Insurance Limited scheme of arrangement. **Your attention is drawn to the Explanatory Statement (and its Appendices) following this summary (see Part I of this document) and the Scheme itself (set out in Part II of this document). Reading this summary is not a substitute for reading the Explanatory Statement (and its Appendices) and the Scheme in full.**

Words and expressions defined in the Scheme (on pages 108 to 113 of this document) shall have the same meaning when used in this summary unless the context otherwise requires. Some additional definitions have also been included in the text of this summary. These are intended to clarify and simplify the summary but, in the event of any inconsistency, the definitions set out in the Scheme shall prevail.

Municipal Mutual Insurance Limited ("MMI")

MMI is an insurance company limited by guarantee which was established in 1903 and which, until recently, wrote commercial lines and personal lines insurance business mainly on a direct basis. MMI and its subsidiaries and associated companies (the "MMI Group") together comprised a substantial general insurance and financial services group. In 1991, the MMI Group was the United Kingdom's ninth largest general insurer in terms of general insurance premium income. It is estimated that in 1989/90 MMI wrote some 90 to 95 per cent. of local government insurance.

Recent events

MMI suffered substantial losses between 1990 and 1992 resulting from, *inter alia*, a need to provide large increases in insurance reserves in respect of both public and employers' liability insurance. These losses reduced MMI's net assets to a level below the Department of Trade and Industry's minimum solvency requirement. The Directors attempted to dispose of all of MMI's undertaking and assets to a third party but, in the event, this did not prove to be possible. In September 1992, MMI ceased to write new, or to renew, general insurance business.

Since September 1992, a number of disposals have been made, including the sale of the right to seek renewal of the larger part of MMI's direct personal and commercial lines insurance business to Zurich Insurance Company along with a number of MMI's assets. The principal disposals are described in fuller detail in paragraph 3 of Section B of the Explanatory Statement. The Directors have taken independent professional advice on the terms and effect of each of these disposals and, additionally, the Directors are, and have been at all times when in office, required to act *bona fide* in the best interests of MMI and for proper purposes.

MMI is now engaged in the process of "running-off" its remaining liabilities and is paying agreed claims in full. This process may continue for at least twenty years. Whilst, on the basis of current information and advice, the Directors believe at the present time that a solvent run-off of MMI's liabilities can be achieved, the solvency of MMI could be affected adversely by future fluctuations in the value of property and other investment assets, decreases in investment yields, increases in liabilities and adjustments in estimated future claims payments. In the light of this, the Directors instructed Cork Gully (the insolvency practice of Coopers & Lybrand) to advise them on the options open to MMI. Cork Gully has advised the Directors that a scheme of arrangement is likely to be more beneficial for Scheme Creditors than the appointment of a provisional liquidator or liquidation and, against the background of the possibility that MMI might conceivably become insolvent (either temporarily or permanently) during the run-off period, the Directors have accordingly resolved to seek to promote a scheme. The Directors have had the assistance in developing the detailed terms of the proposed Scheme of a Sounding Board of representatives from organisations likely, or members of which are likely, to become Scheme Creditors.

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Schemes of Arrangement

A scheme of arrangement under section 425 of the Companies Act 1985 is a compromise or arrangement between a company and its creditors or any class of its creditors which becomes legally binding on the company and *all* its creditors, or *all* the class of creditors, if a majority in number representing three-fourths in value of those creditors present and voting in person or by proxy vote in favour of the scheme at a meeting convened to consider the scheme and the scheme is then sanctioned by the Court. In the event that a scheme of arrangement is sanctioned by the Court and an office copy of the Court order is delivered for registration to Companies House it will bind *all* creditors or *all* the class of creditors, as appropriate, including in either case those who voted against it or did not vote.

The basic steps involved in this process are as follows:—

- A company applies to the Court for leave to convene a meeting of its creditors, or a class of its creditors, to approve the proposed scheme of arrangement.
- The Court grants leave for the company to convene the meeting and the scheme document is posted to the creditors or class of creditors.
- The meeting of creditors or class of creditors is held and votes on whether to approve the proposed scheme of arrangement.
- If the requisite majority of votes in favour of the proposed scheme of arrangement is obtained at that meeting, the company applies for the scheme to be sanctioned by the Court.
- Having taken account of any opposition to the scheme of arrangement, the Court decides whether or not to sanction the scheme of arrangement and, if it does so, an office copy of the Court order is delivered to the Registrar of Companies, at which point the scheme of arrangement becomes binding on all creditors or, as the case may be, all the class of creditors.

The MMI Scheme

MMI is proposing to enter into a scheme of arrangement with certain of its creditors which form a separate class ("Scheme Creditors"). The definition of a Scheme Creditor has been designed in order to limit the class to a manageable number of readily identifiable and traceable organisations of good financial covenant, as is necessary for the Levy described below to be operable.

Broadly speaking, a creditor of MMI is (or will be) a Scheme Creditor if:—

(a) as at the close of business on 30th September, 1993 (the "Record Date") the records of MMI showed Scheme Liabilities (as defined in the Scheme) outstanding to it of not less than £25,000 (in the case of claims reported but not by then agreed or otherwise established, such claims being counted at the value placed on them by MMI in its records); and

(b) the aggregate amount of Scheme Liabilities to such creditor which are or have been agreed or otherwise established, together with the aggregate amount of any Elective Defence Costs (as defined in the Scheme) paid by MMI on its behalf, exceeds £50,000.

The class of Scheme Creditors so defined is estimated to count for more than 98 per cent. by value of all present and potential future insurance claims from commercial policyholders (excluding claims which would be subject to protection from the Policyholders Protection Board and Australian and New Zealand policyholders). Individuals, partnerships and unincorporated bodies of persons all of whom are individuals are also excluded from the class of Scheme Creditors as well as Australian and New Zealand policyholders and Motability Finance Limited.

Although the class of Scheme Creditors will include foreign creditors on whom the Scheme will not be binding, the Scheme contains provisions (set out on pages 119 and 126) which are designed to meet this problem.

Scheme Liabilities are liabilities of MMI under or arising out of an Insurance Contract being liabilities to which MMI was subject on the Record Date or to which MMI has or

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may become subject after the Record Date by reason of an obligation assumed by MMI before the Record Date. However, certain liabilities, including liabilities in respect of which the PPB would be under a duty to secure payment under the Policyholders Protection Act 1975 if MMI were in liquidation, are excluded from the definition of Scheme Liabilities.

Further details of what is a Scheme Liability and who is a Scheme Creditor are set out in paragraph 3 of Section A of the Explanatory Statement.

The Scheme, if sanctioned and if it becomes effective, will affect Scheme Creditors principally as follows:-

- During the Initial Scheme Period (before a Trigger Event, as described below, has occurred), all liabilities of MMI will continue to be payable in full in the ordinary course of business as and when they fall due. Insurance claims reported to MMI will be processed in the normal manner and agreed claims will be paid in full in the same way as they have in the past.
- A Trigger Event will occur if the Directors give written notice to MMI and to the Scheme Administrator that:
  (a) the Directors have concluded that, without the occurrence of a Trigger Event and the operation of the Scheme in accordance with its terms thereafter, there is no reasonable prospect that MMI will avoid going into insolvent liquidation; or
  (b) the number of Directors has fallen, and remained for seven days, below two.
- If a Trigger Event occurs, a Levy may be imposed on all those Scheme Creditors which since the Record Date have been paid (or are treated as having been paid) an amount or amounts in respect of Established Scheme Liabilities which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf since the Record Date, exceed £50,000 in aggregate.

  No Levy will be imposed on any Scheme Creditor in respect of the first £50,000 paid (or treated as having been paid) since the Record Date to or on behalf of such Scheme Creditor in respect of Established Scheme Liabilities or Elective Defence Costs.
- After a Levy has first been imposed, later payments in respect of Established Scheme Liabilities due to Scheme Creditors which have been paid (or are treated as having been paid) an aggregate amount in excess of £50,000 since the Record Date in respect of Established Scheme Liabilities or Elective Defence Costs will be made at a reduced rate (the "Payment Percentage") to the extent that the aggregate of such payments since the Record Date exceeds £50,000.
- All liabilities of MMI which are not Scheme Liabilities will continue to be payable in full as and when they fall due during the period after a Trigger Event has occurred (the "Levy Period"). In addition, Established Scheme Liabilities will be paid in full by MMI to those who are not Scheme Creditors.
- The rate of Levy and the Payment Percentage will be determined by the Scheme Administrator acting in consultation with a Creditors' Committee.
- The PPB has agreed to make certain reimbursements to MMI in respect of payments made by MMI to certain persons who are eligible for protection under the Policyholders Protection Act 1975.
- MMI will remain liable to repay any amount levied by MMI on Scheme Creditors or reimbursed to MMI by the PPB and to make good any reductions in payment to Scheme Creditors through the application of the Payment Percentage. If MMI has insufficient assets to repay these outstanding amounts in full after MMI has fully discharged all of its other liabilities then the payments to Scheme Creditors and the PPB will be reduced *pro rata*.
- If all of MMI's other liabilities have been paid in full then a commission of up to £70 million will be payable to the Scheme Creditors and the PPB as recompense for assuming under the Scheme the risk, in the case of Scheme Creditors, of having a Levy imposed on them and of suffering a reduction in payment of Established Scheme Liabilities (and losing the time value of money as a consequence) or, in the case of the PPB, of having to make reimbursement to MMI. Commission payments

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will be made in proportion to the aggregate amount of Established Scheme Liabilities paid to each Scheme Creditor since the Record Date and of sums repaid to the PPB following reimbursement by the PPB as described below.

- Any surplus assets remaining after payment in full by MMI of all liabilities, including the commission referred to above, will be distributed among the members of MMI in accordance with its Articles of Association.

Further details of how the Scheme will work are set out in paragraph 4 of Section A and Section C of the Explanatory Statement.

The Policyholders Protection Board

The PPB has agreed to join in, and be bound by, the Scheme on the following basis. When, at any time after the Trigger Date, MMI discharges any Protected Liability (as defined in the Scheme) due to a person who (being a Protected Creditor, as so defined) is eligible for protection under section 16(9) of the Policyholders Protection Act, the PPB will reimburse to MMI a certain amount, the amount varying according to whether, broadly speaking, the payment is made by MMI under a compulsory or non-compulsory insurance policy.

Management

During the Initial Scheme Period, the Directors will continue to carry on the day-to-day management of MMI. They will be subject to certain restrictions, however, and will be obliged to make periodic information reports to the Scheme Administrator on the affairs of MMI.

In the event that a Trigger Event occurs, the general powers of management and control of the business, affairs and assets of MMI will pass to the Scheme Administrator, a licensed insolvency practitioner, whose functions will include the management of the run-off of MMI's business and ensuring the carrying out of the Scheme.

The Scheme Administrator will report to a Creditors' Committee, which will be made up initially of eight Scheme Creditors which are local authorities, one member which is not a local authority and the PPB. The Scheme Administrator will consult the Creditors' Committee on a wide range of matters, including, *inter alia*, the imposition of a Levy. Scheme Creditors and the PPB (together "the Voting Creditors") have the ability to replace the Scheme Administrator if the approval of the requisite majority is obtained at a meeting of Voting Creditors.

The Scheme Administrator will be entitled to defeat voluntary winding-up resolutions and to prevent the amendment of certain Articles of Association conferring powers on him. Additionally, during the Levy Period, the Scheme Administrator will be entitled to appoint and remove Directors and to pass a creditors' voluntary winding-up resolution if Scheme Creditors and the PPB resolve that MMI should be wound up. During the Initial Scheme Period, no Controller (as defined in the Scheme) shall be appointed to, or removed from, his respective office without the prior written consent of the PPB. It is intended that the Articles of Association of MMI will be amended before the date on which the Scheme is to become effective so as to give the Scheme Administrator these powers. If such amendment is not approved by the members of MMI then the Directors will not proceed with the Scheme as currently proposed.

The Benefits of the Scheme

The report of the Managing Trustees of MMI, which forms part of the 1992 MMI Group Accounts (which are contained in Appendix B to the Explanatory Statement), contains an unaudited *pro forma* statement of net assets of MMI at 31st December, 1992 which shows the effect of the events which it is anticipated, based on available information, will result in an orderly run-off with a full payment of agreed claims. This *pro forma* statement demonstrates that, after making allowance for the effect of the run-off of its business, MMI would have net assets of £907,000, which represents a surplus of assets over liabilities of less than 0.1 per cent.

MMI's asset portfolio includes real property the value of which will fluctuate during the run-off period. The independent actuarial assessment of MMI's insurance liabilities has

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changed substantially over the past few years. Should future changes in the value of assets or liabilities place MMI in a position where, but for the Scheme, the Directors would be unable to foresee a solvent run-off, the Scheme provides a mechanism to enable MMI to continue to pay claims subject, in the case of Scheme Creditors, to the imposition of a Levy and a reduction in subsequent claims payments.

The Directors believe that the Scheme has the following advantages:—

- If the Directors were unable to foresee a solvent run-off and a provisional liquidator or liquidator were appointed, it is possible that he would himself propose a scheme of arrangement. However, there would in all likelihood be a delay of several months before he could put forward a scheme. Consequently, no claims would be paid to Scheme Creditors for a period of some months or even years until a provisional liquidator's scheme becomes effective. Furthermore, the terms of a provisional liquidator's scheme cannot be foreseen. Accordingly, the Scheme, which is promoted by the Directors, offers Scheme Creditors more certainty.
- If the Company were to become insolvent, the Scheme is expected to be cheaper to administer than a liquidation, principally because liquidation would involve various costs (including the fees of the Department of Trade and Industry Insolvency Service) which the Scheme is designed to avoid. Further costs would mean that there would be less assets available to meet the claims of Scheme Creditors in the event of a winding-up.
- Under the Scheme, MMI's non-cash assets can be realised in an orderly and timely manner rather than on a "forced sale" basis as might be the case in a liquidation. This is likely to result in the avoidance or reduction of losses on realisation.

In its letter to the Company set out as Appendix F to the Explanatory Statement, Cork Gully concludes that: "Having considered the advantages and disadvantages of the proposed Scheme respectively for the general body of the Company's creditors and Scheme Creditors as a class of such creditors as compared with liquidation or any other alternative method of dealing with the problems arising from the Company's financial position . . . it is our considered opinion that the proposed Scheme has substantial advantages for and is likely to be in the best interests of the Company's creditors generally and Scheme Creditors as a class of such creditors".

The Sounding Board

To assist in putting forward a proposal for the Scheme, MMI has held several meetings to consult an informal Sounding Board the members of which were representatives of organisations which are likely, or members of which are likely, to become Scheme Creditors. The Sounding Board members have written to MMI in the terms of a letter, a copy of which is included as Appendix G to the Explanatory Statement.

Independent advice

It must be stressed that neither the Directors nor MMI nor any of their professional advisers nor the Sounding Board nor the PPB are giving advice to Scheme Creditors on their specific position under the Scheme or in the event of liquidation. **Any Scheme Creditor which is uncertain of its own position under the Scheme or in the event of liquidation of MMI should consult its own insurance broker, solicitor, accountant or other professional adviser without delay.**

Action to be taken

The Court has directed that a meeting (the "Court Meeting") be held of those creditors of MMI which either are already Scheme Creditors by the time of the Court Meeting or which consider that they will be Scheme Creditors in the future.

A creditor of MMI will be entitled to attend and vote at the Court Meeting if both:—

(a) as at the close of business on the Record Date the records of MMI showed Scheme Liabilities outstanding to it of not less than £25,000 (in the case of claims reported but not by then agreed or otherwise established, such claims being counted at the value placed on them by MMI in its records); and

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(b) either:—

(i) the aggregate amount of Scheme Liabilities due to such creditor which have been agreed or otherwise established (together with the aggregate amount of any Elective Defence Costs paid by MMI on its behalf) already exceeds £50,000; or

(ii) such creditor considers that it has (or may have) claims against MMI, including claims which have been reported but not agreed or otherwise established and claims based on losses which have been incurred but not reported, of an aggregate amount which would, if established, result in sub-paragraph (b)(i) above being satisfied.

In relation to the Court Meeting, the expression "Scheme Creditors" includes all persons entitled to attend and vote at the meeting.

Having read and considered this document (including the Explanatory Statement (and its Appendices) and the Scheme) in full and having taken professional advice, if appropriate, creditors of MMI which consider that they are Scheme Creditors for the purposes of the Court Meeting are referred to paragraph 7 of Section A of the Explanatory Statement and the notes set out on the enclosed Voting and Proxy Form for further information on the action they should take. In the case of difficulty in completing the Voting and Proxy Form, Scheme Creditors may consult the MMI helpline on 071-222 7933.

EXPECTED TIMETABLE

Record Date for the Scheme	30th September, 1993
Latest recommended time and date for lodging Voting and Proxy Forms for the Court Meeting Note: Voting and Proxy Forms for the Court Meeting may be handed to the Chairman of the Court Meeting	2.00p.m. on Friday, 31st December, 1993
Court Meeting of Scheme Creditors	2.00p.m. on Wednesday, 5th January, 1994
Court hearing of the Petition to sanction the Scheme	Wednesday, 19th January, 1994*
Effective Date of the Scheme	Friday, 21st January, 1994*

* These dates are tentative only, since the date of the Court hearing of the Petition to sanction the Scheme has not yet been fixed.

DEFINITIONS

Words and expressions defined in the Scheme of Arrangement set out in Part II shall have the same meaning when used elsewhere in this document unless the context otherwise requires. You are referred to pages 108 to 113 of this document for the definitions.

Certain additional defined terms are also used, for the sake of clarity and brevity, in the Explanatory Statement set out in Part I of this document but, in the event of any inconsistency, the definitions set out in the Scheme shall prevail.

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PART I COPY

EXPLANATORY STATEMENT

(In compliance with section 426 of the Companies Act 1985)

A: LETTER FROM THE COMPANY

MUNICIPAL MUTUAL

15th November, 1993

To:

Creditors of Municipal Mutual Insurance Limited (the "Company" or "MMI") which are, or which consider that they might in the future become, Scheme Creditors (as defined in the Scheme of Arrangement referred to below)

Dear Sirs,

MMI, an insurance company which was established in 1903, is proposing to enter into a scheme of arrangement (the "Scheme") with certain of its creditors which form a separate class (its "Scheme Creditors", as defined in the Scheme). If approved by the requisite majority of such class of Scheme Creditors and sanctioned by the High Court of Justice of England and Wales (the "Court"), the Scheme will affect the rights of, and will bind, all of the creditors in the class.

The purpose of this document is to explain the present financial position of MMI and the provisions of the Scheme which is proposed. This document comprises three parts: Part I, an Explanatory Statement, Part II which contains the full provisions of the Scheme and Part III which contains the notice of the Court Meeting. The Explanatory Statement is divided into several sections. This letter forms Section A and provides an overview of the proposed Scheme. Section B sets out the background and history of events which have led to the proposal of the Scheme. Section C provides a summary of the provisions of the Scheme and Section D gives details of how the Scheme will be implemented.

You have been sent this document because it is believed that MMI may or may have been responsible for some or all of your insurance or reinsurance cover and that you may be, or might in the future become, a Scheme Creditor. However, receipt of this document does not necessarily mean that you are, or will become, a Scheme Creditor or that you will be affected by the proposed Scheme.

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1. Why has the Scheme been proposed?

On the basis of current information and advice, the Directors believe at the present time that an orderly run-off with the full payment of agreed claims can be achieved. In making this assessment the Directors have had to make their best estimates of the receipt of deferred consideration from Zurich Insurance Company, the realisation of certain properties and quoted investments in excess of their 31st December, 1992 valuation, the recognition of the estimated profit held within the unearned premium provision, a partial distribution of the MMI Group's superannuation scheme surplus, the surplus of future investment income, after provision for run-off expenses, and the provisions made for outstanding claims. By their nature, future expenses and income, together with the provisions made for outstanding claims cannot be estimated with certainty.

In these circumstances, the Directors consider it prudent to put forward the proposed Scheme to ensure that creditors' interests are not disadvantaged if, at any time in the future, the Directors cannot foresee a solvent run-off.

The Directors believe that a scheme of arrangement would give Scheme Creditors substantial advantages if a Trigger Event, as defined in the Scheme and explained in paragraph 4 below, were to occur. These advantages are described in some detail under the heading "Advantages of the Scheme" on pages 27 to 29 of this document. However, in summary, the significant advantage of the Scheme is the avoidance of the Company being put into insolvent liquidation (if at any time in the future the amount of its liabilities, taking into account its prospective and contingent liabilities, were to exceed (either permanently or temporarily) the value of its assets and future income or the Company were to become unable to pay its debts as they fall due), with a consequent saving of costs and avoidance of delay in payment to creditors. Under the Scheme, Scheme Creditors should, therefore, receive earlier payments with a greater value than they would if a provisional liquidator were to be appointed or MMI were to go into liquidation. A letter from Cork Gully (the insolvency practice of Coopers & Lybrand) about the Scheme is set out as Appendix F and contains important advice on where the balance of advantage lies for Scheme Creditors as between the proposed Scheme and other alternative methods of dealing with the problems which might arise if the Company were to become insolvent.

2. What is a scheme of arrangement?

Under English law (section 425 of the Companies Act 1985), a scheme of arrangement (such as that proposed here) is a compromise or arrangement provided for by statute which may be entered into between a company and its creditors or any class of its creditors. It becomes legally binding on the company and all the creditors, or all the class of creditors, if the requisite majority (a majority in number representing three-fourths in value of those creditors present and voting) of those creditors who attend and vote at a meeting convened by the leave of the Court (the "Court Meeting") vote in person or by proxy in favour of the scheme and the Court then sanctions it and an office copy of the Court order is delivered to the Registrar of Companies for registration.

3. Are you affected?

The Scheme is proposed between MMI and its Scheme Creditors. Broadly speaking, a creditor of MMI is (or will be) a Scheme Creditor if:—

(a) as at the close of business on 30th September, 1993 (the "Record Date") the records of MMI showed Scheme Liabilities (as defined in the Scheme) outstanding to it of not less than £25,000 (in the case of claims reported but not by then agreed or otherwise established, such claims being counted at the value placed on them by MMI in its records); and

(b) the aggregate amount of Scheme Liabilities to such creditor which are or have been agreed or otherwise established, together with the aggregate amount of any Elective Defence Costs (as defined in the Scheme) paid by MMI on its behalf, exceeds £50,000.

The definitions of Scheme Creditor and Scheme Liabilities have been designed in order to limit creditors falling within the class of Scheme Creditors to those which are manageable in number, readily identifiable, traceable and of good financial covenant. On

these grounds, individuals, partnerships and unincorporated bodies of persons all of whom are individuals ("Personal Creditors") have been excluded along with those creditors to whom less than £50,000 of Established Scheme Liabilities (as defined in the Scheme) become due and those with Scheme Liabilities of less than £25,000 outstanding to them on the Record Date.

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Australian and New Zealand creditors are also excluded from the class of Scheme Creditors. The reason for this exclusion is that cash is already being held in Australia and New Zealand to meet the claims of Australian and New Zealand policyholders. The Directors believe that these funds are sufficient to meet the total actual and potential insurance liabilities of the Company to its Australian and New Zealand creditors. Even if the funds deposited do not prove to be sufficient, given that the amount owing, or which it is estimated might in the future become owing, to Australian and New Zealand policyholders represents no more than 2 per cent. of the estimated total actual and potential insurance liabilities of the Company and bearing in mind the disproportionate complexity and cost of administering the Scheme in relation to Australian and New Zealand creditors (including the need to convert local currencies into Sterling for voting purposes), the Directors consider that it is in the best interests of Scheme Creditors for such creditors to be excluded. All funds remaining in Australia or New Zealand after the Company has fully discharged its liabilities to its Australian and New Zealand creditors will be returned to the Company.

Claims arising out of insurance contracts issued by MMI in favour of Motability Finance Limited are also excluded from the Scheme. Only £2.4 million of own-damage claims from Motability Finance Limited were outstanding at the end of September 1993. In view of the relatively small amount of such claims, their short-tail nature and the charitable status of the organisation, the Directors have decided that they should be excluded.

It is estimated that there will be around 700 Scheme Creditors whose actual and potential insurance claims are estimated to amount to more than 85 per cent. by value of all of MMI's estimated present and future insurance liabilities and around 80 per cent. by value of all of MMI's estimated present and future insurance and other liabilities to be incurred during the run-off.

The Court has directed that a Court Meeting be held of all creditors of MMI which either are already Scheme Creditors by the time of the Court Meeting or which consider that they will be Scheme Creditors in the future. A creditor of MMI will be entitled to attend and vote at the Court Meeting if both:—

(a) as at the close of business on the Record Date the records of MMI showed Scheme Liabilities outstanding to it of not less than £25,000 (in the case of claims reported but not by then agreed or otherwise established, such claims being counted at the value placed on them by MMI in its records); and

(b) either:—

  (i) the aggregate amount of Scheme Liabilities due to such creditor which have been agreed or otherwise established (together with the aggregate amount of any Elective Defence Costs paid by MMI on its behalf) already exceeds £50,000; or

  (ii) such creditor considers that it has (or may have) claims against MMI, including claims which have been reported but not agreed or otherwise established and claims based on losses which have been incurred but not reported, of an aggregate amount which would, if established, result in sub-paragraph (b)(i) above being satisfied.

In relation to the Court Meeting, the expressions "Scheme Creditor" and "Scheme Creditors" include all persons entitled to attend and vote at the meeting. Accordingly, even if Scheme Liabilities established in your favour and Elective Defence Costs paid on your behalf do not yet in aggregate exceed £50,000, you are still entitled to vote on the Scheme at the Court Meeting if you fall within the definition given above.

All liabilities which are not Scheme Liabilities (as defined in the Scheme), including liabilities due from MMI which do not arise out of an Insurance Contract, liabilities which are due to Personal Creditors and liabilities in respect of which the Policyholders

Protection Board (the "PPB") would be under a duty to secure payment under the Policyholders Protection Act 1975 if MMI were in liquidation will not be taken into account when determining whether a person is a Scheme Creditor.

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For a more detailed description of what is a Scheme Liability and when it becomes an Established Scheme Liability, you are referred to Section C of this Explanatory Statement.

A Record Date of 30th September, 1993 has been chosen for the Scheme because the Company prepares accounts on a quarterly basis and 30th September, 1993 is the latest date before posting this document to which such accounts have been drawn. It is considered that any advantages there may be in selecting a later record date are outweighed by the costly accounting and administrative difficulties which such a choice would cause.

4. How will the Scheme work?

The Initial Scheme Period

Until a Trigger Event, as described below, occurs (if ever), all liabilities of MMI will continue to be payable in full in the ordinary course of business as and when they fall due. Insurance claims reported to MMI will be processed in the normal manner and agreed claims will be paid in full in the same way as they have in the past.

The day to day management of MMI will continue to be carried out by the Directors. They will be subject to certain restrictions, however, and will be obliged to make information reports periodically to the Scheme Administrator and the PPB on the affairs of MMI.

The Levy Period

A Trigger Event will occur (if ever) when the Directors give written notice to MMI and to the Scheme Administrator that:-

(a) the Directors have concluded that, without the occurrence of a Trigger Event and the operation of the Scheme in accordance with its terms thereafter, there is no reasonable prospect that MMI will avoid going into insolvent liquidation; or

(b) the number of Directors has fallen, and remained for seven days, below two.

Following the occurrence of a Trigger Event, a Levy may be imposed on all those Scheme Creditors which since the Record Date have been paid (or are treated as having been paid) an amount or amounts in respect of Established Scheme Liabilities which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf, exceed £50,000 in aggregate. No Levy will, however, be imposed on any Scheme Creditor in respect of the first £50,000 paid (or treated as having been paid) since the Record Date to or on behalf of such Scheme Creditor in respect of Established Scheme Liabilities or Elective Defence Costs.

Additionally, payments made after the imposition of a Levy in respect of Established Scheme Liabilities to such Scheme Creditors will be made at a reduced rate (the "Payment Percentage") to the extent that the aggregate of such payments since the Record Date exceeds £50,000.

All liabilities of MMI which are not Scheme Liabilities will continue to be payable in full as and when they fall due during the Levy Period. Furthermore, Established Scheme Liabilities will be paid in full by MMI to those who are not Scheme Creditors.

On a liquidation of the Company, certain creditors would be eligible for protection under the Policyholders Protection Act 1975. As described in further detail below, the PPB has agreed to join in, and be bound by, the Scheme and to make certain reimbursement to the Company in respect of certain payments made by the Company to Protected Creditors (as defined in the Scheme).

From the Trigger Date, the general powers of management and control of the business, affairs and assets of MMI will pass from the Directors to the Scheme Administrator, a licensed insolvency practitioner, whose functions will include the management of the run-off of MMI's business and ensuring the carrying out of the Scheme.

Payments at the end of the Levy Period

Under the Scheme, the Company will remain liable to repay any amounts reimbursed by

the PPB or levied by the Company on Scheme Creditors and to make good any reductions in payment to Scheme Creditors. If the Company has insufficient assets to repay these outstanding amounts in full after it has fully discharged all of its other liabilities then the payments to the PPB and Scheme Creditors will be reduced *pro rata*.

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If all of MMI's liabilities have been paid in full then a commission (the "Commission") of up to £70 million will be payable to the Scheme Creditors and the PPB as recompense for assuming under the Scheme the risk, in the case of Scheme Creditors, of having a levy imposed on them and of suffering a reduction in payment of Established Scheme Liabilities (and losing the time value of money as a consequence) or, in the case of the PPB, of having to make reimbursement to MMI. The Commission will also provide compensation for interest forgone under the Scheme which would otherwise have been receivable by Scheme Creditors on a solvent liquidation of MMI although no amount of Commission payable will be calculated by reference to the length of time for which interest might otherwise have accrued. As described on page 122, the Scheme provides that no interest is repayable in respect of any period after the Trigger Date. Commission payments will be made in proportion to the aggregate amount of Established Scheme Liabilities paid to each Scheme Creditor since the Record Date and of sums repaid to the PPB following reimbursement by the PPB as described below.

In order to calculate what would be a reasonable amount of Commission, the Directors instructed KPMG Actuarial Services to analyse the risk that the level of claims paid by MMI in the course of the run-off of its business might be larger than KPMG Actuarial Services' mid range estimate of the appropriate level of reserves. KPMG Actuarial Services has written to MMI with its advice and a copy of its letter forms part of Appendix D. The Directors asked the Company's reinsurance brokers, Durtnell & Fowler Ltd., a subsidiary of Willis Corroon Group plc, to investigate the availability and cost of reinsurance for this risk. Durtnell & Fowler Ltd. have advised that it is their opinion that the insurance market is currently unwilling to provide reinsurance other than of a financial nature for this type of risk. A letter containing their advice is included in Appendix D. A financial reinsurance policy is designed to produce a quantified future payment from a given premium payment now. The Directors, with regard to the letter provided by KPMG Actuarial Services and noting the limitations listed therein, have decided that the 5 per cent. probability figure mentioned in the letter (which corresponds to approximately £70 million), represents an appropriate level of potential deterioration which might be borne by Scheme Creditors and the PPB. It is this £70 million which will be payable under the proposed Scheme in the form of Commission to Scheme Creditors and the PPB. If the Company does not have sufficient surplus assets to pay this Commission in full then Commission payments will be reduced *pro rata*.

Any surplus assets remaining after payment in full by MMI of all liabilities and the commission referred to above will be distributed among the members of the Company in accordance with its Articles of Association.

5. Protected Creditors and the PPB

In the event of a liquidation of MMI, certain creditors would be eligible for protection under the provisions of the Policyholders Protection Act 1975. The PPB has agreed to join in, and be bound by, the Scheme on a basis comparable to the position the PPB would be in if MMI were to go into liquidation on the Trigger Date. When, at any time after the Trigger Date, MMI discharges any Protected Liability (as defined in the Scheme) due to a person who is eligible for protection in accordance with that definition and under section 16(9) of the Policyholders Protection Act (a "Protected Creditor"), the PPB will reimburse to MMI a certain amount, the amount varying according to whether, broadly speaking, the payment is made under a compulsory or non-compulsory insurance policy, in each case in the currency of payment by MMI. As at 30th September, 1993 claims reported in respect of potential Protected Liabilities amounted to 11.6 per cent. of all insurance claims reported as at that date. A memorandum containing a brief summary of certain provisions of the Policyholders Protection Act is contained in Appendix I.

6. On whom is the Scheme binding?

If the requisite majority of votes is reached at the Court Meeting and the Court sanctions the Scheme, it will be binding on the Company and all Scheme Creditors, even if they voted against the Scheme or did not vote at all.

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As explained on page 12 above, a creditor of MMI is (or will be) a Scheme Creditor for the purposes of the Scheme (and the rights and obligations conferred and imposed under the Scheme) if the Scheme Liabilities shown on the Company's records to be outstanding to such creditor as at the close of business on the Record Date were in aggregate not less than £25,000 and the aggregate amount of Scheme Liabilities to such creditor which are or have become Established Scheme Liabilities (together with the aggregate amount of any Elective Defence Costs paid by MMI on its behalf) exceeds £50,000.

Some creditors of MMI will fall within this definition by the date of the Court Meeting but there will be other creditors as to whom whether or not they will fall within this category will not be known by then.

As a result of the Court's directions referred to on page 13 above, the creditors entitled to attend and vote at the Court Meeting are those creditors of MMI which either are already Scheme Creditors by the time of the Court Meeting or which consider that they will be Scheme Creditors in the future. A creditor of MMI will be entitled to attend and vote at the Court Meeting if both:—

(a) as at the close of business on the Record Date the records of MMI showed Scheme Liabilities outstanding to it of not less than £25,000 (in the case of claims reported but not by then agreed or otherwise established, such claims being counted at the value placed on them by MMI in its records); and

(b) either:—

  (i) the aggregate amount of Scheme Liabilities due to such creditor which have been agreed or otherwise established (together with the aggregate amount of any Elective Defence Costs paid by MMI on its behalf) already exceeds £50,000; or

  (ii) such creditor considers that it has (or may have) claims against MMI, including claims which have been reported but not agreed or otherwise established and claims based on losses which have been incurred but not reported, of an aggregate amount which would, if established, result in sub-paragraph (b)(i) above being satisfied.

If you consider that you are entitled to attend and vote at the Court Meeting (and are, therefore, a Scheme Creditor for that purpose) you should have careful regard to the contents of this document.

The Scheme will also be binding on the PPB, which has agreed to undertake to the Court to be bound by the Scheme.

Although the class of Scheme Creditors will include foreign creditors on whom the Scheme will not be binding, the Scheme contains provisions (set out on pages 119 and 126) which are designed to meet this problem.

Definitions of "Scheme Liability" and "Established Scheme Liability" are given in the Scheme on pages 112 and 109. If you are in any doubt as to whether you are a Scheme Creditor for the purposes of the Court Meeting or as to the action you should take, you should consult your insurance broker, solicitor, accountant or other professional adviser without delay. Additionally, should you wish any guidance on how to complete the Claims Table contained in the Voting and Proxy Form enclosed with this document, the Company has set up a telephone guidance service which you are welcome to call on 071-222 7933.

7. What should you do?

Please read the information on pages 45 and 46 carefully.

The Scheme will only come into effect if the requisite majority of those which are entitled to attend and vote at the Court Meeting (as described above) vote in favour of the Scheme. The Court Meeting has been convened to be held at Central Hall, Storey's Gate, London SW1 at 2.00p.m. on Wednesday, 5th January, 1994 for the purpose of voting on the Scheme. Notice of the Court Meeting is set out on pages 153 and 154.

If you are a Scheme Creditor for the purposes of the Court Meeting, you are entitled to attend and vote at the Court Meeting.

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Scheme Creditors may attend and vote at the Court Meeting either in person or by proxy. Scheme Creditors which are corporations may vote in person by a representative duly authorised by its governing body.

The value of all actual and potential future insurance claims of Scheme Creditors which are present (whether in person or by proxy) and which vote on whether to approve the Scheme will be noted for the purpose of determining whether or not the requisite majority needed to approve the Scheme has been achieved.

Accordingly, for voting purposes only, the estimated amount of actual and potential future insurance claims against MMI as at the Record Date will be counted. However, before arriving at the number of votes to which a Scheme Creditor will be entitled, the estimated amount of any known Security Interest, letter of credit, trust or right of set-off or cross-claim in the Scheme Creditor's favour and any amount which is expected to be recovered by MMI in respect of the Scheme Liability directly or indirectly from a co-insurer or other third party (except any reinsurer) will be deducted. **These estimates of claims will not be used by MMI, either before or after the Scheme becomes effective, for the purpose of establishing or settling claims under the Scheme and will not be binding on MMI or the PPB; they are for voting purposes only.**

Enclosed with this document you will find a Voting and Proxy Form for the Court Meeting. The Voting and Proxy Form serves three purposes. First, the Form of Proxy allows you to appoint a proxy (i.e., someone who can attend the Court Meeting and vote on whether to approve the Scheme on your behalf). Second, the Form of Proxy also allows you to direct how your proxy shall vote. Third, the Voting and Proxy Form asks you to estimate the Sterling amount of the Scheme Liabilities due to you which are, or which you consider might in the future become, Established Scheme Liabilities. This is required to determine whether you are a Scheme Creditor entitled to vote and if the requisite majority has been reached. If you have an insurance policy or claim against MMI in any currency other than Sterling, the Voting and Proxy Form explains how you can convert the amount of your claim into Sterling. This is for voting purposes only: the Scheme provides for payments to be made to Scheme Creditors in the currency of the policy.

If you are a Scheme Creditor for the purposes of the Court Meeting, you should complete and return the enclosed Voting and Proxy Form as soon as possible, whether or not you intend to attend the Court Meeting.

Please read the Voting and Proxy Form carefully, complete it in accordance with the instructions and notes printed on it and return the Form to the Company in the pre-addressed, pre-paid envelope provided. The Voting and Proxy Form may be submitted at any time before the start of the Court Meeting. However, it would be greatly appreciated and will help to avoid delay and inconvenience at the Court Meeting if you could send it to The Company Secretary, Municipal Mutual Insurance Limited, 22 Old Queen Street, Westminster, London SW1H 9HW as soon as possible and in advance of the Court Meeting. A faxed copy of a Voting and Proxy Form will be accepted subject to receipt of the original prior to or at the Court Meeting.

In order to vote and have your vote counted you must complete the Claims Table of estimated Scheme Liabilities due to you which are, or which you consider might in the future become, Established Scheme Liabilities on page 3 of the Voting and Proxy Form. If you wish to appoint a proxy, the Form of Proxy on the Voting and Proxy Form must be completed. The Voting and Proxy Form must be returned to the Company before the vote is taken at the Court Meeting, whether or not you also wish to appoint a proxy. Claims in respect of which the PPB would be under a duty to secure payment to you under the Policyholders Protection Act if MMI were in liquidation do not count for voting purposes and so must not be added to the value of any Scheme Liabilities before entering a figure in the Claims Table and Box 1 on the Form of Proxy.

To avoid delay at the Court Meeting and to the subsequent determination as to whether the requisite majority has been obtained, you are strongly recommended to return the Voting and Proxy Form to the Company as soon as possible and, preferably, by 2.00 p.m. on 31st December, 1993 but, if you do not do so, you may hand it to the Chairman of the Court Meeting before the start of the Court Meeting or when called to do so at the Court

Meeting before the vote is taken. The return of the Form of Proxy will not prevent you from attending and voting at the Court Meeting in person should you wish to do so.

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If you are a direct insured (as opposed to a reinsured) and you are bankrupt or in liquidation or are subject to any similar insolvency proceedings, a third party with a claim against you in respect of which you are covered under an insurance policy issued to you by MMI may have rights under the Third Parties (Rights Against Insurers) Act 1930. This may mean that they are, or might in the future become, Scheme Creditors of MMI and accordingly entitled to vote on the Scheme. You are, therefore, requested to notify MMI if you are a direct insured and you are bankrupt or in liquidation or are subject to similar insolvency proceedings and to provide MMI with the names of any such third party. You should also inform any such third party of the proposed Scheme. MMI will send a copy of this document to each such third party who is notified to it.

8. Further information

Further information about MMI, the effect of the Scheme and how it is proposed to be implemented is contained in the remainder of this document. Your attention is drawn in particular to the legal opinions set out as Appendix C and the text of the Cork Gully letter set out as Appendix F to this document. The legal opinions given by Mr. D.M. Barnes Q.C. and Mr. R.L. Martin Q.C. state that neither entry into nor participation in the proposed Scheme will be *ultra vires* English and Welsh and Scottish local authorities respectively. When considering the merits of voting for or against the Scheme, however, each local authority which is a Scheme Creditor for voting purposes must consider its own position separately. The Cork Gully letter contains important advice on where the balance of advantage lies for Scheme Creditors as between the proposed Scheme and other alternative methods of dealing with the problems which might arise if the Company were to become insolvent.

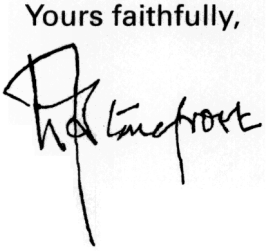
9. Conclusion

To assist in putting forward a proposal for a scheme of arrangement which would be most acceptable to those creditors of MMI which it is proposed should be bound by the Scheme, the Company has held several meetings to consult an informal Sounding Board the members of which were representatives of organisations which are likely, or members of which are likely, to become Scheme Creditors. The Sounding Board members have written to the Company in the terms of a letter, a copy of which is included as Appendix G on page 99.

In its letter to the Company set out as Appendix F to the Explanatory Statement, Cork Gully concludes that: "Having considered the advantages and disadvantages of the proposed Scheme respectively for the general body of the Company's creditors and Scheme Creditors as a class of such creditors as compared with liquidation or any other alternative method of dealing with the problems arising from the Company's financial position . . . it is our considered opinion that the proposed Scheme has substantial advantages for and is likely to be in the best interests of the Company's creditors generally and Scheme Creditors as a class of such creditors".

The Directors believe that the Scheme is in the best interests of Scheme Creditors and, accordingly, recommend that creditors which are entitled to do so vote in favour of the proposed Scheme.

Yours faithfully,



Chairman
for and on behalf of
Municipal Mutual Insurance Limited

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1. The Company

MMI was incorporated in England and Wales under the Companies Acts 1862 to 1900 as a company limited by guarantee on 13th March, 1903. MMI is authorised to carry on general insurance business in the United Kingdom under the Insurance Companies Act 1982. The Company ceased to write new or renewal business in September 1992.

2. The nature of MMI's business

Before MMI ceased to write new and renewal business on 30th September, 1992, MMI and its subsidiaries and associated companies (the "MMI Group") together comprised a substantial general insurance and financial services group. In terms of general insurance premium income, the MMI Group was the ninth largest general insurer in the United Kingdom in 1991.

MMI wrote commercial lines and personal lines insurance business mainly on a direct basis. MMI's commercial lines operations originally concentrated on the insurance of local authorities but the Company later expanded into two other insurance market sectors: direct commercial insurance of, and the provision of risk management services to, large corporations and the direct sale of commercial insurance to small companies through its regional offices. Notwithstanding this expansion, though, 82.4 per cent. of the £347 million in gross written commercial insurance premium income of MMI in 1991 was still received from local government bodies.

MMI started writing personal lines (house and motor) insurance in 1939. These products were at first limited to the staff of local authorities but were later offered to the general public. Personal lines gross written insurance premiums totalled £279 million in 1991 and, in the nine months to 30th September, 1992, totalled £219 million, reflecting the transfer on renewal of the personal lines insurance business from MMI's wholly-owned subsidiary, Municipal General Insurance Limited ("MGI").

3. Recent events

Background to recent financial difficulties

In the first quarter of 1990 MMI and MGI suffered substantial losses on their property accounts caused by the severe winter storms across Northern Europe in January and February 1990. These storms were estimated at the time to have cost MMI £30 million and MGI £10 million. Following the preparation of the management accounts for MMI for the first half of 1990, it became apparent that the level of claims for all classes of business, and not just the property accounts, were running at a significantly higher level than in 1989.

From October 1990 onwards MMI sought substantial price increases, which resulted in average premium increases on business retained in 1991 ranging from 25 per cent. for commercial property to 40 per cent. for employers' liability insurance. In addition, various management actions were taken to improve underwriting controls and the preparation and monitoring of underwriting statistics. However, as a consequence of the substantial price increases, MMI experienced a loss of market share of about 10 per cent. in 1991, although included in the lost market share were many of the customers with the worst loss ratios in the past.

In the fourth quarter of 1990 it became clear that the claims experience on MMI's local authority public and employer's liability accounts in respect of past underwriting years had deteriorated significantly. In view of the intra-group reinsurance treaties, most of the financial deterioration was falling on MGI which, if it had continued to reinsure 80 per cent. of MMI's liability portfolio, would have needed to be recapitalised. Accordingly, the intra-group reinsurance treaties between MMI and MGI were not renewed when they expired on 31st December, 1990. At the same time, MGI protected its balance sheet by purchasing for £55 million a financial reinsurance treaty which is expected to yield £105 million between 1993 and 2000, as well as obtaining, for a premium equal to the unexpired premium reserve, stop loss protection from MMI capped at the level of the losses incurred at 31st December, 1990.

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Substantial losses were also made in 1990 on the writing of personal accident policies for local authorities, which paid the cost of hiring supply teachers if teaching staff were absent from work for more than three days. Large losses were also incurred on the commercial lines insurance account in MGI and on the relaunch of the MMI Group's financial services activities as Prosperity Financial Services.

As a consequence of the above, a consolidated loss before and after taxation of £50 million was recorded for the financial year ended 31st December, 1990. In view of the Inland Revenue's treatment of MMI as a mutual company, no relief was available for the losses incurred against previous years' taxable profits.

In May 1991, it was decided to transfer all of the MMI Group's personal lines activities to MMI with effect from the first renewal after 31st December, 1991, so as to reduce the management expense burden of having separate personal lines businesses in both MMI and MGI.

The management accounts for the first half of 1991 showed that, whilst the substantial premium increases imposed since October 1990 were returning certain underwriting classes, such as commercial property and personal lines, to profitability, for other classes the premium increase had been counterbalanced by further deteriorations in claims experience. Accordingly, in October 1991 MMI announced that, with effect from 1st January, 1992, it was imposing a minimum deductible of £100,000 on each and every incident for liability insurance for its major customers (those with a ground up (i.e., without any deductible) insurance premium of £500,000 or more and all Police and Fire Authorities). In addition, further substantial premium rate increases were imposed for 1992 ranging from an average of 23 per cent. for commercial property to 50 per cent. for employers' liability. These increases led to a further loss of market share.

In the fourth quarter of 1991 it was decided to reduce substantially MGI's writing of commercial and reinsurance business in view of the losses being incurred by these two divisions and MGI's reduced level of net assets. In addition, senior management changes were made in Prosperity Financial Services to reduce the level of losses being incurred.

In March 1992, whilst the 1991 accounts were being prepared, it became apparent that another deterioration had occurred in the claims experience for local authority liability insurance, which would require a much larger provision in the accounts, and that property market values were substantially lower than at the previous year end. Accordingly, the Directors informed the Department of Trade and Industry that it was possible that MMI's and MGI's net assets were less than the statutory minimum solvency requirement calculated in accordance with the Insurance Companies Act 1982. At the same time, the Directors commissioned an independent actuarial review of MMI and an independent valuation of the MMI Group's property portfolio.

In view of the MMI Group's financial position, the Directors decided to cease writing new business in MMI's Australian and New Zealand branches in March 1992. MGI decided to cease writing new commercial insurance and, on 8th April, 1992, sold the right to renew MGI's account to GAN Minster in exchange for free claims handling until 8th November, 1993 . As a consequence of the GAN Minster sale, all the senior management and most of the staff employed in MGI's commercial division were made redundant. A temporary cessation of writing inwards reinsurance in MGI was announced in April 1992 and remained in force until the announcement on 30th September, 1992 of a permanent cessation.

In April 1992, the independent valuation of the MMI Group's property portfolio was received, which reduced the net assets of the MMI Group by £41.2 million. As a consequence, MMI's and MGI's net assets were less than the statutory minimum solvency requirement under the Insurance Companies Act 1982. In view of MMI's inability as a company limited by guarantee to raise external capital, the Directors decided, with the agreement of the Department of Trade and Industry, that the best course of action was to attempt to transfer the whole of the business of the MMI Group to another insurance company with the capital resources necessary to re-finance the MMI Group. Having established that there was serious interest on the part of a number of identified prospective purchasers, MMI issued a press statement on 7th May, 1992 which announced that "discussions were taking place which might lead to proposals being put to members for the transfer of its business to another company".

At the same time, Mr Andrew Maclean, who had been Group Chief Executive since 1985, left MMI. On 11th May, 1992, Mr Brian Wright, a recently retired executive director of Sun Alliance Group plc, joined the MMI Group as Group Chief Executive. The General Manager of MGI also left the MMI Group in May 1992.

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The management of the MMI Group had become increasingly concerned in 1992 about the quality of parts of the commercial insurance business written in MGI during 1990 and 1991. A full in-depth review of the commercial insurance activity of MGI was undertaken in May and June 1992 as a result of which MGI's claim provisions were increased by £43 million and additional reinsurance was purchased to provide further protection for the account.

The MMI Group's accounts for 1991 were completed on 6th July, 1992 showing a consolidated loss after taxation for 1991 of £239 million and net assets of £5 million. At the same time, management accounts for the four months to 30th April, 1992 were published showing a loss after taxation of less than £9.6 million and net assets of slightly over £3 million.

These results reflected the fact that the combined effect of the premium increases and the introduction of a substantial deductible had finally stemmed the losses.

In July 1992, Heads of Agreement were signed with La Garantie Mutuelle des Fonctionnaires ("GMF") for them and certain other members of the Eurosafe consortium to acquire the whole of the MMI Group. At the end of September 1992, following press speculation, the prospect of such a sale faded and the Directors of MMI concluded that further negotiations with GMF would not be fruitful. With no alternative acquirer at an advanced stage of negotiation, the Directors announced on 30th September, 1992 that MMI and MGI would cease to write new business or renew existing policies with immediate effect and a seven day claims payment moratorium for MMI and MGI was announced whilst the MMI Group's financial position was assessed.

Fresh approaches were made to various insurance companies and a positive response was received from Zurich Insurance Company ("Zurich"), which indicated a firm interest in entering into an agreement to acquire the right to renew MMI's business and certain business assets for a consideration that the Directors of MMI evaluated as being sufficient to enable MMI to run off its activities. As a consequence, on 6th October, 1992 MMI and MGI resumed the full payment of claims, although there has been no resumption of the writing of new business or renewal of existing policies.

Since 6th October, 1992 the MMI Group has concluded 17 separate disposals of businesses with a view to strengthening the financial position of MMI and the MMI Group and assisting the orderly run-off of the MMI Group's activities. The principal disposals are described under the heading "Disposals" below.

At a General Meeting of MMI on 24th March, 1993, the members of MMI approved certain amendments to MMI's Articles of Association so as to provide a continuing membership of MMI in view of MMI ceasing to write new business after 30th September, 1992.

In April 1993, the Directors received the result of an independent valuation of the MMI Group's property portfolio as at 31st December, 1992, which reduced the carrying value of the properties in the MMI Group accounts by a further £31.1 million. The down-valuation of the property portfolio was in line with the Directors' expectations.

In preparation for Mr Brian Wright's retirement as Group Chief Executive on 31st May, 1993, Mr Philip Gregory was appointed Acting Group Chief Executive on 1st May, 1993 and Group Chief Executive on 31st May, 1993.

In May 1993, independent actuarial advice was received from KPMG Actuarial Services to assist the Directors of MGI in establishing the undiscounted claims provisions as at 31st December, 1992. On receipt of this advice the Directors of MGI strengthened claims provisions further, having already strengthened claims provisions following actuarial reviews in September and December 1992. Following receipt of the KPMG Actuarial Services report, the Directors of MGI asked the Directors of MMI for financial support to enable them to continue to foresee a solvent run-off of MGI. After careful consideration and after taking independent professional advice, and confirming that the Department of

Trade and Industry had no objection, the Directors of MMI concluded in June 1993 that the financial cost to MMI of MGI having to seek the protection of a Provisional Liquidator would be greater than the financial support requested by MGI. Steps were, therefore, taken to unwind the complex insurance and reinsurance relationships between MMI and MGI. These steps are described in greater detail below under the heading "The relationship between MMI and MGI".

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On 10th September, 1993, KPMG Actuarial Services completed their report to the Directors on MMI's and MGI's claim reserves as at 31st December, 1992. Accordingly, on 30th September, 1993 the audited accounts for the year ended 31st December, 1992 were completed. The accounts for 1992 show a consolidated loss after taxation of £108 million and net liabilities as at 31st December, 1992 of £145.3 million.

The 1992 final audited accounts, including the report of the Managing Trustees, and the unaudited accounts of MMI to 30th June, 1993 are set out in full as Appendix B.

Since completing the Zurich transfer on 9th March, 1993 the activities and assets of several subsidiaries have been transferred to MMI as part of the process of simplifying the run-off process. This process will continue as part of the orderly run-off of the MMI Group.

MMI's three principal remaining corporate investments, in Prime Health Limited, Prosperity Financial Services Limited and Dartford International Ferry Terminal Limited are now being marketed. It is not likely that these companies will be sold until 1994.

As a consequence of the corporate transactions which have occurred, the MMI Group now comprises MMI, MGI, the three investments being marketed for disposal and a number of small subsidiaries the activities of which are being transferred to MMI.

Disposals

Since 6th October, 1992, the MMI Group has made seventeen separate disposals of parts of its business (the principal disposals being described below) with a view to strengthening the financial position of MMI.

Having regard to their existing duty to act *bona fide* in the best interests of the Company (which, in the circumstances, would include the interests of MMI's creditors) and for proper purposes, the Directors obtained independent professional advice on each of the disposals described below. This included an overall assessment of the assets and liabilities being transferred by Cork Gully, who advised on whether remaining creditors were put at any disadvantage by the disposal under consideration, the advice of KPMG Actuarial Services on matters of insurance reserving, legal advice from Slaughter and May and the overview and authorisation, where appropriate, of the Department of Trade and Industry as regulator.

On 20th October, 1992, MMI sold most of the facilities management contracts and most of the net assets of Municipal Mutual Computing Limited to The CFM Group Limited for a consideration of £3,392,000.

In early November 1992, in advance of the main agreement, it was agreed that Zurich would offer renewal terms to MMI's policyholders in exchange for a consideration, part of which would be an advance payment of the deferred consideration payable by Zurich under the main agreement.

On 23rd December, 1992, General Accident Fire and Life Assurance Corporation Plc ("GAFLAC") assumed responsibility and liability for MMI's remaining obligations under certain contracts of buildings and/or contents insurance entered into by MMI with persons introduced to MMI by Cheltenham and Gloucester Building Society. The transaction included the transfer of certain of MMI's investments and other assets to GAFLAC. Subsequently, the underlying policy liabilities have been transferred to GAFLAC under section 51 of the Insurance Companies Act 1982.

In early January 1993, MMI agreed with Zurich, in exchange for a consideration of 10 per cent. of the unexpired premium, to allow it the right to effect mid-term transfers of those commercial customers who wanted to transfer their policies to Zurich.

On 24th February, 1993 MMI (together with MGI) entered into an arrangement with Cornhill Insurance Public Limited Company ("Cornhill") whereby Cornhill assumed

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responsibility and liability for the remaining obligations of MMI and MGI under certain contracts of motor insurance entered into by MMI and MGI respectively with persons introduced to such companies by Automobile Association Insurance Services Limited ("AA Insurance"). As part of the transaction, certain of MMI's and MGI's investment and other assets were transferred to Cornhill. Subsequently, the underlying policy liabilities have been transferred to Cornhill under section 51 of the Insurance Companies Act 1982.

On 9th March, 1993, MMI sold the right to seek renewal of almost all of its direct personal and direct commercial lines insurance business (and certain related businesses) to Zurich. The sale included the acquisition by Zurich of a substantial part of MMI's infrastructure, including the transfer of 1,530 of MMI's employees. A subsidiary of Zurich also acquired the freehold of MMI's Bournemouth premises and Zurich agreed to take out leases on a number of MMI's other properties from which Zurich will conduct the acquired business.

At the same time, Municipal Mutual Computing Holdings Limited ("MMCH"), MMI's subsidiary responsible for providing computer services to companies within the MMI Group, sold substantially all of its computing business and assets to Zurich.

As consideration for the transactions, Zurich paid MMI and MMCH £19.6 million for the assets acquired. Zurich agreed to provide to MMI and MGI, free of charge for an initial period of three years from the date of completion of the sale and thereafter at net cost, claims processing and administration services in respect of most of the insurance business written by those companies prior to 30th September, 1992.

In addition, deferred consideration of up to £44 million is to be paid by Zurich based on the gross premiums received by Zurich from the business transferred in the 36 months from the date of sale, subject to a maximum consideration if Zurich's premiums exceed £600 million. On the basis of Zurich's renewal of MMI's business subsequent to the agreement it is anticipated that this maximum figure of £44 million will have been received by MMI during 1994.

On 1st April, 1993, the Group contracted out its investment management function to Commercial Union Investment Management Limited ("Commercial Union"), with most of the staff previously employed by MMI on such investment management functions moving to work for Commercial Union.

On 29th June, 1993, MMI sold its entire interest in Prosperity de Seguros y Reaseguros SA, its Spanish life assurance subsidiary formed in 1989, to The Standard Life Assurance Company for a cash consideration of £5.5 million.

On 6th August, 1993, MMI (together with MGI) entered into an arrangement with Eagle Star Insurance Company Limited ("Eagle Star") whereby Eagle Star assumed responsibility and liability for the remaining obligations of MMI and MGI under certain contracts of buildings and/or contents insurance entered into by MMI and MGI respectively with persons introduced to such companies by AA Insurance. As part of the transaction, certain of MMI's and MGI's investment and other assets were transferred to Eagle Star. Subsequently, the process of transferring the underlying policy liabilities to Eagle Star under section 51 of the Insurance Companies Act 1982 was commenced.

Also on 6th August, 1993, MMI (together with MMCH and Housing Standards Company Limited) entered into an agreement with Zurich for the sale of its business of providing structural warranty services (the "Building Guarantee business"). The sale included the transfer of all of the MMI employees and assets engaged in the Building Guarantee business for a consideration of £248,000. MMI retains responsibility and liability for its obligations in respect of structural warranties issued prior to the date of the agreement other than for outstanding and future inspections which, together with claims processing and administration, will be undertaken by Zurich free of charge.

On 22nd September, 1993, MMI sold to Credit Local de France ("CLF") its remaining shares in CLF Municipal Bank plc (formerly Municipal Mutual Bank plc) for a cash consideration of £5,528,000. In January 1992, MMI had sold a 51 per cent. interest in CLF Municipal Bank plc to CLF following a reassessment of the strategic value of owning a small bank.

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The relationship between MMI and MGI

As mentioned above, steps have also recently been taken, to which the Department of Trade and Industry raised no objection, to unwind the complex insurance and reinsurance arrangements existing between MMI and MGI. On 9th July, 1993 MMI and MGI agreed that MMI would (i) purchase for £15 million from MGI the entire issued share capital of Prime Health Limited, MGI Prime Health Sales Limited and Prime Healthcare Consultancy Limited and (ii) subscribe at par for 30 million new ordinary shares of £1 each in MGI, as consideration for (a) the cancellation of an 80 per cent. Liability Quota Share Agreement, a Stop Loss Agreement and two 30 per cent. Quota Share Bouquet Treaties between MMI and MGI and (b) MGI agreeing either to novate to MMI certain reinsurance arrangements (including a £105 million financial reinsurance contract) or to hold the benefit of certain reinsurance arrangements on trust for MMI. Novation of the reinsurance arrangements has the benefit of protecting MMI and its creditors from any delay or shortfall in payment to MMI by MGI under the quota share agreements and treaties, which might have arisen were MGI to have gone into insolvent liquidation before all amounts payable to MGI under the reinsurance arrangements had been paid.

In view of the potential conflict of interest that arose for the directors of MMI who were also directors of MGI, the board of MGI took separate independent professional advice, from different professional advisers to those used by MMI, before entering into the transactions described above.

As a consequence of the transactions described above, the continuing solvency of MMI is no longer dependent on the continuing solvency of MGI. However, the following relationships between MMI and MGI continue to exist:-

(a) MMI owns all of MGI's issued share capital;

(b) at 31st October, 1993, MMI owed MGI £1,558,371 on its inter-company account;

(c) MMI is the employer of the 31 employees who are seconded full time to MGI and for whose emoluments MGI reimburses MMI in full;

(d) MGI occupies space in a building owned by MMI at an open market commercial rent under an informal arrangement;

(e) in the past, MMI has insured certain assets with MGI. There were no material claim payments outstanding at 31st October, 1993;

(f) MMI has contracted to provide claims handling services to MGI until the MGI personal lines account is run-off. MMI received a one-off payment of £1.15 million in 1992 for the provision of such services; and

(g) MMI and some of its subsidiaries may occasionally incur expenditure of an overhead nature on behalf of MGI, for which they are fully reimbursed by MGI.

Management and employees

As stated earlier, Group Chief Executive, Mr. Andrew Maclean, left MMI on 6th May, 1992. He was replaced by Mr. Brian Wright who was recruited after his retirement as an executive director of Sun Alliance Group plc to manage the orderly disposal of the MMI Group's assets. Following the completion of the Zurich disposal, Mr. Brian Wright retired and Mr. Philip Gregory, formerly Group Finance Director, succeeded him as Group Chief Executive on 31st May, 1993.

The present Group Chief Executive, Mr. Philip Gregory is contracted to remain with the Group until the summer of 1994, but has indicated that his role would be completed by that stage and that he would wish to leave the MMI Group at that time. Accordingly, Mr. John Barber, who was formerly a senior executive with the Royal Insurance group for 24 years, was appointed a director and Deputy Chief Executive on 3rd November, 1993 with the intention that he should succeed Mr. Gregory as Group Chief Executive, subject to the confirmation of the Board at the time and the approval of the Department of Trade and Industry.

In addition, Mr. Allan Castle was appointed Group Finance Director (a post vacated by Mr. Gregory on 30th April, 1993) on 1st November, 1993, having been Group Financial Controller for the previous three and a half years.

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The number of Directors has reduced from 21 at the Annual General Meeting in 1991 to the present number of 12, of whom three are executives and the remaining nine are non-executive. The Chairman, Mr. Maurice Stonefrost, has indicated his wish to retire from the Board by the end of 1993 and it is the intention of the Board to appoint Sir John Lovill as Chairman in his place. The Board intends to reduce the number of directors of both MMI and MGI to eight at or before the next Annual General Meeting of MMI, in line with the reducing number of subsidiaries and activities. In addition, it is the intention of the Board to have at least three executive directors on the Boards of both MMI and MGI.

In addition to other amendments which are to be made in connection with the implementation of the Scheme, it is also intended to amend MMI's Articles of Association to provide a more relevant framework for the run-off of MMI's business.

As a result of transfers of business and reorganisation of MMI to reflect the fact that new and renewal business is no longer being written, staff numbers have fallen from over 1,600 on 30th June, 1992 to 61 on 1st November, 1993.

At 1st November, 1993, the MMI Group employed 559 employees of whom 92 were employed in either MMI or MGI. Fifteen of the existing staff working on broker introduced personal lines claims are under notice of redundancy in line with the anticipated run-off of liabilities. Thereafter, the number of staff employed is anticipated to decrease slowly over the remaining period of the run-off in line with the level of ongoing activity.

Accordingly, it is believed that the MMI Group currently has an appropriate level of management and staff for its future run-off activities.

4. The current financial position

The audited accounts of MMI and the MMI Group as at 31st December, 1992 and the consolidated unaudited accounts of the MMI Group for the six months ended 30th June, 1993 are set out as Appendix B. Management accounts for the nine months ended 30th September, 1993 have not yet been completed.

The audited accounts for 1992 show net liabilities for the MMI Group as at 31st December, 1992 of £145.3 million. However, the MMI Group figures include MGI. Accordingly, the most relevant financial information for consideration by creditors of MMI is MMI's balance sheet as at 31st December, 1992, which shows net liabilities of £129.9 million.

In preparing MMI's balance sheet at 31st December, 1992 there were two large items which required considerable judgment in assessing the appropriate carrying value for the balance sheet, namely the market value of properties and the provision for outstanding claims. Accordingly, the Directors commissioned independent advice for both items.

Over fifty of the highest value properties were valued as at 31st December, 1992 either by Chesterton, in respect of properties in England and Wales, or by Ryden, in respect of those in Scotland. The remaining properties, which together comprise only 20 per cent. by value, were valued by the MMI Group's professional staff who are members of the Royal Institution of Chartered Surveyors.

In respect of the provision for outstanding claims, the Directors commissioned KPMG Actuarial Services to assist the Directors in establishing the undiscounted claims provision for all classes of business, except for Australia and New Zealand where Coopers & Lybrand in Australia assisted the Directors. In this connection, Note 18 to the 1992 accounts contains an important description of the position:—

> "Provision is made in the accounts for the estimated cost of claims notified but not settled at the date of the balance sheet and for the estimated cost of claims incurred but not notified at that date. Independent actuarial advice has been received from KPMG Actuarial Services to assist the Managing Trustees in establishing the undiscounted claims provisions for all classes of business, except for overseas branches and agencies, for both the Company and MGI as at 31st December, 1992. The provisions have been made having regard to the past claims experience, current judicial interpretations of the law and other relevant information currently available.

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However, no allowance has been made for any new categories of claim not so far reflected in the experience seen. Furthermore, the inherent uncertainty of the insurance process makes it likely that historical data will not be wholly predictive of the actual future emergence and development of claims. In addition, a substantial measure of judgement is involved in both establishing the individual claim provisions and in interpreting the past claims experience as part of the process of establishing the total claims provision. By their nature certain classes of business are inherently more uncertain than others and the ultimate cost of their claims is more likely to vary as a result of subsequent developments. These classes include liability business in both MMI and MGI and in particular, the establishment of provisions in MGI for certain stop loss reinsurance contracts for Lloyd's members' in respect of 1989 to 1991 is especially uncertain."

The Company's audit report is set out on page 78 of this document and you are recommended to read the report in full.

As has been noted above MMI's balance sheet as at 31st December, 1992 shows net liabilities of £129.9 million. However, this does not take account of future income and expenses until completion of the run-off, the likely movement in asset values during that period and transactions completed subsequent to 31st December, 1992. In order to illustrate the Directors' best estimate as at 30th September, 1993 of the effect which events during the run-off are likely to have on MMI's financial position, the Directors presented the following unaudited *pro forma* statement of net assets of MMI as at 31st December, 1992 in their report on the 1992 accounts:—

Unaudited *pro forma* statement of net assets of MMI at 31st December, 1992

	Company balance sheet *£000*	Adjustments *£000*	Pro forma net assets *£000*
Fixed assets	5,547	—	5,547
Investments and property	375,965	34,000	409,965
Associated and subsidiary companies	44,612	—	44,612
Current assets	374,812	91,232	466,044
Total assets	800,936	125,232	926,168
Liabilities	930,852	(5,591)	925,261
(Deficiency)/surplus of assets	(129,916)	130,823	907

The pro forma net assets show the estimated financial position of the Company at 31st December, 1992 and is based upon the audited balance sheet of the Company at that date after making the following adjustments:—

(a) Current assets above have been increased by £44,000,000 to reflect the deferred consideration receivable under the terms of the Agreement with Zurich. The Managing Trustees believe that, based on information on current levels of business renewal, the maximum amount will have been received by the Company during 1994.

(b) Investments and property have been increased by £34,000,000 to reflect the anticipated proceeds from the sale of properties and quoted investments in excess of their valuations as at 31st December, 1992. The Managing Trustees consider, based on the information available to them, that such proceeds are a realistic projection given the current plan for the orderly disposal of the Group's properties and quoted investments over the next seven years.

(c) Current assets have been increased by £2,500,000, being an estimate of the after tax receipt from a partial distribution of the Group's Superannuation Scheme surplus in 1996. A formal actuarial valuation of the Scheme at 31st March, 1993 is currently being undertaken.

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(d) Unearned premium provision has been reduced by £5,591,000 to reflect the anticipated profit which will arise from the balance held at 31st December, 1992.

(e) Current assets have been increased by £44,732,000 representing the surplus of investment income after provision for run-off expenses and the additional investment income which the Company expects to generate on realisation of the assets at the values described in (a) to (d) above.

No adjustment has been made for the tax recoveries which would result from a favourable outcome of discussions being held with the Inland Revenue regarding the mutual taxation status of MMI (see note 10 to the 1992 accounts). If there were a favourable outcome, MMI would receive a repayment of tax already paid of approximately £24 million and would have sufficient tax losses carried forward to extinguish an estimated £24 million of future tax payable over the run-off period.

The unaudited *pro forma* statement of net assets summarises the basis upon which the Directors anticipate, based on information currently available, that there will be an orderly run-off with a full payment of claims. However, by their nature, future expenses and income, together with the provisions made for outstanding claims, cannot be estimated with certainty. Accordingly, it is almost certain that the actual outcome will vary from the *pro forma* statement of net assets, although it is not possible to determine at this stage whether any variation would be positive or negative. In this connection, a positive margin of less than £1 million after discharging liabilities of £925 million is small and is the reason for the Directors promoting the Scheme in order to minimise the disruption and financial loss which creditors may suffer should any future variation in MMI's financial position be adverse.

5. Proposal for a Scheme of Arrangement

In view of the Company's current financial position, the Directors instructed Cork Gully to advise them on the options open to MMI.

Cork Gully has advised the Directors that a scheme of arrangement is likely to be more beneficial for Scheme Creditors than the appointment of a provisional liquidator or liquidation and, against the background of the possibility that MMI may become insolvent (either temporarily or permanently) during the run-off period, the Directors accordingly resolved to seek to promote a scheme.

6. Advantages of the Scheme

As a result of the financial difficulties experienced by MMI, there is a risk, due to changes in future asset values or future reserving estimates, that MMI might become insolvent, either temporarily or permanently, during the period of run-off of its insurance business and, as a consequence, a provisional liquidator or liquidator being appointed in respect of it or its business and assets. The Directors believe that there are significant advantages for Scheme Creditors under the Scheme as opposed to an insolvent liquidation or receivership. In particular:-

6.1 were a provisional liquidator to be appointed, it is possible that the provisional liquidator would himself propose a scheme of arrangement but there would in all likelihood be a delay of several months before he could put forward a scheme, during which time no claims would be paid, and the terms of the Scheme could not be foreseen. A scheme promoted by the Directors would offer Scheme Creditors more certainty;

6.2 if MMI were to become insolvent, the Scheme is expected to be cheaper to administer than a liquidation, principally because a liquidation will involve various costs (including the fees of the Department of Trade and Industry Insolvency Service) which the Scheme is designed to avoid. In a liquidation, statutory fees are levied upon realisations and investments made by a liquidator, details and examples of which are contained in paragraph 3.4 of the Cork Gully letter to be found as Appendix F. The realisations fees charged in a compulsory liquidation are on a sliding scale but in a voluntary liquidation are limited to £12,500. However, in a compulsory liquidation, realisations of £800 million would, for example, attract fees in excess of £1 million. In addition to the fee charged on realisations, a separate

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charge of 0.625 per cent. is imposed on all investments made by a liquidator and each reinvestment thereof whether or not the liquidation is compulsory or voluntary. It is not possible to say with any certainty what such fees would amount to over the period of the liquidation but on the basis of the assumptions set out in paragraph 3.4 of the Cork Gully letter the fees would be within the range of £35 to £45 million;

6.3 under the Scheme, MMI's non-cash assets could be realised in an orderly and timely manner rather than on a "forced sale" basis, which would be likely to occur under any of the alternative methods of dealing with MMI's financial difficulties and which would result in significant losses on realisation being avoided or reduced;

6.4 under the Scheme, claims will continue to be paid as and when they become established even after a Trigger Event has occurred, albeit at a reduced rate. Under a liquidation there would be likely to be considerable delays before any distribution is made by a liquidator. This is because a liquidator will not want to make any distribution to creditors until he has had time to assess MMI's liabilities. He will not want to pay away assets too early at the risk of having insufficient assets to pay like distributions to later proving creditors. Thus, creditors would have to bear substantial financing costs before being paid in a liquidation;

6.5 under the Insolvency Regulations 1986, a liquidator is restricted to investing funds available in Government securities such as Treasury Bills. In a scheme this restriction would not apply and therefore a higher return on investment should be achievable by normal commercial placement; and

6.6 Scheme Creditors will be paid in the currency of their policy whereas, in a liquidation, the liquidator would be required to convert creditors' claims into Sterling at the exchange rate on the date of the liquidation, even though many of these claims may not be established for some time and creditors could be exposed to currency mis-matches between dividends and claims.

The Directors consider that the Scheme should operate to give Scheme Creditors a higher return than in a liquidation on a net present value basis. It is particularly important to take into account the time value of money and the potential benefits accruing through payments being received earlier under the Scheme.

In comparing the Scheme with a liquidation the following should be considered:—

(a) although claims arising under current policies after the Trigger Date will continue to be paid in accordance with the provisions of the Scheme (when, if MMI had gone into liquidation on the Trigger Date, only unexpired premiums would have been repayable to policyholders), since the potential future liability of MMI under current policies is only of relatively small amount, the Directors have decided to treat current policyholders in the same way as other creditors;

(b) although the Scheme is considered to be more beneficial to Scheme Creditors than the insolvent liquidation of MMI and should result in a quicker distribution with lower costs than in a liquidation, each Scheme Creditor must make up its own mind, and take whatever professional advice it considers appropriate, on whether the Scheme would operate to its benefit; and

(c) if there is a liquidation of MMI following termination of the Scheme, the normal order of the payment of claims in an insolvent liquidation is varied by the Scheme in order to ensure that, as far as possible, Scheme Creditors are treated equally. This is described in more detail on page 44 of this document. In summary, payments received by Scheme Creditors under the Scheme in respect of Established Scheme Liabilities (as defined in the Scheme) are to be treated as payments on account of dividends in the liquidation, so that Scheme Creditors who have received payment of their Established Scheme Liabilities subject to imposition of a percentage levy or have received the Payment Percentage of their Established Scheme Liabilities will not be entitled to any further dividend in the liquidation until all Scheme Creditors have received an equivalent percentage dividend on Scheme Liabilities.

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In considering whether to approve the Scheme, the likelihood of MMI being able to run-off its business without becoming insolvent should also be taken into account. If MMI were to remain solvent, then creditors which are or which consider that they might in the future become Scheme Creditors would not be at a disadvantage if the Scheme were not implemented. Nonetheless, the Directors consider it prudent that MMI should enter into the Scheme to secure the advantages described above against the possibility of MMI being placed into insolvent liquidation.

7. Material litigation

Details of all litigation which, to the knowledge of the Directors, is material in the context of the Scheme (except for litigation which has arisen in the normal course of MMI's business in respect of insurance or reinsurance contracts to which MMI is party) are set out in Appendix E.

8. Cork Gully letter

Cork Gully have been instructed to advise on where the balance of advantage lies for Scheme Creditors as between the Scheme and other alternative methods of dealing with the problems which might arise were MMI to become insolvent. They have written to the Company on certain financial aspects of the Scheme as compared to an insolvent liquidation. Their letter is set out as Appendix F. Cork Gully are of the opinion that the Scheme would be more beneficial for Scheme Creditors than an insolvent liquidation of MMI.

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C: SUMMARY OF THE SCHEME

The Scheme is set out on pages 105 to 151 of this document. The principal provisions of the Scheme are summarised below. This summary has been prepared to help you understand the Scheme. It should be ignored for the purpose of interpreting the Scheme, which qualifies this summary in its entirety.

1. Application of the Scheme

The Scheme will apply to each creditor of MMI which becomes a Scheme Creditor and in respect of all Scheme Liabilities to such Scheme Creditor, including all Scheme Liabilities which do not become Established Scheme Liabilities until after the Record Date of 30th September, 1993.

2. Scheme Liabilities

Scheme Liabilities are, subject to certain exclusions described below, liabilities of MMI under or arising out of any Insurance Contract to which MMI was subject on the Record Date or to which MMI has or may become subject after the Record Date by reason of an obligation assumed by MMI before the Record Date.

Scheme Liabilities include claims by direct policyholders, brokers, other insurance companies, assignees and other persons to whom rights under Insurance Contracts are or have been transferred. A Scheme Liability also includes interest which may be payable up to the Trigger Date (but not thereafter) on the amount owed by MMI.

Excluded from the definition of a Scheme Liability are liabilities:—

(a) in payment of which MMI had drawn a cheque on or before the Record Date;

(b) which would, on becoming Established Liabilities, be Protected Liabilities for the purposes of the Scheme;

(c) which (disregarding any assignment which has been effected on or after the Record Date) are, or would be (but for any such assignment), liabilities to Personal Creditors;

(d) which are discharged by way of commutation;

(e) which are PPB Liabilities (as described on page 37 below);

(f) under or arising out of an Insurance Contract written or issued by a branch of MMI in Australia or through an agency of MMI in New Zealand; or

(g) under or arising out of an Insurance Contract written or issued or renewed by MMI in favour of Motability Finance Limited.

An Insurance Contract is any treaty or contract of insurance or reinsurance of any kind whatsoever which was entered into by MMI as insurer or inward reinsurer on or before the Record Date or under which MMI assumed any obligation or liability on or before the Record Date.

As mentioned above, the Scheme does not apply to liabilities which are not Scheme Liabilities. Accordingly, liabilities which are not Scheme Liabilities will be payable in full by MMI both before and after any Trigger Event and in priority to payments in respect of Scheme Liabilities to Scheme Creditors.

The following are examples of liabilities which are not Scheme Liabilities:—

(a) costs, charges, expenses and disbursements incurred by MMI in connection with the negotiation, preparation and carrying out of the Scheme, including remuneration of the Scheme Administrator and Deputy Scheme Administrator (being liabilities not arising out of any Insurance Contract); and

(b) liabilities under or arising out of an Insurance Contract which are:—

  (i) liabilities to individuals to whom MMI has issued an insurance policy; or

  (ii) liabilities in respect of which (and to the extent to which) the PPB would owe a duty to secure payment under section 6, 7 or 8 of the Policyholders Protection Act if MMI were a company in liquidation ("Protected Liabilities")

3. Established Scheme Liabilities

A Scheme Liability will be an Established Scheme Liability for the purposes of the Scheme when there has been established (whether before, on or after the Record Date

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and whether by agreement or by any arbitration provided for under the terms of the Insurance Contract giving rise to the Liability or any judicial action or proceeding which is not the subject of any appeal) in relation thereto an obligation on the part of MMI to pay an ascertained sum of money.

The amount of an Established Scheme Liability will be the amount established by agreement, arbitration or judicial proceeding notwithstanding that any payment in respect thereof may have been made (or treated as having been made) since the Record Date. The amount will also take into account any Security Interest over the assets of MMI, any letter of credit or trust in favour of the creditor concerned, any effective right of set-off or cross-claim which might be relied on by the creditor if MMI were being wound up and any amount which has been recovered by MMI in respect of the Scheme Liability from a co-insurer or other third party.

Provision is made in the Scheme to the effect that in determining whether a creditor is a Scheme Creditor, no account shall be taken of any Assignment (as defined in the Scheme) effected on or after the Record Date of the whole or any part of any Scheme Liability.

Provision is made in the Scheme for cases where interests in Insurance Contracts are transferred on or after the Record Date pursuant to statute, statutory instrument or other legislation or delegated legislation. These provisions have been made in anticipation of the forthcoming local government reorganisation which will be likely to affect a number of Scheme Creditors.

4. The Scheme Periods

The Scheme Periods comprise two distinct periods of operation of the provisions of the Scheme: the Initial Scheme Period and the Levy Period.

The Initial Scheme Period will run from the date on which an office copy of the Order of the High Court of Justice of England and Wales sanctioning the Scheme is delivered to the Registrar of Companies in England for registration (the "Effective Date") until the occurrence of a Trigger Event. The Levy Period will run from the first date on which a Trigger Event occurs until termination of the Scheme.

During the Initial Scheme Period, all liabilities of MMI will be payable in the ordinary course of business as and when they fall due and the management and control of the business and affairs of MMI will, subject to certain restrictions described in paragraph 15 below, continue to be carried on by the Directors. The Scheme Administrator and the PPB will have certain limited rights as described further below.

During the Levy Period all liabilities of MMI other than Scheme Liabilities to Scheme Creditors will continue to be payable in the ordinary course of business as and when they fall due. The Scheme makes provision relating to the payment of Scheme Liabilities to Scheme Creditors during the Levy Period. The rights of Scheme Creditors in relation to Scheme Liabilities are modified by the Scheme and Scheme Creditors will be subject to the imposition of a Levy and the reduction in subsequent payments in respect of Scheme Liabilities as described further below.

After the occurrence of a Trigger Event, management and control of the business, affairs and assets of MMI pass to the Scheme Administrator, who is additionally given a number of specific powers during the Levy Period as described further below.

5. Operation of the Levy and application of the Payment Percentage

After the occurrence of a Trigger Event, a Levy may be imposed on all those Scheme Creditors which, at the date of imposition of the Levy, have been paid (or are treated as having been paid) since the Record Date an amount or amounts in respect of Established Scheme Liabilities and which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf since the Record Date, exceed £50,000 in aggregate. The Levy will only be imposed in respect of amounts paid (or treated as having been paid) since the Record Date to or on behalf of a Scheme Creditor in respect of Established Scheme Liabilities or Elective Defence Costs in excess of the first £50,000. No Levy will be imposed on any Scheme Creditor in respect of the first £50,000 so paid (or treated as having been so paid) to or on behalf of such Scheme Creditor.

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Additionally, after the imposition of any Levy, payments in respect of an Established Scheme Liability made to a Scheme Creditor to which (and including such payment) there has been paid (or there is treated as having been paid) an aggregate amount in excess of £50,000 since the Record Date in respect of Established Scheme Liabilities and Elective Defence Costs will be made at a reduced rate (the "Payment Percentage") to the extent that such payment when aggregated with other such payments since the Record Date exceeds £50,000.

The rate of the Payment Percentage prevailing from time to time will be equal to 100 minus the aggregate of the rate of Levy last imposed and all earlier Levies (if any), expressed as a percentage, subject, as described below, to the Scheme Administrator exercising his power to increase the Payment Percentage.

The rate of any Levy and the Payment Percentage will be such as the Scheme Administrator considers will ensure that, having made reserve for outstanding Established Scheme Liabilities and those Scheme Liabilities which the Scheme Administrator considers may become Established Scheme Liabilities (after taking into account the provision for the reduction in payment of Established Scheme Liabilities referred to above), MMI will have sufficient assets to meet in full all of its liabilities as and when they fall due other than:—

(a) Scheme Liabilities to Scheme Creditors and liabilities to the PPB;

(b) the liability for the repayment of amounts Levied;

(c) the liability to pay the balance of any Established Scheme Liabilities to which the Payment Percentage has been applied; and

(d) the liability to pay the Commission,

(all as further described below).

In considering whether MMI has sufficient assets, the Scheme Administrator will be entitled to take into account any monies which Scheme Creditors are liable to pay to MMI on the imposition of a Levy, all other assets of MMI (except those held on trust), including rights against reinsurers, and the prospect of future income.

For the purpose of determining the rate of Levy and/or the Payment Percentage, the Scheme Administrator must consider such financial and/or actuarial information and/or other information and advice as he considers appropriate, after consulting the Creditors' Committee.

No interest will be paid by MMI in respect of amounts Levied or in respect of amounts not paid to a Scheme Creditor by virtue of the Payment Percentage being applied to reduce the payment of Established Scheme Liabilities to such Scheme Creditor.

The Scheme Administrator may, after consulting the Creditors' Committee, suspend payments to Scheme Creditors in respect of Established Scheme Liabilities for such periods (not exceeding three months) as he considers necessary for him to decide whether or not to impose any Levy and to reduce the Payment Percentage or to increase the Payment Percentage.

If any Scheme Creditor fails to pay any amount of any Levy when due and payable, then interest will accrue on the amount of such Levy remaining outstanding as provided in the Scheme and, until such Levy has been paid in full, such Scheme Creditor will not be entitled under the Scheme to receive from MMI any payment in respect of any Scheme Liability.

6. Adjustments to the rate of Levy and the Payment Percentage

The Scheme Administrator is required to carry out a review of the assets and liabilities of MMI at least once in each year. In addition, if at any time after a Levy is first imposed the Scheme Administrator considers, having regard to the information available to him relating to the financial position of MMI, that the then prevailing Payment Percentage is at a level which is too low or too high to be in the best interests of Voting Creditors as a whole, the Scheme Administrator may carry out additional reviews of the assets and liabilities of MMI.

If, following any such review and after consulting the Creditors' Committee, the Scheme Administrator concludes that the prevailing Payment Percentage is at a level which is too

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high to be in the best interests of Voting Creditors, a further Levy will be imposed on all those Scheme Creditors which have by that time been paid (or are treated as having been paid) since the Record Date an amount or amounts in respect of Established Scheme Liabilities which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf since the Record Date, exceed £50,000 in aggregate.

If, however, following any review and after consulting the Creditors' Committee, the Scheme Administrator concludes that the then prevailing Payment Percentage is at a level which is too low to be in the best interests of Voting Creditors as a whole, he may increase the Payment Percentage. In the event of an increase in the Payment Percentage, MMI will, within 60 days after such increase, notify Scheme Creditors and the PPB of the increase and make a payment to such Scheme Creditors and the PPB designed to put them in the position they would have been in had the higher Payment Percentage rate been prevailing since the Trigger Date and, in the case of Scheme Creditors, any Levy had only been imposed at an equivalent lower rate. For example, if a Scheme Creditor has been paid £100,000 in respect of Established Scheme Liabilities, a Levy of 20 per cent. had originally been imposed on that Scheme Creditor (amounting to £10,000, being 20 per cent. of £100,000 - £50,000) but the Payment Percentage is subsequently increased from 80 per cent. to 90 per cent., then the Scheme Creditor will be repaid £5,000.

7. Payments at the end of the Levy Period

If, after all Scheme Liabilities have become Established Scheme Liabilities, payment in respect of all Established Scheme Liabilities due to Scheme Creditors has been made subject to imposition of a Levy or at a reduced rate in accordance with the Scheme and all of MMI's liabilities have been paid in full other than Scheme Liabilities due to Scheme Creditors and liabilities to the PPB ("PPB Liabilities"), MMI has any surplus assets then MMI will pay the balance of Established Scheme Liabilities to Scheme Creditors and the PPB Liabilities to the PPB. If MMI does not have sufficient surplus assets to pay in full all of the outstanding PPB Liabilities, the balance of Established Scheme Liabilities due to Scheme Creditors and the amounts levied on Scheme Creditors, then payment shall be made to the PPB and Scheme Creditors *pro rata* to the amounts respectively owed to them.

If there are any assets remaining after all liabilities under or arising out of an Insurance Contract have become Established Liabilities and MMI has paid in full all such Established Liabilities, all liabilities arising under the Scheme and all other liabilities of MMI then the Scheme Creditors and the PPB will be entitled to be paid a commission.

The Commission will also provide compensation for interest forgone under the Scheme which would have otherwise have been receivable by Scheme Creditors on a solvent liquidation of MMI. As described on page 122, the Scheme provides that no interest is payable as part of any Established Scheme Liability in respect of any period after the Trigger Date.

In order to calculate what would be a reasonable amount of Commission, the Directors instructed KPMG Actuarial Services to analyse the risk that the level of claims paid by MMI in the course of the run-off of its business might be larger than KPMG Actuarial Services' mid range estimate of the appropriate level of reserves. KPMG Actuarial Services has written to MMI with its advice and a copy of its letter forms part of Appendix D. The Directors asked the Company's reinsurance brokers, Durtnell & Fowler Ltd., a subsidiary of Willis Corroon Group plc, to investigate the availability and cost of reinsurance for this risk. Durtnell & Fowler Ltd. have advised that it is their opinion that the market is currently unwilling to provide reinsurance other than of a financial nature for this type of risk. A letter containing their advice is included in Appendix D. A financial reinsurance policy is designed to produce a quantified future payment from a given premium payment now. The Directors, with regard to the letter provided by KPMG Actuarial Services and noting the limitations listed therein, have decided that the 5 per cent. probability figure mentioned in the letter (which corresponds to approximately £70 million), represents an appropriate level of potential deterioration which might be borne by Scheme Creditors and the PPB. Accordingly, £70 million will be payable under the proposed Scheme in the form of commission to Scheme Creditors and the PPB.

The Commission will be payable to Scheme Creditors and to the PPB in proportion to the aggregate amounts of Established Scheme Liabilities and PPB Liabilities paid to each of

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them respectively since the Record Date. If MMI does not have sufficient surplus assets to pay the Commission in full then commission payments to each Scheme Creditor and the PPB will be reduced *pro rata*.

Any surplus assets remaining, after payment in full by MMI of all its liabilities and the Commission, will be distributed among the members of MMI in accordance with the Articles of Association.

8. Enforcement of Scheme Liabilities

Except as mentioned in paragraph 9 below and except to the extent that MMI has failed to perform any obligation under the provisions of the Scheme in respect of a Scheme Liability to a Scheme Creditor, Scheme Creditors are prohibited during the Levy Period from taking any step or proceeding against MMI or its property in any jurisdiction for the purpose of enforcing payment of any Scheme Liability.

If, notwithstanding the prohibition, a Scheme Creditor does take any such step or proceeding after the Trigger Date, it will be treated as having received, on account of the Scheme Liability due to it, an advance payment equal to the amount or gross value of any money, property, benefit or advantage obtained by it at the expense of MMI and its entitlement to payment under the Scheme will be reduced accordingly.

This bar on proceedings will not preclude any person from taking any appropriate action to determine the question whether MMI is liable in respect of any Scheme Liability and, if so, the amount of such Scheme Liability or otherwise enforcing the terms of the Scheme.

9. Security, Letters of Credit, Trusts and Set-offs

The Scheme does not affect the right of any Scheme Creditor to take any appropriate action to enforce:—

(a) any Security Interest over the assets of MMI which could have been enforced if MMI were being wound up and the Trigger Date was the date on which the order that MMI be wound up was made or which has been created after the Trigger Date to secure liabilities of MMI incurred after the Effective Date;

(b) any letter of credit or trust issued or created by or in respect of MMI of which such Scheme Creditor is a beneficiary, if such letter of credit or trust was issued or created before the Trigger Date or has been issued or created after the Trigger Date to replace an existing letter of credit or trust or to secure liabilities incurred by MMI after the Effective Date.

The Scheme does not affect the rights of MMI against any person in respect of any wrongful drawdown or enforcement of any letter of credit or trust issued or created by or in respect of MMI.

A Scheme Creditor which is under a liability to MMI may, in relation to MMI, rely on any set-off or cross-claim upon which it could have relied if MMI were being wound up and the order that MMI be wound up had been made on the Trigger Date.

No Scheme Liability which has been assigned to a person on or after the Trigger Date may be applied in extinguishing or reducing any liability of that person to MMI.

No liability of a Scheme Creditor to MMI which arises out of an obligation incurred by the Scheme Creditor on or after the Trigger Date may be extinguished or reduced by any Scheme Liability due to the Scheme Creditor concerned.

10. Election to Defend Decisions and Elective Defence Costs

Some of the policies written by MMI provide that MMI is not only liable to the policyholder for the full amount of the policyholder's loss covered by the policy but is also liable to indemnify the policyholder against the costs of defending third party claims against him. Under the Scheme, MMI is entitled to appoint a loss adjuster, consulting engineer, medical examiner, lawyer or other adviser to defend a claim made by a third party against a policyholder and to pay direct to such adviser the full cost of doing so, even where there is no obligation to do so. The Directors believe that this promotes greater efficiency in the run-off of MMI's business.

If such a decision is made, the total amount which MMI has paid out on behalf of a Scheme Creditor to the adviser is taken into account in calculating the amount payable to

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the Scheme Creditor under the Scheme, and will affect the amount received by the Scheme Creditor.

For example: suppose a Scheme Creditor which has already been paid more than £50,000 in respect of Established Scheme Liabilities has a further claim against MMI for £100 and the costs of investigating and defending the claim against the Scheme Creditor amounted to £40; the total liability owed by MMI to the Scheme Creditor equals the principal loss sustained under the policy (£100), together with the amount paid out on account of defence costs (£40), i.e., a total of £140.

(a) If a Trigger Event has occurred and a Levy of, say, 5 per cent. is imposed and subsequent payments to Scheme Creditors in respect of Established Scheme Liabilities are reduced to a Payment Percentage of 95 per cent., the Scheme Creditor's normal entitlement is 95 per cent. of £140 (i.e., £133). However, since MMI has already paid £40 directly to the adviser, the Scheme Creditor will only be entitled to retain or receive £93.

(b) If, however, (using the same figures of £100 and £40) the Levy is 75 per cent. and the Payment Percentage is 25 per cent., the Scheme Creditor's normal entitlement is 25 per cent. of £140 (i.e., £35). Since MMI has already paid £40 directly to the adviser on behalf of the Scheme Creditor, the Scheme Creditor would not be entitled to retain or receive any payment under the Scheme at this stage.

If, at a later date, the Payment Percentage is increased, the Scheme Creditor may be entitled to receive a payment under the Scheme, depending on the amount of the increase.

There are provisions in the Scheme enabling the Scheme Administrator to revoke an Election to Defend Decision.

11. Commutations and other arrangements

During the Levy Period, if the Scheme Administrator considers that it would be in the best interests of Voting Creditors, MMI may enter into Commutations (as defined in the Scheme) and other contractual arrangements (not being Insurance Contracts) with creditors under which all or a part of the total liability of MMI to the relevant creditor under an Insurance Contract becomes an Established Liability otherwise than as a result of an obligation to pay an ascertained sum of money being established in the normal course. Such Commutations and other arrangements are only permitted, however, if they are made on the basis that no other claim may be made in respect of the liability, or that part of the liability, which is the subject of the relevant Commutation or arrangement.

During the Levy Period, MMI may not, however, enter into such a Commutation or contractual arrangement unless the Scheme Administrator is satisfied that such Commutation or arrangement will reduce the net liabilities of MMI, the Commutation or arrangement will not adversely affect or prejudice MMI's rights under any relevant reinsurance contract and the PPB has consented in writing to the Commutation or arrangement (unless the creditor concerned has confirmed, in a legally binding form to the reasonable satisfaction of the PPB, that it is not a Protected Creditor in respect of the liability concerned or that it waives any rights which it may have against the PPB in respect of that liability and agrees to the discharge of the liability).

Cash Commutation payments made in full discharge of a liability of MMI will not be subject to any Levy or reduction under the Scheme. Equally, they cannot subsequently be increased and do not count towards a Scheme Creditor's entitlement to any Commission.

MMI may also enter into contractual arrangements during the Levy Period with any reinsurer for the full discharge of any such reinsurer's liabilities to MMI under reinsurance contracts in consideration for a cash payment to MMI if the Scheme Administrator considers that it would be in the best interests of Voting Creditors to do so.

The Scheme Administrator will consider any request made by a Scheme Creditor, supported by appropriate actuarial information, for MMI to enter into any such Commutations and contractual arrangements.

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12. Interest on Scheme Liabilities

Scheme Creditors will be entitled to receive payments in respect of interest as part of an Established Scheme Liability only where they are entitled to such interest by reason of contract, judgment against MMI, decree or otherwise for a period ending on or before the Trigger Date.

The Directors consider that it is in the best interests of Scheme Creditors that interest should not expressly accrue on Scheme Liabilities after the Trigger Date (or on amounts Levied by MMI or on the balance of Established Scheme Liabilities not paid by MMI by virtue of application of the Payment Percentage) since the calculation of such interest would be so administratively complex and costly that any advantage there might be to Scheme Creditors would be out-weighed. Furthermore, payment of interest might result only in the imposition of a greater or further Levy and reduction in payments. As described above, Scheme Creditors are entitled to receive Commission to recompense them for the risk of suffering a Levy or a reduction in payments and the loss of the time value of money as a consequence, although the amount of Commission payable is not calculated by reference to the length of time for which interest might otherwise have accrued.

13. Currency of payment

Any amount payable to a Scheme Creditor under the Scheme in respect of an Established Scheme Liability due to such Scheme Creditor will be paid in the currency in which such Established Scheme Liability was incurred (or, where the relevant Insurance Contract allows such Scheme Creditor to elect to make a claim in any other currency and any such election is duly made, that currency). The currency in which an Established Scheme Liability was incurred is not necessarily the currency in which the Scheme Creditor incurred a liability to a third party in respect of the Established Scheme Liability.

Any set-off or cross-claim expressed in a currency other than that of the relevant Established Scheme Liability will, in the absence of agreement otherwise between the Scheme Creditor and MMI, be converted into the currency of the relevant Established Scheme Liability at the rate of exchange specified in the Insurance Contract to which the Established Scheme Liability relates or, if no such rate is specified, a rate as specified in the Scheme on the date on which the Scheme Administrator accepts that the set-off or cross-claim is available to the Scheme Creditor or the set-off or cross-claim is otherwise determined.

14. Payments by the PPB

In order to assist those to whom any Protected Liability is due and who are eligible for protection in accordance with that definition and under section 16(9) of the Policyholders Protection Act ("Protected Creditors"), the PPB has agreed, pursuant to the discretionary powers conferred on the PPB by section 16, to be bound by the Scheme (subject to it becoming effective) and, if (but only if) a Trigger Event has occurred, to make certain payments to MMI (by way of reimbursement in respect of payments made by MMI in discharge of Protected Liabilities) in accordance with the terms of the Scheme.

When a claim against MMI by a Protected Creditor is established, MMI will pay the claim to the Protected Creditor in full (free of any Levy or Payment Percentage reduction). If a Trigger Event has occurred and it is determined that the Protected Creditor would have been entitled to a payment from the PPB in respect of that claim if MMI had gone into liquidation on the Trigger Date, the PPB will, subject to payment having been made by MMI to the Protected Creditor and provided that such payment was made after the Trigger Date, reimburse to MMI a certain percentage (the "Reimbursement Percentage") (depending broadly on whether the Protected Liability arose under a compulsory or a non-compulsory insurance contract) of MMI's payment. If the Reimbursement Percentage increases following the imposition of a further Levy, the PPB will make additional reimbursement to MMI in respect of Protected Liabilities discharged by MMI and for which (and to the extent to which) MMI has already received some reimbursement by that time. In all cases, reimbursement by the PPB will be in the currency of the payment by MMI.

A Protected Liability is an Established Liability of MMI in respect of which (and to the extent to which) the PPB would owe a duty under section 6, 7 or 8 of the Policyholders

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Protection Act if MMI were a "company in liquidation" and the Trigger Date were the "beginning of the liquidation", in each case within the meaning of the Policyholders Protection Act, and references in those sections to the amount of any liability were references to the amount as established in the case of an Established Liability.

In the case of payments in discharge of Protected Liabilities arising under compulsory insurance policies, the Reimbursement Percentage is equal to 100 minus the Payment Percentage and in the case of payments in discharge of Protected Liabilities arising under non-compulsory insurance policies, the Reimbursement Percentage is equal to 90 minus the Payment Percentage (or, if the Payment Percentage is greater than 90, zero).

Reimbursement by the PPB will be made as soon as reasonably practicable and, in any event, by no later than thirty days following whichever is the latest of the date on which the Scheme Administrator delivers certification to the PPB in accordance with the Scheme in respect of the payment for which MMI is seeking reimbursement, the date on which the PPB agrees or it is otherwise determined (so as to bind the PPB) that the liability concerned is a Protected Liability, the first Levy Notice Date or, if later, the date which is 30 days after the Trigger Date (or, in the case of additional reimbursement on an increase in the Reimbursement Percentage, the Levy Notice Date relating to the Levy giving rise to such an increase) and the date on which it appears to the PPB that it has adequate funds to make the reimbursement having regard both to its obligations under the Scheme and to its other responsibilities.

If, following receipt of certification in respect of payment of a Liability, the PPB does not agree that the Liability is a Protected Liability, then the PPB is required to notify the Scheme Administrator of the absence of such agreement as soon as reasonably practicable and, in any event, within 90 days of such delivery.

In making its determination as to whether any Established Liability is a Protected Liability for the purposes of the Scheme the PPB is obliged, so far as reasonably practicable, to interpret the definition of Protected Liability in a manner consistent, in all material respects, with that which it would adopt, in like circumstances, in determining whether any liability of a company in liquidation is one in respect of which the PPB would be under a duty to secure any payment under the Policyholders Protection Act. MMI and the Scheme Administrator are (both during the Initial Scheme Period and the Levy Period) prohibited from applying to the Court for a determination in relation to the interpretation or construction of any provision of the Policyholders Protection Act unless the PPB consents but this does not affect enforcement of the PPB's obligation to apply a consistent interpretation as described above.

Each such payment made by the PPB to MMI will give rise to a liability of the same amount, constituting a debt owed by MMI to the PPB (a "PPB Liability").

The reimbursement obligations of the PPB under the Scheme are subject to certain conditions, limitations, qualifications and other provisions which would have applied, or could have been imposed by the PPB, under the Policyholders Protection Act if MMI had been a company in liquidation. They are also conditional, unless the PPB consents, on there having occurred no unremedied breach by the Scheme Administrator of the terms of the Scheme which materially and adversely affects the interest of the PPB in the Scheme.

There is an overall limitation on the obligations of the PPB under the Scheme in respect of any creditor or liability of MMI by reference to the obligation which it would have had if MMI had been in liquidation, save for the PPB's obligation to make payment in the currency of the Established Liability.

The PPB will not have an obligation to make any reimbursement to MMI in respect of a payment which appears to the PPB would result in a material benefit being conferred on any person who was a member of MMI on the date on which the application is made to the Court to sanction the Scheme, in his capacity as such, or on a person who had any responsibility for, or who may have profited from, the circumstances giving rise to the financial difficulties of MMI. For this purpose, any benefit which might accrue to any such person who is a policyholder of MMI in his capacity as such will be disregarded.

The PPB will also not have an obligation to make any reimbursement in respect of liabilities of MMI to the extent to which they relate to any period of cover on or after the

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Trigger Date. This corresponds with the obligations which the PPB would have been under if MMI were a company in liquidation.

Immediately upon any reimbursement being made by the PPB to MMI there will automatically be assigned to the PPB all rights and claims which MMI may have in respect of the Protected Liability for which the PPB is making reimbursement, together with all rights and claims which MMI may have against any other persons in respect of any event giving rise to the Protected Liability. Any obligation of the PPB to reimburse MMI for payment of any Protected Liability will, if the PPB so elects, be conditional on there first being assigned to it such rights and claims as are referred to above.

As soon as reasonably practicable after discharge in full of any PPB Liability, the PPB shall re-assign (at MMI's cost and expense) to MMI all rights and claims (to the extent not already exercised or enforced) against the Protected Creditor the payment of whose Protected Liability gave rise to the PPB Liability.

The Scheme contains obligations on each of MMI and the Scheme Administrator to provide the PPB with certain information.

A memorandum containing a brief summary of certain provisions of the Policyholders Protection Act is contained in Appendix I.

15. Carrying on business

Under the Scheme, MMI is prohibited from carrying on any business, except in connection with and for the purpose of the carrying out of the Scheme (and all matters incidental thereto), and from entering into any further insurance or reinsurance contracts or renewing, replacing, extending or varying any existing Insurance Contract in a manner which would increase the total amount of any liability of MMI to any person under such contract. The prohibition does not, however, preclude MMI (with the Scheme Administrator's consent if a Trigger Event has occurred) from entering into, renewing, replacing, extending or varying contracts of insurance protecting MMI or its Directors, officers, employees or agents against usual business risks and contracts of reinsurance in relation to liabilities to which MMI is subject on the Effective Date.

For the purpose of carrying out the Scheme, MMI is also allowed to manage and (subject to certain restrictions) dispose of or develop property held by MMI at the Effective Date and, if the Scheme Administrator and the PPB have given their prior written consent, to have transferred to it liabilities under insurance and reinsurance contracts entered into by MGI and to create any trust over the transferred assets in connection with any such transfer.

MMI is also prohibited, subject to certain exceptions, from creating or causing or permitting to be created, any trust of or in relation to any asset of MMI or from appropriating or setting aside any asset to meet any of its liabilities except in accordance with the terms of the Scheme or in circumstances where such transaction is carried out in connection with the establishment of any escrow arrangement or the deferral of payment of consideration in connection with the disposal of any asset by MMI on arms' length commercial terms.

During the Initial Scheme Period, MMI is prohibited from disposing of any asset (or disposing by one transaction or a series of related transactions of a number of assets) recorded in its books as having a value in excess of £3,000,000 or from entering into any commutation under which MMI agrees to make a cash payment of more than £250,000 or from incurring expenditure of more than £500,000 on the development of any site unless MMI has first obtained from a licensed insolvency practitioner written advice that such disposal, commutation or development will not be prejudicial to the interests of its creditors as a whole.

Additionally, during the Levy Period, MMI may not arrange for the issue or creation of any new letters of credit, trusts, bonds or other instruments or security over any asset except in order to replace existing letters of credit or trusts or in order to secure liabilities incurred after the Effective Date or to provide security for the purpose of any litigation, arbitration or other proceedings in relation to any liabilities of MMI and provided that the Scheme Administrator considers that to do so would be in the best interests of Voting Creditors.

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At any time when the Scheme Administrator is not exercising general powers of management, MMI must promptly provide the Scheme Administrator and the PPB with all information in MMI's possession or under MMI's control or the control of its agents which the Scheme Administrator or the PPB may respectively request in order to satisfy himself or itself that the management of MMI is being prudently conducted.

16. The management of MMI

During the Initial Scheme Period, the day-to-day management of MMI will continue to be carried on by the Directors, subject to the restrictions mentioned above.

No Controller (as defined in the Scheme) may be appointed or removed during the Initial Scheme Period without the prior written consent of the PPB.

During the Levy Period, but not before, the Scheme Administrator will have general powers of management and control of the business, affairs and assets of MMI for the purpose of implementing, and in accordance with the terms of, the Scheme. As described further below, during the Levy Period the functions of the Scheme Administrator include the management of the run-off of MMI's business and the supervision and ensuring of the carrying out of the Scheme.

17. The Scheme Administrator

The Scheme Administrator must be an individual qualified to act as an insolvency practitioner in accordance with section 390 of the Insolvency Act 1986.

In exercising his powers and carrying out his duties under the Scheme, the Scheme Administrator must act *bona fide* and with due care and diligence in the interests of Voting Creditors as a whole.

The initial Scheme Administrator will be Gareth Hughes.

The Scheme Administrator may resign his appointment at any time by giving not less than six months' notice in writing to MMI and the Creditors' Committee. He may be called upon to resign by a resolution passed by at least three-fourths of all the members of the Creditors' Committee and, if he declines to do so, may be removed by a resolution passed by a majority in number representing at least three-fourths in value of the Voting Creditors present and voting either in person or by proxy at a meeting of Voting Creditors convened for the purpose.

Immediately after and, in any event, within 30 days after, the resignation of the Scheme Administrator or the office of Scheme Administrator being vacated for one of the reasons set out in the Scheme, the Creditors' Committee will be entitled to appoint another person, who is qualified to act in such capacity, to be Scheme Administrator.

If at any time the Scheme Administrator is unable to carry out his functions under the Scheme, then the Deputy Scheme Administrator shall have full power and authority under the Scheme to carry out such functions until such time as the Scheme Administrator is able to resume such functions. The provisions of the Scheme relating to the Scheme Administrator apply *mutatis mutandis* to the Deputy Scheme Administrator whilst he is carrying out such functions and certain provisions apply at all times whilst the Deputy Scheme Administrator holds office. The Deputy Scheme Administrator must at the time of his appointment and throughout his tenure of office be a licensed insolvency practitioner. The initial Deputy Scheme Administrator will be Nigel Hamilton.

The Scheme Administrator will ensure that there is in force such bond as would have had to be in force if MMI had been wound up in England and he had been appointed its liquidator.

During the Initial Scheme Period, the Scheme Administrator will be entitled to receive a report every six months from the Directors on the affairs of MMI, to convene meetings of the Directors for the purpose of obtaining information concerning the affairs of MMI and to receive certain other information.

Additionally, the Scheme Administrator will be entitled, after consultation with the Creditors' Committee, to exercise such powers as may be conferred upon him by the Articles of Association:—

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(a) both during the Initial Scheme Period and the Levy Period to exercise such voting or other rights as may be conferred upon him by MMI's Articles of Association in order to ensure compliance with the provisions of the Scheme relating to Directors (Part 9, except for Clause 9.1.4) or to defeat any resolution put to the members of MMI to wind up MMI voluntarily or to alter any provision of the Articles of Association containing any of the powers conferred on the Scheme Administrator as a special member of MMI or any provision of MMI's Memorandum of Association; and

(b) during the Levy Period:—

(i) to appoint any person who is willing to act as a director of MMI and remove any person as a director of MMI and to block any other such resolution put either by the Directors or other members of MMI; and

(ii) when directed to do so by a Creditors' Resolution of Scheme Creditors and the PPB, to pass a resolution to wind-up MMI voluntarily.

The Scheme Administrator must, by exercising his powers under MMI's Articles of Association, ensure that no amendment is made to MMI's Memorandum or Articles of Association which would, in the PPB's opinion, adversely affect the interest of the PPB in the Scheme unless authorised not to do so by a resolution of the Creditors' Committee in favour of which the PPB voted.

During the Initial Scheme Period, the Scheme Administrator must, unless (and only unless) authorised in writing by the PPB not to do so, exercise such powers as may be conferred on him by MMI's Articles of Association to ensure that no Controller of MMI (as defined in the Scheme) is appointed or removed without the PPB's consent.

It is intended that, before the Effective Date, the Articles of Association of the Company will be amended to give the Scheme Administrator the power necessary to exercise the rights described above. The proposal is that, under the Articles, the Scheme Administrator will be a special member of the Company with weighted voting rights sufficient to allow him to requisition general meetings of the members of the Company and to carry or, as the case may be, defeat any resolution relating to the business described above. If such amendment is not approved by the members of MMI then the Directors will not proceed with the Scheme as currently proposed.

During the Levy Period, the Scheme Administrator will also have the power:—

(a) to agree claims and process reinsurance recoveries as part of the run-off of MMI's business;

(b) to take possession of, collect, get in and hold all the property and assets of MMI and to do all such things as may be necessary for the realisation in due course of any such property or assets;

(c) to have full access at all times to all books, papers and other documents of MMI and to attend all Board meetings;

(d) to do all things which may be necessary or expedient for the protection of MMI's assets;

(e) to bring or defend any action or other legal proceedings in the name and on behalf of MMI or otherwise;

(f) to be remunerated and reimbursed his proper expenses;

(g) to employ and remunerate advisers or agents in connection with the conduct of his functions under the Scheme;

(h) to give directions to the Directors in relation to the exercise by them of their rights and powers in connection with MMI;

(i) to do all acts and to execute in the name and on behalf of MMI any deed, receipt or other document and to use MMI's seal;

(j) to borrow and to make any payment which is necessary or incidental to the performance of his functions and to give a valid discharge for amounts received by MMI;

(k) to delegate to any person qualified to act all or any of his powers and duties conferred under the Scheme;

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(l) to apply, or cause MMI to apply, to the Court for directions in relation to any particular matter arising in the cause of the Scheme; and

(m) to attend meetings of the Creditors' Committee.

In exercising his powers and carrying out his duties under the Scheme, the Scheme Administrator must consult with, and take account of the views expressed by, the Creditors' Committee on matters material to the Scheme, including the imposition of any Levy, any increase in the Payment Percentage and any appointment or removal of Directors.

During the Levy Period, any power conferred on MMI or its officers, whether by statute or by the Memorandum and Articles of Association, which could be exercised in such a way as to interfere with the exercise by the Scheme Administrator of his powers in relation to MMI as referred to above shall not be exercisable except with the consent of the Scheme Administrator, which may be given either generally or in relation to particular cases (provided this shall not relieve the Directors from their duty to act in accordance with the Companies Act 1985).

During the Levy Period, the Scheme Administrator must review the rate of Levy and the Payment Percentage at least once each year.

Within 90 days after the rate of Levy and the Payment Percentage have been set in any year or have been adjusted at any time, the Scheme Administrator must prepare a report on the affairs of MMI and the operation of the Scheme and send the report to each member of the Creditors' Committee and to each Director. The Scheme Administrator is not under a duty to provide a copy of the report to any Scheme Creditor unless specifically requested in writing to do so.

The fees and expenses of the Scheme Administrator are subject to the approval of the Creditors' Committee.

18. The Creditors' Committee

The Scheme provides for a Creditors' Committee to represent Scheme Creditors and the PPB and to monitor the implementation of the Scheme and supervise the Scheme Administrator in the performance of his functions under the Scheme.

The Creditors' Committee must consist of not less than four nor more than ten members of whom one will be the PPB and one will be a Scheme Creditor which is not a Local Authority. Any Scheme Creditor, the PPB or any other person with the written consent of the Scheme Administrator is eligible for appointment as a Committee Member.

The names of the initial Committee Members are set out in Clause 1.3.4 of the Scheme (page 114 of this document). This is subject in the case of each of the proposed initial Committee Members which is a local authority to it obtaining the necessary internal authorisation for it to become a Committee Member.

The Creditors' Committee may appoint any eligible person as a member, either to fill a vacancy or as an additional Committee Member, by a resolution passed by at least two-thirds of the Committee Members present. In appointing replacement or additional members, the Creditors' Committee must endeavour to ensure that the composition of the Creditors' Committee is such as to secure a proper balance of the interests of Scheme Creditors.

Scheme Creditors and the PPB may, by Creditors' Resolution, remove any Committee Member (other than the PPB) from office and so appoint any eligible person as a member, either to fill a vacancy or as an additional Committee Member.

The Creditors' Committee will be entitled by a resolution passed by at least three-quarters of all its members to call upon the Scheme Administrator to resign.

If the Scheme Administrator ceases to hold office for any reason, or if he is removed by the Voting Creditors, the Creditors' Committee may, by a simple majority of its members present and voting at the relevant meeting, appoint any person to be the Scheme Administrator in his place.

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Each Committee Member (other than the PPB) which is a body corporate or a joint authority, board or committee or a partnership may appoint a senior executive or officer (or, in the case of partnerships, a partner) as its Nominated Representative to represent it at meetings of the Creditors' Committee. The PPB may also appoint a PPB Representative and an alternate for the PPB Representative.

The Creditors' Committee must meet at least once in each year (commencing in 1994) for the purpose of receiving a report from the Scheme Administrator on the affairs of MMI and operation of the Scheme, and at such other times as seem desirable for the purpose of the Creditors' Committee performing its functions under the Scheme. The Creditors' Committee will elect one of its number as Chairman. MMI will pay all the reasonable costs of summoning meetings of the Creditors' Committee and the reasonable out-of-pocket expenses of the members of the Creditors' Committee in attending meetings of Voting Creditors.

The Creditors' Committee may require the Scheme Administrator to provide it with information concerning the affairs of MMI and the operation of the Scheme but the Scheme Administrator is not obliged to disclose any information the release of which he determines would be detrimental to the interests of MMI and Voting Creditors as a whole. If, however, the Scheme Administrator refuses to provide such information, he must give the reasons for his decision to the Chairman of the Creditors' Committee.

Each member of the Creditors' Committee must, in performing his functions as such, act *bona fide* in the best interests of the Voting Creditors as a whole.

Each Committee Member must use its best endeavours to avoid conflicts of interest in performing its duties under the Scheme. Each Committee Member must, and must procure that its representatives, officers and employees shall, preserve the confidentiality of information concerning MMI and the operation of the Scheme and use such information only for the purpose of performing their responsibilities and functions under the Scheme unless they have obtained the prior written approval of the Scheme Administrator.

19. Responsibility of the Scheme Administrator and others

The Scheme provides that acts done or omitted to be done in good faith and with reasonable care by the Scheme Administrator, the Deputy Scheme Administrator, any Director of MMI, any member of the Creditors' Committee (or any Nominated Representative or, in the case of the PPB, PPB Representative or PPB Alternate, all as defined in the Scheme) or any Voting Creditor in accordance with, and to implement, the provisions of the Scheme and the exercise in good faith and with reasonable care of their powers under the Scheme, may not be challenged by any Voting Creditor. Subject to the Companies Act 1985, no such person shall be liable for any loss, unless such loss is attributable to his own negligence, default, breach of duty, breach of trust, fraud or dishonesty (or, in the case of the Scheme Administrator and Deputy Scheme Administrator, to that of any partner, employee or delegate of the Scheme Administrator or Deputy Scheme Administrator).

MMI will indemnify such persons (other than Voting Creditors) against liabilities incurred by them in defending proceedings brought against them relating to their respective responsibilities under the Scheme in which they are found not to be liable.

20. Meetings of Voting Creditors

The Scheme provides for meetings of Scheme Creditors and the PPB (together "Voting Creditors") to be held. Meetings shall be held when convened by the Scheme Administrator whenever and for whatever purpose he thinks fit or when he is requested to do so in writing by either (a) not less than seventy Voting Creditors or (b) any Voting Creditor, or Voting Creditors which represent the requisite value. Voting Creditors will represent the requisite value if the aggregate of Scheme Liabilities due to them and, in the case of the PPB, the aggregate amount of PPB Liabilities either outstanding from, or paid by, MMI to the PPB, exceed £80 million.

The voting procedure provides that each Scheme Creditor shall have one vote for every pound Sterling of its Scheme Liabilities which, if established, will be the amount agreed

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or settled with MMI or, if not established, the amount estimated by the Scheme Creditor, subject to a determination (for the purposes only of voting) by the Scheme Administrator.

As described above, during the Levy Period PPB Liabilities may become due from MMI to the PPB. In the same way as Scheme Creditors are given the right to vote at meetings of Voting Creditors, the Scheme provides for votes to be conferred on the PPB so as to allow the PPB to participate in the operation of the Scheme and have a share of control over how the Scheme is implemented. The PPB will have one vote for every pound Sterling of PPB Liabilities outstanding from, or paid by, MMI to the PPB at the relevant time and shall be counted as a separate Voting Creditor in respect of each PPB Liability on any vote to remove the Scheme Administrator or Deputy Scheme Administrator or to appoint anyone with the appropriate qualifications in his place.

All Scheme Liabilities and PPB Liabilities denominated in currencies other than Sterling will be converted into Sterling at the average of the rates respectively quoted by National Westminster Bank Plc for the purchase and the sale of Sterling with or for the relevant currency at or around 11.00 a.m. on the day specified in the Scheme.

If a Scheme Creditor disputes the value which has been put on its Scheme Liabilities for the purpose of requesting a meeting of Voting Creditors, the dispute will be referred to the President of the Society of Practitioners in Insolvency or such other individual or individuals qualified to act as an insolvency practitioner as he may nominate. The decision of the President or such other person will be final (but only as regards the convening of a meeting on the relevant occasion).

If a Voting Creditor disputes the amount for which its votes should be counted, the question will be referred to the Chairman of the relevant meeting of Voting Creditors, whose decision will be final (but only as regards the vote on that occasion).

The Scheme Administrator will be the Chairman of all Voting Creditors' meetings except if a resolution is proposed which directly concerns him. In that case, the Chairman of the Creditors' Committee will preside.

No business will be transacted at a meeting of Voting Creditors unless a quorum is present when the meeting commences. The quorum is 20 Voting Creditors present in person or by proxy and having the right to vote at the meeting. All resolutions put to the vote at such meeting will be decided on a poll rather than on a show of hands. The PPB will count as a separate Voting Creditor in relation to each separate PPB Liability.

A resolution may only be passed at a meeting of Voting Creditors if it is passed by a majority in number representing three-fourths in value of Voting Creditors which, being entitled so to do, are present and vote in person or by proxy at that meeting.

The Voting Creditors have the power to pass a resolution to remove from office the Scheme Administrator, the Deputy Scheme Administrator or a member of the Creditors' Committee (other than the PPB) and to appoint another person in his or its place and also to terminate the Scheme.

21. Duration of the Scheme

It is anticipated that the Scheme may continue for at least twenty years since claims under most insurance contracts written by MMI (for example, public liability and employers' liability contracts) may be made at any time (and, indeed, in the case of "long tail" business, may be made many years after the occurrence of the events giving rise to the claim), provided the loss giving rise to the claim occurred or is deemed to have occurred during the policy period. By way of illustration, of the employers' liability claims made during the six months to 30th June, 1993 more than 18 per cent. by number arose from occurrences which took place before 1985. Further, owing to their complexity, claims may also take many years to settle even after they have been made.

Because the Directors are not able to determine when all claims will have been made and settled it is not, therefore, possible to set a termination date for the Scheme.

However, the Scheme will be terminated if:—

(a) all of the Liabilities of MMI have been discharged in full;

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(b) MMI is ordered to be wound up by the Court;

(c) a voluntary winding-up of MMI is commenced under the Insolvency Act 1986;

(d) a receiver is appointed by the Court in relation to MMI's business and assets;

(e) a Creditors' Resolution that the Scheme shall be terminated and MMI wound up is passed at a meeting of the Voting Creditors; or

(f) the Scheme Administrator, with the agreement of the Directors and the Creditors' Committee, gives notice in writing to MMI that, after due enquiry, he has concluded that the Scheme is no longer in the interests of the general body of Voting Creditors.

In the event of the termination of the Scheme and a liquidation of MMI, the normal order of the payment of claims in an insolvent liquidation is varied by the provisions of the Scheme. The assets of MMI will be applied in discharge of:-

(a) first, all liabilities of MMI to which preference would be given in the winding-up of MMI by virtue of the Insolvency Act 1986;

(b) second, all liabilities of MMI, other than Scheme Liabilities due to Scheme Creditors and PPB Liabilities, which are proved in the winding-up of MMI; and

(c) third, all Scheme Liabilities due to Scheme Creditors and PPB Liabilities

and to the extent that any such liabilities are in excess of the amount of MMI's assets, they will be paid in the order set out above and rateably within each category.

Upon liquidation, the balance of Established Scheme Liabilities (and claims treated as being Established Scheme Liabilities) either unpaid to Scheme Creditors (by virtue of the application of the Payment Percentage in reducing the payments or otherwise) or paid but subsequently repaid following imposition of a Levy will become payable immediately. All payments already received by Scheme Creditors in respect of Established Scheme Liabilities or made on their behalf in respect of Elective Defence Costs will be treated as payments on account of a dividend in the winding-up; those Scheme Creditors will not be entitled to any further dividend in the winding-up until all Scheme Creditors proving in the winding-up have received an equivalent percentage dividend. Thereafter and subject thereto, a Scheme Creditor will be entitled to share in the assets of MMI *pari passu* with other Scheme Creditors and the PPB until paid in full. The purpose of these provisions is to ensure that, as far as possible, all Scheme Creditors are treated equally.

22. Dealings with brokers

MMI is aware that some brokers may have funded their clients' claims against MMI, sometimes without their clients' knowledge. The Directors have been advised that brokers who have funded their clients' claims do not thereby become creditors of MMI in respect of funded claims unless they have received an assignment from their clients in respect of the claims funded. It follows that those policyholders whose brokers have funded some or all of their claims (other than on the basis of an assignment of claims to the brokers) remain creditors of MMI in respect of those claims and, depending on the value of their claims (and other claims they might potentially make in the future), will be entitled to vote at the Court Meeting and will rank as Scheme Creditors and receive payments under the Scheme accordingly.

Insofar as brokers have effected a set-off in account with MMI where there was no legal right to do so or have recovered but not paid to MMI monies properly so payable, so that there are sums due to MMI from brokers, these sums will be claimed by MMI.

23. Taxation

If Scheme Creditors have any doubts as to the tax treatment of payments received under the Scheme, they should seek appropriate advice from their professional advisers.

Every Scheme Creditor who receives this document is strongly advised to consult their professional adviser as to their own tax position.

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1. The Court Meeting

Before the Scheme can become effective and binding, a resolution to approve the Scheme must be passed at the Court Meeting by the Scheme Creditors. The resolution to approve the Scheme must be passed by the requisite majority provided by section 425 of the Companies Act 1985. The requisite majority is a majority in number representing three-fourths in value of those Scheme Creditors who, being so entitled, are present and vote at the Court Meeting in person or by proxy. You will find, on pages 153 and 154 of this document, a notice convening the Court Meeting.

2. Valuation of claims for voting purposes

In order to determine whether the requisite majority for voting purposes has been reached, MMI must be notified of the value of each Scheme Creditor's insurance claim or claims (both actual and potential). Claims in respect of which the PPB would be under a duty to secure payment to you under the Policyholders Protection Act if MMI were in liquidation will not be counted.

For voting purposes, each Scheme Creditor's actual and potential future insurance claims against MMI will be counted by deducting from the estimated amount of each such claim the estimated amount of any known right of set-off or cross-claim, the estimated value of any known Security Interest, letter of credit or trust in the Scheme Creditor's favour and any amount expected to be recovered by MMI in respect of the Scheme Liability directly or indirectly from a co-insurer or other third party (except any reinsurer).

Please notify MMI of your claim(s) for voting purposes by using the Claims Table on the enclosed Voting and Proxy Form and, if you wish to appoint a proxy, please use the Form of Proxy. The Claims Table asks you to estimate the value of your present insurance claim(s) and potential future insurance claim(s) against MMI. This will include, amongst others, claims which have been agreed and those not yet agreed. You will need to provide particulars of any estimated claims and will need to include details regarding the basis upon which the figure has been estimated. The Chairman of the Court Meeting will verify these claims against MMI's records and will determine whether or not these estimates of the value of such claims are fair and reasonable before they are counted for voting purposes. **These estimates (whether by Scheme Creditors or the Chairman of the Court Meeting) will not be relevant, and will not bind MMI or the PPB, for the purpose of calculating payments under the Scheme; they are for voting purposes only.** To the extent that it is practicable, rejections or reductions of claims for voting purposes will be notified to you before or at the Court Meeting but in all cases you will be notified of any rejection or reduction of your claim(s) against MMI by not less than five business days before the date of the Court hearing.

Even if you are currently in dispute with MMI about your claim(s), you will still be eligible to vote at the Court Meeting. Acceptance by MMI of a Scheme Creditor's estimate of his claim(s) for voting purposes will not affect or prejudice MMI's right to dispute the claim for any other purpose.

3. Currency conversion for voting purposes

Claims against MMI may be denominated in various currencies. In order to determine whether or not the requisite majority (as to the value of the claims of Scheme Creditors voting in favour of the Scheme) has been achieved, the value of any non-Sterling insurance claim(s) of Scheme Creditors who are present and vote at the Court Meeting in person or by proxy on the Scheme will be converted into Sterling. If your claim(s) against MMI is(are) in a currency other than Sterling you will need to calculate the value of your claim(s) in Sterling by using the currency conversion rates printed on the Voting and Proxy Form. These rates will not be relevant for the purpose of calculating payments under the Scheme; they are for voting purposes only. The rate for each currency is the average of the rates respectively quoted by National Westminster Bank Plc for the purchase and the sale of Sterling with or for that currency at or around 11.00 a.m. on 8th November, 1993, being the latest practicable day before the printing of this document.

The value of any non-Sterling Security Interest, right of set-off or cross-claim or letter of credit or trust will also be converted into Sterling using the same currency conversion rates.

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4. Appointing a proxy

If you are a Scheme Creditor for the purposes of the Court Meeting, you are entitled to attend and vote at the Court Meeting either in person or by proxy (i.e., a person nominated to attend the Court Meeting and vote on your behalf). If you are a Scheme Creditor which is a corporation you may vote in person by a representative duly authorised by your governing body. If you wish to appoint a proxy please complete the Form of Proxy on page 2 of the enclosed Voting and Proxy Form in accordance with the instructions printed thereon. These should be carefully followed since the proxy may otherwise be invalid and be rejected. Completion and return of the Form of Proxy will not prevent Scheme Creditors from attending and voting in person at the Court Meeting.

5. Returning the Voting and Proxy Form

The Voting and Proxy Form should be returned to The Company Secretary, Municipal Mutual Insurance Limited, 22 Old Queen Street, Westminster, London SW1H 9HW. For your convenience, a pre-addressed and pre-paid envelope is enclosed with this document. Voting and Proxy Forms may be submitted at any time before or at the start of the Court Meeting. However, it would be greatly appreciated and will help to avoid delay and inconvenience at the Court Meeting if you could return it as soon as possible and in advance of the Court Meeting. A faxed copy of a Voting and Proxy Form will be accepted subject to receipt of the original by post or by personal delivery either prior to or at the Court Meeting.

In order to vote and have your vote counted you must complete the Claims Table of estimated Scheme Liabilities due to you which are, or which you consider might in the future become, Established Scheme Liabilities on page 3 of the Voting and Proxy Form. If you wish to appoint a proxy, the Form of Proxy on the Voting and Proxy Form must be completed. The Voting and Proxy Form must be returned to the Company before the vote is taken at the Court Meeting, whether or not you wish to appoint a proxy. Claims in respect of which the PPB would be under a duty to secure payment to you under the Policyholders Protection Act if MMI were in liquidation do not count for voting purposes and so must not be added to the value of any Scheme Liabilities before entering a figure in the Claims Table and Box 1 on the Form of Proxy.

In order to avoid delay at the Court Meeting and to the subsequent determination as to whether the requisite majority has been obtained, you are strongly recommended to return the Voting and Proxy Form to the Company as soon as possible and, preferably, by 2.00 p.m. on 31st December, 1993 but, if you do not do so, you may hand it to the Chairman of the Court Meeting before the start of the Court Meeting or when called to do so at the Court Meeting before the vote is taken.

6. After the Court Meeting

After the Court Meeting the votes must be checked and verified. This process is expected to have been completed within two days after the Court Meeting.

7. Sanction by the Court

In order for the Scheme to become operative and binding, the Court must sanction the Scheme after it has been approved by the requisite majority of Scheme Creditors at the Court Meeting. An office copy of the Court Order will be delivered to the Registrar of Companies for registration. Once an office copy of the Court Order is delivered, the Scheme will become effective. Notification to this effect will appear in the following newspapers and publications: the *Financial Times*, *Lloyd's List*, *Public Finance*, *Local Government Chronicle*, *Municipal Journal* and *Housing Association Weekly*. The Scheme will be binding on all those who become (or who are deemed to have become) Scheme Creditors, including those who may have voted against the Scheme or who did not vote.

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8. Effective Date of the Scheme

It is anticipated that, if the Scheme is sanctioned by the Court, it will become effective by 21st January, 1994. A long-stop date for the Scheme to become effective, of 30th April, 1994 (or such later date as the Court may allow), has been fixed.

9. Creditors' Committee

It is proposed that the Creditors' Committee will, subject to the necessary internal authorisations being obtained, initially consist of the members listed in Clause 1.3.4 of the Scheme (page 114 of this document). Eight of the initial members of the Creditors' Committee are local authorities. The ninth member is the PPB and the tenth member (which, under the Scheme, must not be a local authority) is the National Federation of Housing Associations.

10. Interests of the Directors

All of the Current Directors are members of MMI except Illtyd Harrington. None of the Directors is a creditor of MMI. If the Scheme is sanctioned by the Court, except as disclosed on pages 24 and 25 (Management and employees), it is envisaged that the Current Directors will continue in office. The Directors are entitled under the Scheme to an indemnity out of the assets of MMI against any liability incurred by them in defending successfully any proceedings brought against them in relation to their respective responsibilities under the Scheme. Save as aforesaid, the effect of the Scheme on the interests of the Directors will not differ from its effect on the like interests of others.

11. Interests of Coopers & Lybrand/Cork Gully

Coopers & Lybrand act as auditors to MMI and its associated and subsidiary companies and, in addition, provide other services and advice to the MMI Group (including, but not limited to, tax and actuarial advice).

Cork Gully, the insolvency practice of Coopers & Lybrand, have advised, and continue to advise, MMI on matters relating to MMI's solvency, including in relation to the Scheme.

From time to time, Coopers & Lybrand/Cork Gully will be a creditor of MMI to the extent of any unpaid fees due to them.

12. Interests of the members of the Sounding Board

None of the individual members of the Sounding Board is a member or creditor of MMI.

The members of the Sounding Board acted in their personal capacity and not on behalf of their employers (which, or members of which, are or may become Scheme Creditors) or as representatives of local authorities generally.

13. Inspection of documents

The documents or copy documents listed in Appendix H on page 100 will be available for inspection by creditors and members of MMI after the date hereof until the close of the Court Meeting at the following location during ordinary business hours on business days (excluding Saturdays and public holidays):—

Slaughter and May,
35 Basinghall Street,
London EC2V 5DB

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APPENDICES

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APPENDIX A

Curricula Vitae of the initial Scheme Administrator, the initial Deputy Scheme Administrator and the Current Directors

The initial Scheme Administrator

Gareth Howard Hughes

Gareth Hughes has been a partner in Ernst & Young since 1988.

Gareth Hughes has specialised in insolvency and corporate recovery since 1981. During that time he has acted as investigating accountant, receiver or liquidator to numerous companies with particular reference to the financial services and insurance sectors.

He was seconded to Bermuda in 1988 and 1989 to work full time on the liquidation of Mentor Insurance Limited, which agreed a scheme of arrangement with its creditors in February 1993. Since returning to the UK in early 1990 he has been involved in advising and/or appointed to approximately one hundred companies in England and Wales.

He has during this time advised a number of insurance and reinsurance companies in financial difficulties. His formal appointments in the insurance sector include Scan Re Insurance Company Limited, which is promoting a scheme of arrangement with its creditors, in addition to two of the insurance companies known as "KWELM", which have recently circulated details of a scheme of arrangement to creditors.

Gareth Hughes is a fellow of the Institute of Chartered Accountants in England and Wales and a licensed insolvency practitioner.

The initial Deputy Scheme Administrator

Nigel James Hamilton

Nigel Hamilton was made a partner in a predecessor firm of Ernst & Young in 1975.

He is partner in charge of the National Insolvency and Recovery practice of Ernst & Young and has been involved in all types of formal insolvency appointments advising on corporate recovery and reconstruction and carrying out viability investigations. His insurance appointments include Mentor Insurance Limited and Scan Re Insurance Company Limited.

He is a Council member and past President of the Society of Practitioners of Insolvency and Chairman of the Insolvency Practitioners Committee of, and a member of, the Council of the Institute of Chartered Accountants in England and Wales.

Nigel Hamilton is a fellow of the Institute of Chartered Accountants in England and Wales and a licensed insolvency practitioner.

The Current Directors

Mr. John P. Barber

Aged 45. Joined the Company as Deputy Chief Executive and appointed to the Board on 3rd November, 1993. Formerly Managing Director of Royal Reinsurance having held various positions with the Royal Insurance Group in the last 24 years. A member of the Council of London Insurance and Reinsurance Market Association (LIRMA) since 1992. Chairman of the ABI Reinsurance Committee since October 1992 and a member of the Management Committee of the General Insurance Council since September 1992. Fellow of the Chartered Insurance Institute 1972.

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Mr. Allan C. D. Castle

Aged 47. Appointed to the Board on 1st November, 1993 as Group Finance Director, having joined the Company in May 1990 as Group Financial Controller. Former Finance Director and Company Secretary of Laser Scan Holdings plc, formerly Financial Controller of a substantial privately owned business in Hong Kong and Assistant Group Treasurer of P&O. Qualified as a Chartered Accountant in 1969.

Mr. Stuart G. Errington

Aged 64. Appointed to the Board in April 1989. Formerly Chairman and Chief Executive of Mercantile Credit Group and of the Finance Houses Association from 1982 to 1984 and the Equipment Leasing Association from 1976 to 1978. A Director of Barclays Merchant Bank Limited and Barclays Bank UK Limited from 1979 to 1986. Currently a director of Kleinwort Overseas Investment Trust PLC, Nationwide Building Society, Northern Electric plc and Chairman of the National Association of Citizens Advice Bureaux.

Mr. Philip P. C. Gregory

Aged 38. Joined the Company and appointed to the Board in November 1989 as Group Finance Director. Appointed Group Chief Executive on 31st May, 1993. Former Group Finance Director of Sema Group Plc and formerly Senior Manager, KPMG Peat Marwick. Qualified as a Chartered Accountant in 1979.

Mr. Illtyd Harrington

Aged 62. Appointed to the Board in April 1985. Former Chairman of the Greater London Council. From 1973 to 1977 he was Chairman of the Greater London Council's Policy and Resources Committee. Former Councillor with Paddington Borough Council and Westminster City Council. Deputy Lieutenant of London. Justice of the Peace for 26 years.

Sir Peter Harrop

Aged 67. Appointed to the Board in March 1988. He was Second Permanent Secretary at the Department of the Environment until his retirement in March 1986. A director of Thames Water Plc and former director of National Home Loans Plc. A former Chairman of the National Bus Company and a Trustee of the British Museum.

The Rt. Hon. the Lord Merlyn-Rees

Aged 72. Appointed to the Board in December 1990. Life Peer. Former Secretary of State for Northern Ireland, Home Secretary, Parliamentary Secretary for the Army and the Royal Air Force and Member of Parliament for South Leeds.

Sir John Lovill

Aged 64. Appointed to the Board in March 1988. Former Chairman of the Association of County Councils. Councillor for East Sussex County Council from 1967 to 1989 and Leader from 1973 to 1977. Chairman of Sussex Police Authority from 1976 to 1979. Chairman of Nationwide Small Business Property Trust. A director of a number of private companies.

Sir David Montgomery

Aged 62. Appointed to the Board in April 1980. He was Vice-Convenor of Tayside Regional Council until his appointment in 1979 as Chairman of the Forestry Commission, a position he held until 1989. Chairman of the Finance Committee for the Tayside Regional Council from 1974 to 1979. Vice-President Convention of Scottish Local Authorities from 1978 to 1979.

Mr. John L. Morgan

Aged 74. Appointed to the Board in July 1986. Former Chairman of the Association of District Councils. Councillor with Test Valley Borough Council. Former Chairman of the European Affairs Committee of the International Union of Local Authorities. Past President of the Standing Conference of Local and Regional Authorities of Europe.

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Mr. Joe Small

Aged 64. Appointed to the Board in January 1989. A Solicitor of the Supreme Court. Recently retired as a senior partner in a city firm of solicitors where he served for many years and continues to act as a consultant.

Mr. Maurice F. Stonefrost

Aged 66. Appointed to the Board in April 1987. Former Director General and Clerk to the Greater London Council and President of the Chartered Institute of Public Finance and Accountancy. Former Chief Executive of British Rail Pension Trustee Company. Currently Deputy Pro-Vice Chancellor to the City University, member of the Committee reviewing the finances of the Church Commissioners and Executive member of the Architectural Heritage Fund.

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APPENDIX B

Audited accounts for the year ended 31st December, 1992

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* Page references are to pages of this document

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APPENDIX C

Legal opinions on whether participation in the Scheme will be *ultra vires* local authorities

Opinion of Mr. D. M. Barnes Q.C.

"IN THE MATTER OF: MUNICIPAL MUTUAL INSURANCE LIMITED

ADVICE

1. I am asked to advise generally on the capacity of local authorities to enter into a scheme of arrangement under s. 425 of the Companies Act 1985 as creditors of Municipal Mutual Insurance Limited ("MMI") and, in particular:—

(a) as to whether the obligations which would be assumed by local authorities as Scheme Creditors pursuant to the scheme of arrangement to which this opinion will appear as an Appendix (the "Scheme") would constitute a guarantee;

(b) as to whether the participation of local authorities in the Scheme and their obligations (including their potential future obligations) thereunder (including the imposition of a levy and subsequent reduction in payment of insurance claims) will be intra vires; and

(c) as to whether the answers to (a) and (b) above would be different if the Policyholders Protection Board were not to agree to be bound by the Scheme as provided therein.

The essential background facts are as follows.

2. MMI was founded as a company limited by guarantee in 1903. It ceased to write new or renewal insurance policies in September 1992. It has long catered for the insurance needs of local authorities, although a significant portion of its business was carried on with other public and private sector commercial organisations. The nature of the proposed scheme is that it will cover certain categories of creditors. Those covered will be organisations with a claim arising out of an insurance contract with MMI where either the claim subsisted on the 30th September 1993 or will be made after that date. Persons will not be covered unless their claims or potential claims amount to £50,000 or more and £25,000 or more of claims were shown on the Company's records to be outstanding as at 30th September 1993 (the Record Date of the Scheme). Policyholders who are individuals, partnerships or unincorporated associations of persons who are all individuals will not be covered. I have been given certain details of commercial claims reported as at the 31st December 1992. A total of 1,921 creditors were involved of which 694 (or 36%) had aggregate claims of £50,000 or more and 1,227 (or 64%) had aggregate claims of less than £50,000. Of those in the former category 95% in value came from local authorities and 5% from other public and private sector commercial creditors.

3. Once in force the scheme will permit MMI to meet claims in full in the ordinary way until a "trigger event" occurs such as the Directors determining that there is no reasonable prospect of MMI avoiding going into insolvent liquidation. Following a trigger event two matters will occur. First, payments to scheme creditors in respect of agreed claims in aggregate totalling over £50,000 will be reduced by an appropriate percentage to the extent that they exceed £50,000. Secondly, a levy at the same percentage will be made on the amount of such claims already paid — i.e. a part will be returned to MMI. The rate of the reduction and levy will be such as appears necessary for MMI to remain solvent. Policyholders who are outside the scheme will have their claims paid in full and will not be subject to the levy. The rate of reduction and levy will be reviewed at regular intervals. If possible, in due course and depending on the financial position of MMI, creditors within the scheme will be paid a part or the whole of the amounts foregone by them as a result of the reduction or the levy.

4. The major advantage of the scheme to all participants is that it will avoid the expenses and delay which are often attendant upon an insolvent liquidation of a company. It will enable claims to be largely paid subject to a reduction in what is considered an ordered and equitable manner. Under s. 425 of the Companies Act 1985 the scheme will bind all creditors of the class covered by its provisions provided at least 75% of the creditors by value and a majority in number agree to it and it is sanctioned by the Court.

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5. Local authorities are creatures of statute with the result that their power to carry out any form of activity must be founded on some form of statutory authorisation. Various Acts of Parliament contain a wide gamut of powers applicable to local authorities. It is curious that there are few specific powers to enter into contracts of insurance. I say it is curious because many of the activities of authorities are in spheres where insurance is a usual aspect of the activities, for example the holding of property. Any prudent property owner would consider some form of insurance of the property held. There are exceptions. For example, as my instructions point out, s. 140 of the Local Government Act 1972, as substituted by the Local Government (Miscellaneous Provisions) Act 1982, empowers local authorities to enter into contracts of insurance against the risk of a member of the authority meeting with a personal accident while engaged on the business of the authority.

6. It would be absurd if local authorities had no general power to insure their physical assets or to insure against their liabilities. In my opinion that power does exist and derives from the power given by s. 111 of the Local Government Act 1972 to enter into subsidiary transactions. Section 111(1) provides:

> **"(1) Without prejudice to any powers exercisable apart from this section but subject to the provisions of this Act and any other enactment passed before or after this Act, a local authority shall have power to do anything (whether or not involving the expenditure, borrowing or lending of money or the acquisition or disposal of any property or rights) which is calculated to facilitate, or is conducive or incidental to, the discharge of any of their functions."**

In this context the word "functions" embraces all the duties and powers of a local authority: Hazell v. Hammersmith L.B.C. [1991] 2 WLR 372 per Lord Templeman at p. 383. Local authorities have power to acquire and to own property and have power to employ staff. These powers are functions of the authority in question. It would be legally possible to own real property without insuring it against normal risks covered by insurance such as destruction by fire. However, to do so would be an imprudent and risky course. It would leave the owner subject to large but haphazard losses. Thus the insurance of real property is an ordinary incident of the ownership of that property, in much the same way as a proper programme of maintenance of the property and a proper method of security for the property are ordinary incidents of ownership. It seems to me to be perfectly obvious that in these circumstances the insurance of the property held is something which (a) is calculated to facilitate and (b) is conducive to and (c) is incidental to the power and function of owning property, and for this reason is authorised by s. 111(1) of the Local Government Act 1972. Similar considerations and a similar conclusion apply to other forms of insurance entered into by local authorities in connection with their many and various other functions.

7. Once this point is reached it seems to me necessarily to follow that all normal and proper dealings with the insurances so effected also fall within the ambit of s. 111(1) of the Act. For example, it may be that a person effecting substantial insurance would normally take the advice of a risk management adviser. It seems to me that a local authority could do just this relying upon their powers under s. 111(1). If the insurance company with which the insurance is effected meets actual or potential financial difficulties the assured must in all common sense take steps to secure and protect their position. Should it be the case that a scheme under s. 425 of the Companies Act 1985 is the best course available to secure and protect the position of the insured persons it seems to me that it inevitably follows that participation in such a scheme is in principle within the power of a local authority under s. 111(1) of the Local Government Act 1972. It is sometimes said that for an activity to be authorised by s. 111(1) it must be incidental to a function of the authority and that a further activity cannot be said to be incidental to something which is itself incidental to a permitted function. It may well be that the use of s. 111(1) to authorise something which is twice removed from an expressly authorised function is not permissible. This does not affect the present reasoning. The expressly authorised function of the authority is something such as the ownership of property for a specified purpose. On a correct analysis activities such as insuring the property or making the most prudent arrangements when an insurance becomes subject to potential difficulties are both incidental to the express function, and so are both in my opinion clearly authorised by the language of s. 111(1).

8. In my opinion a useful analogy can be drawn from the power of local authorities to compromise claims brought against them. In re Norwich Provident Insurance Society (1878) 8 Ch. D. 334 Sir George Jessel M.R. said at p. 340 that local authorities had a general power to compromise claims brought against them. In Holsworthy U.D.C. v. Holsworthy R.D.C. [1907] 2 Ch. 62 Warrington J. said at p.73,

> **"a compromise, if entered into bona fide, and if it does not involve the doing of any act by one of the parties which is itself ultra vires, may be made by and may be binding on a Corporation just as on an individual."**

These words were cited with approval as expressing the correct principle in Hazell v. Hammersmith LBC (supra), per Lord Templeman at p. 392. In the present case various local authorities have actual or potential claims against MMI under contracts of insurance. It may be in the general interest of all involved that in certain circumstances those claims are limited in amount by a scheme of compromise. There is nothing inherently ultra vires in compromising a claim by agreeing to enforce only a part of the total claim. Consequently it seems to me to accord precisely with the principles as regards compromises adumbrated in the above decision that the local authorities can validly compromise their claims in the manner proposed.

9. One matter raised in my instructions is whether the action of the local authorities in participating in the scheme could be impugned on the basis that they were giving a guarantee. The power of local authorities to give guarantees has been a topic much discussed recently and is, I understand, the subject of current litigation in the case of Credit Suisse v. Allerdale D.C. I do not think that the scheme could possibly be categorised as a guarantee or as anything akin to a guarantee. A guarantee has been defined as "an accessory contract by which the promisor undertakes to be answerable to the promisee for the debt, default or miscarriage of another person whose primary liability to the promisee must exist or be contemplated": see Halsbury's Laws, Volume 20, para. 101. Under the proposed scheme the members of the scheme are not to be answerable for the debts or obligations of anybody. Consequently I do not consider that the question of a guarantee is germane to the present question.

10. For the reasons explained it seems clear to me that local authorities do in principle have the capacity in law to enter into the proposed scheme. I must go on to consider whether there are any specific aspects of the proposed arrangements which might cast doubt on this conclusion.

(1) One aspect of the scheme is that it will involve only a class of the total creditors of MMI (as mentioned in paragraph 2 of this Advice). Other creditors will continue to have their claims paid in full and will not be subject to any levy. These other creditors will therefore benefit from the scheme in that the risk of insolvent liquidation of MMI is reduced, but will bear none of the burden of a possible reduction in the amount obtained on claims. The reason why other creditors are not sought to be brought within the ambit of the scheme is, I am told, that it would not be practical to include them because of the large number of policyholders involved. In my view the benefit conferred on the other creditors without any corresponding burden cannot in principle render the scheme ultra vires as regards the local authorities who will be within it. The question which I am at present considering is whether the scheme is in principle within the powers of the authorities. The incidental effect that others are benefitted cannot in itself render the scheme ultra vires.

(2) I am referred to the position of the Policyholders Protection Board under the Policyholders Protection Act 1975. That Board has a statutory duty to make payments to certain holders of insurance policies, and in the event of the liquidation of MMI some creditors would be entitled to payments from the Board. It is hoped that the Board will join in the scheme by agreeing to reimburse MMI certain amounts in specified circumstances. I need not set out the details as currently proposed. The impetus to the Board to participate in the scheme is that it would thereby hope to reduce its ultimate liabilities. In my opinion the participation or otherwise of the Board cannot affect the principle of the capacity of local authorities themselves to join in the scheme. The Board must reach its own decision in the light of its own statutory responsibilities. The vires of the actions of local authorities cannot in principle depend upon its decision.

(3) It is not at present clear precisely what will happen at the end of the period of operation of the scheme when all claims and liabilities have been ascertained. If any surplus is available this will in the first instance be paid to creditors under the scheme who have received (by reason of the levy or reduced payment) less than the full amount due to them. If MMI still has any assets remaining then a commission will be paid to the class of creditors bound by the Scheme. Thereafter any remaining surplus will be paid to members of MMI. This also has no bearing on the principle involved. Clearly such a payment of commission could work only to the benefit of creditors within the scheme and the prospect of its occurrence cannot invalidate the scheme or render it ultra vires as regards the local authority participants.

11. For the reasons explained in the last paragraph it does not seem to me that there are any specific aspects of the proposed scheme which throw doubt upon its validity or suggest that it may be beyond the powers of local authorities to participate in it.

12. Each local authority which has an existing or potential claim upon MMI will be bound to consider whether it should participate in the scheme. There are two aspects of the decision to participate. One is a consideration of whether the scheme is in the general interests of those who will participate in it. This is a general matter independent of the position of any individual participant. I have outlined the overall purpose and advantages of the scheme as they have been outlined to me. No doubt any authority will wish to consider the nature of and background to the scheme with care, and to take any necessary advice, before deciding whether to assent to it. The other aspect of any decision is a consideration of the individual position of the particular authority involved. With hundreds of authorities involved it is obvious that not all will be in the same position. Different Councils will have different policies in place, and may have different existing claims or expectations of future claims. Because it may be in the general interest of local authority policyholders to agree to the scheme it does not inevitably follow that to agree would be in the interest of every authority. For these reasons each authority must itself consider its position and make its own decision whether to participate in the scheme. In assessing the validity of an action of a local authority in exercising an alleged power there are always two questions, namely (1) whether the power exists, and (2) if so, whether the exercise of the power is valid in the particular instance under review. The answer to the latter question generally depends upon whether the decision has been taken on the basis of having regard to all material considerations and for the proper purposes.

13. **Conclusions**

(1) Local authorities who are policyholders with MMI do in principle have power under s. 111(1) of the Local Government Act 1972 to enter into the proposed scheme of arrangement under s. 425 of the Companies Act 1985.

(2) The proposed scheme is not a guarantee.

(3) There are no detailed aspects of the proposed scheme known to me which would render participation in it outside the powers of the local authorities.

(4) Each local authority, before reaching a decision on whether it will agree to the scheme, should consider both the general and overall benefit of the scheme and how its own particular circumstances and position will be affected by the operation of the scheme.

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D. M. BARNES Q.C.

4, Breams Buildings, London EC4A 1AQ
17th September 1993"

Opinion of Mr. R. L. Martin, Q.C.

"OPINION of SENIOR COUNSEL

for

CONVENTION OF SCOTTISH LOCAL AUTHORITIES

re MUNICIPAL MUTUAL INSURANCE LIMITED

I refer to the letters of instruction and have considered the Instructions to Counsel and the Advice by Mr. Michael Barnes, QC dated 17th September, 1993.

I am asked to advise generally on the capacity of a local authority in Scotland to enter into a scheme of arrangement under section 425 of the Companies Act 1985 ("the 1985 Act") as creditors of Municipal Mutual Insurance Limited and, in particular:—

(a) as to whether the obligations which would be assumed by a local authority as a Scheme Creditor pursuant to the Scheme of Arrangement to which this Opinion will appear as an Appendix (the "Scheme") would constitute a guarantee;

(b) as to whether the participation of a local authority in the Scheme and their obligations (including their potential future obligations) thereunder (including the imposition of a levy and subsequent reduction in payment of insurance claims) would be intra vires: and

(c) as to whether the answers to (a) and (b) above would be different if the Policyholders Protection Board were not to agree to be bound by the Scheme as provided therein.

I am of opinion that the analysis and advice by Mr. Barnes would hold good in respect of a local authority in Scotland, and that it would be intra vires for a local authority acting under the Local Government (Scotland) Act 1973 ("the 1973 Act") to enter into the proposed scheme of arrangement in terms of Section 425 of the 1985 Act.

Mr. Barnes has based his views upon an analysis of Section 111(1) of the Local Government Act 1972 ("the 1972 Act") and has referred to certain authorities decided upon the basis of that section. In Scotland, the equivalent provision is Section 69(1) of the 1973 Act, which is in identical terms. It is also to be noted that there is a very close, if not exact, relationship between the provisions of the Acts for the two jurisdictions, not least in relation to the arrangements for discharge of functions by local authorities: Section 101(1) of the 1972 Act, Section 56(1) of the 1973 Act.

In general, I would expect the Court of Session to apply the same principles to the interpretation and application of Section 69(1) of the 1973 Act, as the courts in England would apply to Section 111(1) of the 1972 Act. More particularly, there are examples of decisions of the Court of Session in construing Section 69(1) of the 1973 Act which have drawn support from, or at least drawn no distinction with, decided cases in England under Section 111(1) of the 1972 Act.

By way of recent example, I refer to **Thomson v. City of Glasgow District Council 1992 S.L.T.805** in which reference was made to **Hazell v. Hammersmith & Fulham London Borough Council [1992] 2 A.C.1**, which is referred to by Mr. Barnes, and also to **R. v. Richmond London Borough Council ex parte McCarthy & Stone (Developments) Limited**, now reported at **[1992] 2 A.C.48**. I also refer to **Commission for Local Authority Accounts in Scotland v. City of Edinburgh District Council 1988 S.L.T.767**, in which the Lord Justice-Clerk (Ross) referred to the decision in **R. v. Inner London Education Authority ex parte Westminster City Council [1986] 1 W.L.R.28**, in which case Glidewell J. in applying Section 142(2) of the 1972 Act quoted with approval the opinion of Lord Ross in **Meek v. Lothian Regional Council 1982 S.C.84** in dealing with the equivalent in Scotland, Section 88(2) of the 1973 Act.

An examination of these authorities has satisfied me that in applying the equivalent legislation, the Court of Session would adopt the same approach as that likely to be

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adopted in the opinion of Mr. Barnes by the courts in England, and accordingly that a local authority in Scotland may proceed to participate in the proposed arrangement subject to their own consideration of the circumstances applicable under reference to paragraph 12 of Mr. Barnes' Advice.

I have considered one aspect of the Advice in particular, namely the argument that participation in the scheme might properly be regarded as incidental to something which is already incidental to a function of a local authority, and thus ultra vires. This I have done in light of the speech of Lord Lowry in **R. v. Richmond London Borough Council ex parte McCarthy & Stone (Developments) Limited**, sup. cit. at page 70. If the taking out of insurance is incidental to a function of the local authority, and I agree with Mr. Barnes in this respect, it might be said that the making of a compromise was incidental to the taking out of insurance, and thus incidental to something which was already incidental to a function.

If this approach were correct, anything done in consequence of the taking out of insurance would be incidental to it, including the making of a claim. This would lead to the ludicrous result that a local authority was empowered to take out insurance, but not to make any claim following an event covered by that insurance.

In my opinion, the correct analysis is to say that the putting in place of insurance is incidental to a function, but that putting in place includes all aspects of the insurance cover including the obtaining of a policy, the payment of premiums, the making and receipt of claims, and in present circumstances the reaching of a compromise in relation to future claims. I therefore agree with the view expressed by Mr. Barnes at the end of paragraph 7.

I now consider the potential argument that the arrangement amounts to a form of guarantee which might be ultra vires of a local authority.

A guarantee is a form of cautionary obligation defined in **Bell's Principles, 10th Edition at paragraph 245** as "an accessory obligation or engagement, as surety for another, that the principal obligant shall pay the debt or perform the act for which he has engaged, otherwise the cautioner shall pay the debt or fulfil the obligation." This definition would appear to correspond to that quoted by Mr. Barnes from **Halsbury's Laws of England, Volume 20 paragraph 101**, and I therefore agree with Mr. Barnes that the arrangement proposed does not possess the principal characteristic of a guarantee, namely that an obligation is assumed for the debts or obligations of a third party.

With respect to the position of the Policyholders Protection Board, I have reached the opinion that their refusal to agree to be bound by the Scheme could not affect the vires of a local authority to enter into the Scheme. In this regard, I refer to paragraph 10(1) of Mr. Barnes' Advice and have nothing to add.

I therefore conclude that participation by a local authority in Scotland in the Scheme would be intra vires, subject only to each local authority carrying out an assessment of their own circumstances.

The Opinion of



R. L. Martin, QC,
Advocates' Library,
Parliament House,
Edinburgh.

3rd November, 1993."

APPENDIX D

Letters from KPMG Actuarial Services and Durtnell & Fowler Ltd. relating to the Commission

KPMG Actuarial Services

Actuaries and Consultants

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United Kingdom

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Telex 8811541 KPMGLO G
Telefax +44 71-832 8524
DX 38050 Blackfriars

The Managing Trustees
Municipal Mutual Insurance Limited
22 Old Queen Street
Westminster
LONDON SW1H 9HW

11 November 1993

Gentlemen

MMI Proposed Scheme of Arrangement

1 Introduction

1.1 In accordance with your letter of instruction we have further analysed the variability associated with the mid range figures identified in our report on the IBNR reserves required for the UK business as at 31 December 1992 and dated 10 September 1993 ("the report"). To this end we have analysed the following accounts:

- Public Liability,
- Employers Liability,
- Motor Vehicle,
- Fire General,
- Risk and Financial Management Programme ("RFMP") Liability and Motor.

In aggregate the undiscounted mid range reserve, including IBNRs as estimated in the report, for the total book of UK business is some £820 million of which the five accounts above represent some £730 million. These figures are net of all reinsurance except the aggregate excess of loss agreement referred to in note 18 to MMI's 31 December 1992 accounts, which provides for an aggregate recovery of up to £105 million between 1993 and 2000. We understand that the figure of £820 million has been incorporated, after adjustment for this agreement, in MMI's 31 December 1992 accounts.

1.2 We have constructed a probability distribution for the ultimate cost of claims to each of the five accounts listed in 1.1. These distributions have been selected judgmentally bearing in mind:

- the sources of variation analysed in the report,
- the possible interaction between these sources.

Partners: P J Butler CBE, C M Sharman OBE, M D V Rake, R W Whewell, C A Evers, M Christophers, R C Wilkinson, P D Crutchett

Actuaries:- P J Akers, K A Bannister, S G Bishop, M Chistophers, T E Crowter, P D Crutchett, N C Dexter, C A Evers, J C Herrick, C A Melvin, I Pickering, M R Sanders, M Shelley, I Sykes, A V Twigg, R C Wilkinson

- Members of the Association of Consulting Actuaries

Member firm of
Klynveld Peat Marwick Goerdeler

Appointed Representative of KPMG Peat Marwick which is authorised by the Institute of Chartered Accountants in England & Wales to carry on investment business.

The address for the purposes of Section 4, Business Names Act 1985 is 1 Puddle Dock, Blackfriars, London EC4V 3PD

We have not carried out a rigorous statistical analysis. Indeed we do not consider that a rigorous statistical framework is appropriate for an analysis of MMI's IBNR reserves.

1.3 The sole purpose of the analysis we have undertaken is to assist in the determination of the commission referred to in your letter. The results of this analysis should not be used for any other purpose. In particular they should not be viewed as, and should not be relied upon as, a guide to potential ultimate claim costs.

1.4 We have in this analysis tried to assess in theoretical terms the sources of variation in the ultimate claims cost analysed in our report. We have not attempted to measure the total risk of payments under the Scheme being reduced, nor have we addressed market perceptions of this risk. Some of the key risks which in consequence we have not tried to assess are discussed in 3.

1.5 We understand that MMI's reinsurance brokers, Durtnell & Fowler, have been asked to investigate what cover may be currently available to reinsure MMI's claims run-off and therefore recommend to MMI a value for the commission. The analysis of variability that we have undertaken forms part of the background to that investigation. We have discussed our methodology with Durtnell & Fowler.

2 Results

2.1 The constructed probability distributions discussed in 1.2 allow us to estimate a probability of ultimate claim costs exceeding any particular amount. Equally we can estimate a level of outturn which has a given probability of being exceeded.

2.2 The following table shows the results of this process for probabilities of 7%, 5%, 3% and 1% for each of the five accounts analysed. As an illustration, the entry under 3% for the Public Liability Account is £31.1 million. This means that the probability, as derived from the distribution constructed for the Public Liability Account, of ultimate claim costs exceeding the mid range figure identified in the report by more than £31.1 million is 3%. We caution that the limitations listed in 3 should be borne in mind when interpreting these figures.

	Amount above mid range exceeded with given probability (£m)			
Account	7%	5%	3%	1%
Public Liability	22.5	26.0	31.1	40.2
Employers Liability	15.5	17.9	21.3	27.1
Motor Vehicle	6.0	7.0	8.5	11.5
Fire General	9.2	10.8	13.1	17.8
RFMP Motor & Liability	7.7	8.7	9.9	11.4
Sum (see 2.3)	60.9	70.4	83.9	108.0

2.3 The table shows for each chosen probability the sum of the estimated levels of outturn for the five accounts. A calculation, at the chosen probability, based on the aggregate of all five accounts would produce a lower level than this sum. This is discussed further in 3.3. In the context however of the difficulty in measuring the inter-relationship between the forces driving claims development within the different accounts we have chosen not to adjust these sums.

3 Limitations

3.1 The limitations listed in the report also apply to this further work. The inherent uncertainty of the insurance process makes it almost certain that historical data will not be wholly predictive of actual future emergence. In particular, our analysis of ultimate claim costs has been based solely on the nature of MMI's claims development to date, as recorded in their management information systems. In

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consequence we stress that the following issues, amongst others, have not been considered:

- significant social, economic, legislative or judicial changes affecting claims development,
- new heads of claim appearing in the future,
- significant changes in the nature of claims handling affecting claims development,
- significant changes in the development pattern of known heads of claim,
- reinsurance security.

No adjustment has been made in the report nor in this analysis for claims handling expenses nor for the time value of money.

3.2 The data available for this analysis was the same as that used for our review of IBNR reserves as at 31 December 1992. In particular:

- no information about claims development beyond 30 June 1993 has been used;
- we have made no analysis of the adequacy of unearned premiums as at 31 December 1992.

3.3 We have analysed the variability associated with the five accounts listed in 1.1. We have not looked at these accounts together. To the extent that different factors influence the experience of each account there will be a measure of independence between claims development to each account. As an illustration of this, if the constructed probability of each account exceeding the best estimate by more than £10 million were 1%, then the constructed probability of all five accounts together exceeding the combined best estimate by more than £50 million (being the sum of the five individual layers) would *not* be 1%. The theoretical constructed probability would be somewhat less, depending on the degree of independence between claims development within the different accounts.

3.4 We have made no attempt to analyse variability other than within the accounts listed in 1.1. Although the variability within the remainder of the business is likely to be small in comparison with that within the accounts we have analysed, we caution that it is possible that claims development within the other accounts will develop beyond their recommended mid range figures.

3.5 In assessing the variability associated with ultimate claim costs we have attempted to address the risk that ultimate claim costs will be higher than those predicted. We have made no attempt to address any other factors influencing the extent to which MMI's liabilities will ultimately be paid. Principal amongst these are:

- changes in the timing of future claims payments,
- the performance of MMI's assets.

3.6 It must be stressed that we have undertaken this analysis for the sole purpose of assisting in the determination of a commission. This analysis is not intended to be, and should not be relied upon as, a guide to potential ultimate claims outturn nor to current market perceptions of that outturn. In particular any one of the factors listed in the foregoing paragraphs could have a significant effect on the current perceived view of the possibility of changes in future claims experience. In consequence commercial premiums charged to provide cover for the risks outlined in this letter could be very different from any theoretical amounts derived from this analysis.

Yours faithfully

KPMG Actuarial Services

KPMG Actuarial Services

DURTNELL & FOWLER LTD.

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INSURANCE BROKERS

Telephone
071 481 8631 (Switchboard)
071 488 8827 (Direct line)

TEN TRINITY SQUARE, LONDON EC3P 3AX

and at Lloyd's

11 November 1993

The Managing Trustees
Municipal Mutual Insurance Ltd
22 Old Queen Street
Westminster
LONDON
SW1H 9HW

Dear Sirs

We have been asked to comment in the light of prevailing market conditions on both the availability and pricing of reinsurance cover to protect the Company against deterioration of the total outstanding loss reserves. We have discussed with KPMG Actuarial Services the advice given by them to you in their letter dated 11th November 1993.

In our view, no reinsurance markets would entertain an unlimited reinsurance protection in view of the uncertainties of this class of business, together with the very bitter experience that reinsurers have suffered in this area. We have given this matter considerable thought and regrettably find we are simply unable to provide an indication of costing to you for such cover, which in any event would not be acceptable to reinsurance markets at this time.

It follows, therefore, that reinsurance protection would have to be purchased for a finite layer, rather than on an open-ended basis. Even such protection could only be costed by reinsurers after their own detailed actuarial study of the risk involved. Paragraph 3.6 of KPMG's letter draws particular attention to the effect on their perception of this risk of various changes in underlying assumptions. In these circumstances, we believe it probable that reinsurance could only be bought on acceptable terms on a basis with very little risk transfer, such as a "time and distance" cover.

If you were to contemplate arranging such financial reinsurance, we strongly urge that full recognition is given to the accounting and tax treatment of the transactions involved, particularly in view of the much closer regulatory scrutiny that such contracts now attract.

Yours faithfully
DURTNELL & FOWLER LTD

T R H THOMAS
Director

APPENDIX E

Material litigation

Set out below are details of all litigation which, to the knowledge of the Directors, is material in the context of the Scheme (except for litigation which has arisen, in the normal course of MMI's business, in respect of insurance or reinsurance contracts to which MMI is party):—

The London Borough of Harrow commenced proceedings against MMI on 18th January, 1993 alleging that MMI had failed to disclose material facts to it at the time of the renewal of its contract with MMI; that the announcement made on 30th September, 1992 of a suspension of claims payments amounted to an anticipatory repudiation of the contract by MMI which Harrow was entitled to, and did, accept; and that MMI has wrongfully retained certain documentation belonging to Harrow. Harrow claims a return of the premium paid to MMI amounting to £352,055, which represented a part payment of the annual premium, a return of the claims handling fees paid and damages representing the increased cost to Harrow of having insured elsewhere following Harrow's transfer of its policies to alternative insurers.

In turn, MMI has counterclaimed against Harrow for sums owed to it in respect of outstanding premium amounting to £258,095. MMI has been advised by Leading Counsel that it has a strong defence to Harrow's claims and a strong chance of recovering the outstanding premium owed to it by Harrow.

APPENDIX F

Cork Gully letter

Cork Gully

the insolvency practice of
Coopers & Lybrand

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cables Colybrand London
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Municipal Mutual Insurance Limited
22 Old Queen Street
Westminster
LONDON
SW1H 9HW

11 November 1993

Dear Sirs

Municipal Mutual Insurance Limited ("the Company")

Introduction

1.1 We were instructed by you on 6 May 1992 to act on behalf of the Company and its associated and subsidiary companies in respect of certain matters relating to the Company's solvency and inter alia to provide appropriate advice in the light of the relevant legislation. We were subsequently instructed on 3 December 1992 to investigate and if thought advisable prepare in consultation with the Company's solicitors and counsel a scheme of arrangement and in particular to advise where in our opinion the balance of advantage respectively lies for the general body of creditors of the Company and the Scheme Creditors as a class of such creditors as between the proposed Scheme of Arrangement and other alternative methods of dealing with the problems which might arise if the Company were to become insolvent.

1.2 Cork Gully is the insolvency practice of Coopers & Lybrand. Prior to our appointment as outlined above Coopers & Lybrand acted and continues to act as auditors to the Company and its associated and subsidiary companies and in addition provides other services and advice to the Company including but not limited to tax and actuarial advice.

1.3 We understand that this report will form an Appendix to the Explanatory Statement to be issued in relation to the proposed Scheme. It should therefore be read in conjunction with the Explanatory Statement all appendices thereto and the Scheme document itself. All documents should be read in full.

1.4 The terms used in this report bear the meaning given to them in the Scheme.

1.5 Scheme Creditors who are in any doubt as to the opinions expressed in this report are advised to take independent professional advice.

1.6 This report is divided into the following sections:

Alternatives to Liquidation or a Scheme of Arrangement	Paragraphs 2.1 to 2.7
Liquidation	Paragraphs 3.1 to 3.8
Scheme of Arrangement	Paragraphs 4.1 to 4.7
Liquidator's Remedies	Paragraphs 5.1 to 5.3
Reinsurance Recoveries	Paragraph 6.1
Conclusions	Paragraphs 7.1 to 7.2

Coopers & Lybrand is a member firm of Coopers & Lybrand (International)

A list of partners' names is available at the above address. Cork Gully is a trading name of Coopers & Lybrand, which is authorised carry on investment business Chartered Accountants in England and Wales.

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Alternatives to Liquidation or a Scheme of Arrangement

2.1 The alternative approaches for dealing with the problems of an insurance company in financial difficulties other than by way of a scheme or liquidation broadly comprise:

(i) Ad Hoc Commutation
(ii) Informal Arrangement
(iii) Voluntary Arrangement
(iv) A Reduction in Contracts pursuant to Section 58 of the Insurance Companies Act 1982
(v) Recapitalisation.

2.2 Each of 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 in the present matter.

2.3 An Ad Hoc Commutation of liabilities would require the Company to settle its obligations on the basis of individual negotiations with many thousands of creditors. The administrative burden and cost of such an approach renders Ad Hoc Commutation impracticable. However even if Ad Hoc Commutation were possible each settlement would be on the basis of the best terms which the Company could negotiate with each individual creditor consequently there is no certainty that equality of treatment for all creditors would be possible. Moreover throughout the period of the commutation exercise which could take many years the Company could be open to the threat of litigation and the Company's assets would be subject to the possibility of execution by individual creditors who objected to the commutation exercise. Bearing in mind that many creditors would be private policyholders seeking to recover awards of damages made against them which in the absence of insurance they could not meet it is probable that winding-up proceedings would be instituted in order that such creditors could avail themselves of the protection afforded by the Policyholders Protection Act 1975. Finally in the event of ultimate insolvency there would always be the possibility that the cost of effecting earlier settlements might be so high that insufficient funds would be available to meet the costs of later settlements either on a similar basis or at all.

2.4 An Informal Arrangement or compromise unless agreed to by every creditor would not bind all creditors to the Arrangement but only those who agree to be bound by it. With many thousands of creditors it is unlikely that the Company could obtain the agreement of all its creditors either within a reasonable timescale or at all. The likelihood of litigation or execution by individual creditors who declined to be bound to the Arrangement or of winding-up proceedings for the reasons set out in paragraph 2.3 above would thus remain substantial.

2.5 A Voluntary Arrangement under Part I of the Insolvency Act 1986 could lay before creditors proposals for a compromise or arrangement with them similar to those contained in the Scheme. However unlike the requirements for the approval of a scheme which are more fully set out in the Explanatory Statement a Voluntary Arrangement would only be binding upon those creditors who received notice of it. There is a possibility that some creditors would not receive notice notwithstanding the Company's best efforts to reach them. Such creditors would not be bound to the terms of the Voluntary Arrangement and the Company would continue to be at risk of the threat of litigation or execution to the detriment of the general body of creditors. Moreover since the provisions of the Policyholders Protection Act would not apply to a Voluntary Arrangement the Policyholders Protection Board would not be able to participate in it.

2.6 A Reduction in Contracts pursuant to Section 58 of the Insurance Companies Act 1982 is permitted as an alternative to winding-up. However in order to obtain an order from the court it would be necessary to demonstrate to the court that the Company is unable to pay its debts. For the reasons set out in paragraph 4.1 below this could not presently be demonstrated. Moreover since a Reduction in Contracts is a mechanism much more appropriate to life assurance it is difficult to envisage how this could be applied for instance to liability contracts. However even if an application to the court for a Reduction in Contracts could be made it is most unlikely that the court would grant such a reduction in contracts in the present circumstances since this would deprive private policyholders of the benefits of the Policyholders Protection Act.

2.7 The Company is a mutual company having no share capital and therefore it has no access to capital from its members so that Recapitalisation is not possible.

Liquidation

3.1 In the event of liquidation a liquidator or liquidators would be appointed whose task would be to realise the Company's assets and distribute them rateably among the Company's creditors. However it is unlikely that an early distribution would be made to creditors since a liquidator would need to be satisfied that the ultimate liabilities of the Company had been ascertained before making distributions. Failure to do this could result in excess distributions being made to earlier proving creditors leaving insufficient funds available to enable like distributions to be made to later proving creditors.

3.2 Because the liquidator of an insurance company is dealing with an estate where the ultimate level of assets and liabilities is unlikely to be known for some considerable time it is doubtful that a liquidator would wish to make interim distributions until he is satisfied that he can gauge with accuracy the ultimate level of those assets and liabilities. It is probable therefore (subject to the comments contained in paragraph 3.3 below) that there would be a material delay between the appointment of a liquidator and the payment of a first interim distribution. Not only would creditors have to wait longer before receiving distributions out of the estate but they would also have to bear the financing costs of the delayed payment of their claims for a longer period than is anticipated under the Scheme thus reducing the time value of distributions.

3.3 It is of course possible that a provisional liquidator or liquidator with a view to minimising further loss to creditors would seek to promote a scheme as a means of overcoming the problems of uncertainty as regards the ultimate level of assets or liabilities however there can be no certainty that this would happen or what the timing and terms of any scheme might be.

3.4 In addition to having to wait longer for distributions in a liquidation with or without a scheme creditors would also have to bear the burden of the additional costs which would be incurred in a liquidation. In a liquidation statutory fees are levied upon any realisations or investments made by a liquidator by The Insolvency Service (an Executive Agency within the Department of Trade and Industry). In a compulsory liquidation fees charged on realisations are on a sliding scale; by way of example realisations made of £10 million would attract fees of £275,250 and realisations of £800 million would attract fees in excess of £1 million. The fees charged on realisations in a creditors voluntary liquidation (i.e when a company resolves that it be wound up voluntarily but no declaration of solvency is made) are considerably less being limited to a maximum of £12,500.

However in addition to the fee charged on realisations an additional charge of 0.625% is made on all investments made by a liquidator and each reinvestment thereof whether or not the liquidation is compulsory or voluntary. Whilst it is not possible to say with certainty what such fees would amount to we have estimated that assuming a 10 year liquidation commencing on 1 January 1994 with dividends payable in the fifth seventh and tenth years and further assuming that investments are made in 6 month Treasury Bills the fees would be within the range £35 to £45 million. Furthermore there is a restricted range of investments which a liquidator may make which may not necessarily produce as commercial a yield as might be available in the money market.

The Insolvency Service has advised that at the present time investments may not be made in Treasury Bills with maturity dates beyond 11 February 1994 other than 3 month Treasury Bills. It is not known what arrangements will exist after that date. If investments in 3 month Treasury Bills or any alternative investments then available to insolvency practitioners do not yield in excess of 3.5% net after deducting the fees made on investments by The Insolvency Service then it is likely that realisations will be left on deposit with The Insolvency Service account at the Bank of England which yields 3.5% per annum.

3.5 Under UK insolvency law claims denominated in currencies other than sterling crystallise into sterling at the rate of exchange prevailing at the date of liquidation. A number of the Company's creditors have claims against the Company in currencies other

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than sterling. In a liquidation creditors with such foreign currency claims would be at risk of adverse exchange rate movements however the scheme provides that such creditors will receive payments in respect of their Established Scheme Liabilities in their original currencies thus avoiding any exchange risk.

3.6 Liquidators are not likely to risk speculating over the future value of assets and therefore a liquidator will typically seek to realise a company's assets as quickly as possible. Consequently the proceeds which would be achieved from realisations of assets by a liquidator particularly if they are made on a forced sale basis could well be lower than those which might be achieved by the adoption of a more commercial approach.

3.7 On a solvent liquidation interest would be payable on creditors' claims. Under the Scheme no such interest is payable after the Trigger Date although the Scheme provides for a commission (as described in the Company's Explanatory Statement to which this letter forms an Appendix) to be payable to Scheme Creditors and the PPB. However the commission does not take into account the timing of any payment or payments made to any Scheme Creditor under the Scheme.

3.8 Under the Scheme claims arising under current policies will continue to be payable (even after the Trigger Date) in accordance with the provisions of the Scheme. If MMI were to go into liquidation however only unexpired premiums would be repayable to policyholders.

Scheme of Arrangement

4.1 The balance sheet which forms part of the 1992 audited accounts of the Company shows a net deficiency of £129 million as at 31 December 1992. The Company's pro-forma balance sheet as at the same date shows a surplus of assets over liabilities of only £907,000 or approximately 0.1% of liabilities. This is a sufficiently small surplus to require the Board of Managing Trustees to consider carefully the basis upon which the run-off of the Company's liabilities should be conducted.

4.2 Whilst the Company's surplus is below the statutorily required level for an insurance company operating on a going concern basis the Company has not traded on this basis since it ceased underwriting on 30 September 1992 and commenced to run-off its liabilities.

4.3 On either of the usual tests of solvency the Company on the basis of the pro-forma balance sheet is solvent in so far as its assets exceed its liabilities (the balance sheet test) and it is able to meet its obligations as they fall due (the cashflow test) over the period of the run-off of its liabilities.

4.4 The current run-off projection indicates that there will be a surplus of assets over liabilities however since that run-off projection covers a period of some 10 years the Managing Trustees are aware that material developments could take place over that period which may adversely affect the Company's position.

4.5 The projection is particularly sensitive for instance to changes in interest rates and the realisable value of assets. For the purposes of its statutory accounts the Company does not discount its reserves in order to take account of the time value of money and does not make a provision for run-off costs anticipating that future investment income will be sufficient to cover such costs. However the pro-forma balance sheet does take account of both future investment income and run-off costs. In the event of a material reduction in interest rates it is possible that future investment income will be insufficient to meet the run-off costs which would mean that the excess expenditure would have to be met out of the Company's limited pro-forma balance sheet surplus. Similarly the Company has a range of investments including investment property the value of which is again sensitive to interest rate changes. Historically investment property has tended to increase in value over time although there have from time to time been temporary falls in the market. Whilst therefore it is reasonable for the Managing Trustees to assume that over the period of the run-off the value of investment property will rise it is nevertheless possible that it could fall.

4.6 During the period of the run-off of the Company's liabilities it is possible that material claims could arise unexpectedly of such large amounts that the Company could be

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rendered insolvent. Should this or some other contingency arise which renders the Company insolvent the Scheme provides a mechanism to enable the Company to continue to pay claims in a substantially normal manner albeit subject in the case of Scheme Creditors to the imposition of a levy and a reduction of subsequent claim payments.

4.7 Protected Creditors whose claims arise under non-compulsory insurance policies who would receive only 90% of their claims in a liquidation will be paid in full under the Scheme so that such creditors have a material advantage under the Scheme as compared with a liquidation.

However the liabilities to which this provision of the Scheme applies are very small in relation to the Company's overall liabilities and have been estimated by the Company as at 30 September 1993 to be approximately £21 million reducing to approximately £2.5 million by 31 December 1995. The additional payments which might therefore arise reduce from £2.1 million to £250,000 over this period. The saving on administrative costs likely to arise as a result of this simplified approach is considered to be such that Scheme Creditors should not be materially disadvantaged.

Liquidator's Remedies

5.1 If the Scheme is adopted as an alternative to liquidation then in the absence of the appointment of a liquidator any remedies available to a liquidator under the provisions of the Insolvency Act 1986 would not be available to the Scheme Administrator and so would be lost. However regardless of whether the Scheme is adopted as an alternative to liquidation the Managing Trustees are and have been at all times when in office subject to a duty to act bona fide in the best interests of the Company (which in the current circumstances would include the interests of the Company's creditors) and for proper purposes. Even if the proposed Scheme is approved and becomes effective any breach of such duties would make the Managing Trustees liable for breach of duty. Furthermore since the Managing Trustees first became aware of the Company's financial difficulties the advice of this firm has been obtained on all material transactions entered into by the Company.

5.2 Under the provisions of the Insolvency Act 1986 a liquidator is able to pursue recoveries for the benefit of the insolvent company arising out of the wrongful trading or fraudulent trading of any past or present director including a shadow director or against the creditor preferred where there had been any voidable preference or against any party who has been the beneficiary of any transaction at an undervalue.

5.3 No investigation has been conducted with a view to determining whether any such remedies exist since as stated in the Company's Explanatory Statement the Managing Trustees can foresee a solvent run-off and are subject in any event to liability for breach of duty. If the Scheme is adopted as an alternative to liquidation then to the extent that they may exist any causes of action which might have given rise to the remedies available to a liquidator as described above may still give rise to other claims such as for breach of duty by the Managing Trustees.

Reinsurance Recoveries

6.1 We understand that the Board of Managing Trustees have taken the advice of Slaughter and May solicitors and counsel and have drafted the Scheme in such a way as to remove or minimise the possibility of it containing any waiver or release of any of the creditors' claims against the Company which might entitle reinsurers to decline to pay in circumstances where they would be obliged to pay if the Company were in insolvent liquidation.

Accordingly there is no reason on this basis to assess the Scheme any differently from liquidation as regards likely reinsurance recoveries.

Conclusions

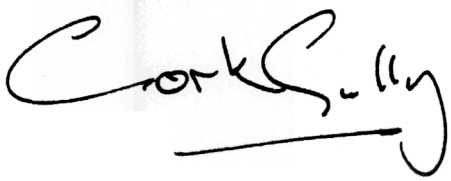
7.1 Having considered the advantages and disadvantages of the proposed Scheme respectively for the general body of the Company's creditors and Scheme Creditors as a class of such creditors as compared with liquidation or any other alternative method of

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dealing with the problems arising from the Company's financial position (the detailed considerations of which are more fully set out above) it is our considered opinion that the proposed Scheme has substantial advantages for and is likely to be in the best interests of the Company's creditors generally and Scheme Creditors as a class of such creditors.

7.2 This report has been prepared for the Company. It does not represent advice to individual creditors on their specific position under the Scheme or in the event of liquidation. Any creditor who is uncertain concerning their own position under the Scheme or in the event of liquidation should seek appropriate advice.

Yours faithfully



CORK GULLY

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APPENDIX G

Letter from the members of the Scheme Creditors' Sounding Board

To: Municipal Mutual Insurance Limited ("MMI")

15th November, 1993

Scheme of Arrangement

In May 1993, MMI asked for the assistance of local authorities in developing a proposal for MMI to enter into a scheme of arrangement with its creditors, or a class of them, and in preparing the necessary documentation. The undersigned were nominated to form a local authority "Sounding Board" for this purpose.

We were able to assist MMI in particular on the type, and level of detail, of information likely to be necessary in the Scheme documentation and the extent to which there should be a comparison in the Scheme documentation between the proposed scheme of arrangement and other courses of action available to MMI and its creditors.

Whilst the Sounding Board is not responsible for its contents, we believe that the final Scheme documentation to be sent to Scheme Creditors substantially reflects input from the Sounding Board to the process so that each local authority and other Scheme Creditors can consider their position.

On the basis of the information in the document in which this letter will form an Appendix, we will be advising our individual employing authorities or, in the case of Martin Pilgrim, the authorities which are members of the Association of Metropolitan Authorities, to vote in support of the Scheme, recognising that each local authority must reach its own decision in the light of its own circumstances.

We sign this letter in our personal capacity and not on behalf of our employers or as representatives of local authorities generally.

We consent to the inclusion of a copy of this letter as an Appendix to the Explanatory Statement.

Yours faithfully,

W J Church

Bill Church
Director of Law and Administration
Hertfordshire County Council

Bernard Clarke

Bernard Clarke
City Finance Manager
Rochester upon Medway City Council

David Newlands

David Newlands
Deputy Director of Finance
Lothian Regional Council

Martin Pilgrim

Martin Pilgrim
Under Secretary, Finance
Association of Metropolitan Authorities

Michael Shaw
Director of Finance
Gateshead Metropolitan Borough Council

Bill Sulman

Bill Sulman
Principal Insurance Officer and Risk Manager
Nottingham County Council

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APPENDIX H

List of documents available for inspection

Copies of the following documents will be available for inspection by creditors and members of MMI during ordinary business hours on business days (excluding Saturdays and public holidays) at the offices of Slaughter and May, 35 Basinghall Street, London EC2V 5DB from the date of this document until the close of the meeting of Scheme Creditors to consider the Scheme of Arrangement (the "Court Meeting"):—

1. current and proposed new Memorandum and Articles of Association of MMI;
2. legal opinions of Mr. D.M. Barnes Q.C. and Mr. R.L. Martin Q.C. set out as Appendix C, together with the instructions to Counsel relating thereto;
3. letters from KPMG Actuarial Services and Durtnell & Fowler Ltd. set out as Appendix D;
4. Cork Gully letter set out as Appendix F;
5. letter from the members of the Scheme Creditors' Sounding Board set out as Appendix G;
6. written consent of Cork Gully to the issue of this document with the inclusion of references to their name in the form and context in which they are included and to the appearance of their letter as an Appendix;
7. written consent of KPMG Actuarial Services to the issue of this document with the inclusion of references to their name in the form and context in which they are included and to the appearance of their letter as an Appendix;
8. written consent of Durtnell & Fowler Ltd. to the issue of this document with the inclusion of references to their name in the form and context in which they are included and to the appearance of their letter as an Appendix;
9. written consent of the Policyholders Protection Board to the issue of this document substantially in the form of the proof attached to the letter and to the inclusion of references to the Policyholders Protection Board in the form and in the context in which they appear and agreement to be bound by the Scheme;
10. written consents of each of Chesterton and Ryden to the issue of this document with the inclusion of references to their respective names in the form and context in which they are included; and
11. the written consents referred to in Clauses 1.3.2 and 1.3.4 of the Scheme (initial Scheme Administrator, initial Deputy Scheme Administrator and initial members of the Creditors' Committee).

Copies of these documents will also be available for inspection by creditors and members of MMI at the Court Meeting.

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APPENDIX I

Memorandum on the Policyholders Protection Act 1975

1. PRELIMINARY

1.1 This memorandum provides a brief summary of certain provisions of the Policyholders Protection Act relevant to the Scheme. Words and expressions defined in the Scheme document in which this memorandum appears as an Appendix apply in this memorandum, unless the context otherwise requires.

1.2 This memorandum is not an exhaustive guide to all the provisions of the Policyholders Protection Act which may be relevant to the Scheme. **Any person who is in any doubt as to the effect of the provisions of that Act or their relevance to the Scheme should take his own independent legal advice.**

2. BASIS OF THE PPB's INVOLVEMENT IN THE SCHEME

2.1 The PPB will participate in the Scheme pursuant to its discretionary powers under section 16 of the Policyholders Protection Act to take such measures as it considers appropriate for the purposes of safeguarding policyholders of a company in financial difficulties to enable the company to continue to carry on insurance business. The PPB has power to make payments pursuant to that section on such terms and on such conditions as it thinks fit.

2.2 The PPB's obligations under the Scheme are determined principally by reference to the duties which, on a liquidation of MMI, it would owe to certain policyholders or security holders of MMI in respect of certain liabilities. Certain aspects of these duties are mentioned below.

3. DUTIES OF THE PPB IN THE EVENT OF LIQUIDATION

3.1 On a liquidation of MMI there would be two categories of liabilities of MMI towards certain policyholders or security holders which would qualify for protection from the PPB:—

(a) those where the liability may be protected as to 100 per cent. of its amount; and

(b) those where the liability may be protected as to 90 per cent. of its amount.

3.2 **It should be noted that the duties of the PPB referred to in paragraph 2.2 (and hence its obligations under the Scheme) are subject to a number of important qualifications. Furthermore, the existence of any duty of the PPB in any particular case depends upon the relevant conditions of the Policyholders Protection Act being satisfied.** Some of these qualifications and conditions and certain pertinent definitions are summarised or described below.

3.3 **100 per cent. protection**

Subject to the relevant provisions of the Policyholders Protection Act, it is the duty of the PPB to secure that a sum equal to the full amount of any "liability subject to compulsory insurance" of a company in liquidation towards any policyholder or security holder is paid to the policyholder or security holder as soon as reasonably practicable after the beginning of the liquidation. For this purpose, as well as for the purposes of the 90 per cent. protection referred to below, a policy must have been a policy of insurance which was "a United Kingdom policy" at the time when the liquidation of the company began.

3.4 "A liability subject to compulsory insurance" is a liability required under specified enactments to be covered by insurance (or by some other provision for securing its discharge). The specified enactments are section 1(4A)(d) of the Riding Establishments Act 1964, section 1 of the Employers' Liability (Compulsory Insurance) Act 1969, Part VI of the Road Traffic Act 1988 and the equivalent provisions in force in Northern Ireland. Policies evidencing contracts of insurance effected for the purposes of section 19 of the Nuclear Installations Act 1965 are also covered.

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3.5 A policy of insurance is a United Kingdom policy "at any time when the performance by the insurer of any of his obligations under the contract evidenced by the policy would constitute the carrying on by the insurer of insurance business of any class in the United Kingdom."

3.6 Where a claim relates to a liability under a policy of one of the types specified above which is not a liability subject to compulsory insurance, it is only eligible for 90 per cent. protection. This 90 per cent. protection is discussed below.

3.7 The PPB also has a duty, subject to the relevant provisions of the Policyholders Protection Act, to secure that a sum equal to the full amount of any liability of a company in liquidation in respect of a sum payable to a person entitled to the benefit of a judgment under certain legislation (section 149 of the Road Traffic Act 1972 or section 151 of the Road Traffic Act 1988 or the equivalent provisions in force in Northern Ireland) is paid to that person as soon as reasonably practicable after the beginning of the liquidation.

3.8 **90 per cent. protection**

The 90 per cent. protection is only available in respect of the liabilities of a company in liquidation towards "private policyholders". Subject to the relevant provisions of the Policyholders Protection Act, it is the duty of the PPB to secure that a sum equal to 90 per cent. of the amount of a liability of a company in liquidation towards a "private policyholder" under the terms of a relevant policy (which, as indicated above, must have been a United Kingdom policy at the relevant time) is paid to the policyholder as soon as reasonably practicable after the beginning of the liquidation.

3.9 A "private policyholder" means a policyholder who is either:—

(a) an individual; or

(b) a partnership or other unincorporated body of persons all of whom are individuals.

3.10 A liability will not qualify for the 90 per cent. protection unless the policy under which such liability arises is a "general policy" or one of the types referred to in paragraph 3.6 above. A "general policy" means any policy evidencing a contract the effecting of which constituted the carrying on of general business within the meaning of the Insurance Companies Act 1982, with the exception of reinsurance and certain specified classes of business. The categories of "general business" which are relevant for the purposes of the Policyholders Protection Act are accident, sickness, land vehicles, railway rolling stock, fire and natural forces, damage to property, motor vehicle liability, general liability, credit, suretyship, miscellaneous financial loss and legal expenses and assistance for persons getting into "difficulties" when, for example, travelling.

4. ASSIGNMENTS

4.1 Any duty of the PPB to assist a policyholder of a company in liquidation by the measures described above is subject to compliance on the part of the policyholder with any conditions imposed by the PPB with respect to the total or partial assignment to the PPB of his rights under or in respect of the policy and certain other rights.

4.2 The Scheme contains a provision (in Clause 6.2) by which all rights which MMI has in respect of a Protected Liability in relation to which reimbursement has been made by the PPB to MMI, shall be automatically assigned by way of security to the PPB with effect from reimbursement being made. Alternatively, the PPB may require a separate assignment to it of such rights in advance and as a pre-condition to reimbursement by it.

5. OTHER RELEVANT PROVISIONS

5.1 **General**

The reimbursement obligations of the PPB to MMI under the Scheme in respect of a Protected Liability are expressly made subject to the same conditions, limitations, qualifications and other provisions contained or referred to in, or capable of being imposed under, specified sections of the Policyholders Protection Act. Some potentially significant aspects of these provisions are summarised below.

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5.2 **Insufficiency of funds**

The PPB finances its functions in relation to general business by means of levies imposed upon authorised insurance companies carrying on general business in the United Kingdom. The amount an insurance company can be required to pay in respect of general business is limited, in any financial year, to one per cent. of its income liable to the levy in the year last ending before that financial year. Accordingly, the PPB's duties under sections 6 to 8, including the duties described above (and, therefore, its obligations under the Scheme) are qualified to the extent that they do not require the PPB to make any payment at a time when it appears to the PPB that the funds available for it fall short of what it needs to carry out its various responsibilities (including any responsibilities towards policyholders of companies other than MMI).

5.3 However, in the event that funds do fall short, the obligations of the PPB to make payment under the Scheme will be postponed and not avoided. It is not possible to forecast the amounts required for the PPB to perform all its responsibilities which may arise during the period of the Scheme. Although, since its inception, the PPB has not had to postpone a payment on the ground of insufficiency of funds, it is possible that responsibilities giving rise to substantial payments will arise in future years.

5.4 **Duplication of liability**

Section 9(1) provides that the PPB shall not, by virtue of any provision of sections 6 to 8, be required to secure any sum for a policyholder in respect of a policy of a company in liquidation which was a United Kingdom policy at the beginning of the liquidation or (as the case may be) for a person entitled to the benefit of a judgment, by reference to any liability (or any part of any liability) which is duplicated by the liability of any other authorised insurance company which is not a company in liquidation.

5.5 By virtue of section 9(2), a liability of a company towards a policyholder is duplicated by the liability of another company for these purposes in so far as that other company is also under a liability under the terms of any general policy which was a United Kingdom policy at the beginning of the first-mentioned company's liquidation, to make any payment to or on behalf of the policyholder in respect of the matter to which the liability of the first-mentioned company relates.

5.6 **Payment to a person other than the policyholder**

Under section 13(1) of the Policyholders Protection Act, where it appears to the PPB, in the case of any policy of a company in liquidation:—

(a) that payment in respect of any sums falling due under the policy could have been made in accordance with the policy to a person other than the policyholder; or

(b) that any sums paid under the policy would have been subject to any trust, charge or other agreement binding on the policyholder,

the PPB may secure the payment of any sum payable to the policyholder in accordance with any of the provisions of sections 6 to 10 (in whole or in part) to that other person or (as the case may be) to the person appearing to the PPB to be entitled under the trust, charge or agreement in question, instead of to the policyholder.

5.7 Any payment made by virtue of the provisions of section 13(1) of the Policyholders Protection Act to a person other than the policyholder is treated as a payment to the policyholder and may be made on such conditions (with respect to the total or partial assignment to the PPB of any rights of the recipient against the policyholder or any other person, or otherwise) as the PPB thinks fit.

6. PAYMENT TO THE POLICYHOLDER BY THIRD PARTIES

Section 14(1) of the Policyholders Protection Act provides that any payment made by any person other than the PPB (such as an insurance broker or other intermediary) to the policyholder, to a person entitled to the benefit of a judgment or to any other person, being a payment referable to any such liability of a company in liquidation as is mentioned in section 6, 7 or 8, shall be treated as reducing any sum payable by the PPB to the policyholder or to the person entitled to the benefit of the judgment in accordance with any provision of those sections, by reference to that liability. In its application to the Scheme, payments made by MMI are disregarded for the purposes of section 14(1).

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7. SECTION 16

To qualify for reimbursement under the Scheme, a Protected Liability must, *inter alia,* be due to a person who, in addition to satisfying the other specified eligibility criteria referable to a liquidation, meets the requirement of section 16(9) of the Policyholders Protection Act. This requirement means that you must be a policyholder in respect of a general policy of MMI which was a United Kingdom policy at the time of the application to the Court under section 425 of the Companies Act 1985 for the sanctioning of the Scheme.



PART II

SCHEME OF ARRANGEMENT

pursuant to section 425 of the
Companies Act 1985 of Great Britain

between

MUNICIPAL MUTUAL INSURANCE LIMITED

and

ITS SCHEME CREDITORS
(as defined in the Scheme)

and

to be binding on

THE POLICYHOLDERS PROTECTION BOARD

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PART 1

PRELIMINARY

1.1 **Definitions**

1.1.1 In the Scheme, unless the context otherwise requires or unless otherwise expressly provided for, the following words and expressions shall bear the following meanings:—

"Act"	the Companies Act 1985 (as supplemented and amended);
"Articles of Association"	the articles of association substantially in the form of the proposed new articles referred to in Appendix H to the explanatory statement comprised in the document in which this Scheme appears as Part II, as from time to time amended in accordance with their terms and the terms of the Scheme;
"Assignment"	an assignment under the terms of an Insurance Contract or otherwise and shall include a novation, and the words "Assigned" and "Assignees" shall be construed accordingly;
"Board"	the board of Directors of MMI from time to time;
"Commission"	£70 million, being the commission provision for payment of which is made in Clause 5.7;
"Commutation"	a contractual arrangement (other than an Insurance Contract) under which all or a part of the total Liability of MMI to a creditor under an Insurance Contract is discharged in full in consideration for a cash payment by MMI and which the Board or, after the Trigger Date, the Scheme Administrator is satisfied (having taken advice from actuaries if considered appropriate) will increase the net assets or, as the case may be, reduce the net Liabilities of MMI;
"Controller"	shall have the meaning given in paragraphs (a) and (b) of section 7(4) of the Insurance Companies Act 1982;
"Court"	the High Court of Justice of England and Wales;
"Court Meeting"	the meeting convened by MMI with leave of the Court to consider and, if thought fit, to approve the Scheme;
"Court Order"	the Order of the Court sanctioning the Scheme approved at the Court Meeting;
"Creditors' Committee"	the committee established pursuant to Clause 10.1;
"Creditors' Resolution"	a resolution passed by a majority in number representing three-fourths in value of the Voting Creditors which, being so entitled, are present and vote either in person or by proxy at any meeting of Voting Creditors;
"Current Directors"	the persons whose names are set out in Clause 1.3.3;
"Deputy Scheme Administrator"	the person whose name is set out in Clause 1.3.2.2 or such other person as may be appointed as the Deputy Scheme Administrator in accordance with the provisions of the Scheme;
"Directors"	the Managing Trustees or, as the case may be, directors of MMI from time to time;

"Effective Date"	the date on which an office copy of the Court Order shall have been delivered to the Registrar of Companies in England for registration in accordance with Clause 2.4;
"Election to Defend Decision"	in relation to any Insurance Contract, a decision by the Directors (during the Initial Scheme Period) or by the Scheme Administrator (during the Levy Period) for MMI to provide a Scheme Creditor with, or to engage, a loss adjuster, consulting engineer, medical examiner, lawyer or other adviser to defend a claim made against that Scheme Creditor, notwithstanding the fact that the Insurance Contract may not give rise to an obligation on MMI to do so;
"Elective Defence Costs"	in relation to any Election to Defend Decision, the costs incurred which MMI has paid or which have been agreed to be paid by MMI after the Record Date;
"Established Liability"	a Liability of MMI under or arising out of an Insurance Contract and in respect of which, at any relevant time, there has been established (whether before, on or after the Record Date and whether (i) by agreement or (ii) by arbitration (insofar as the same is provided for under the terms of the Insurance Contract) or any judicial action or proceeding which is not the subject of any appeal) an obligation on the part of MMI to pay an ascertained sum of money at that time (and, for the purposes of the Scheme, the amount of an Established Liability shall be the amount at which it is or has been so established notwithstanding any payment made (or treated as having been made) in respect thereof after the Record Date);
"Established Scheme Liability"	a Scheme Liability which has become an Established Scheme Liability in accordance with Clause 2.2;
"Estimated Value"	in relation to a Reported Scheme Liability in respect of which the books of MMI at the close of business on the Record Date recorded a value placed thereon by MMI, the value as so recorded;
"Excluded Liability"	(a) any Liability of MMI under or arising out of an Insurance Contract to the extent that MMI had drawn a cheque in payment thereof on or before the Record Date, or (b) any Liability of MMI under or arising out of an Insurance Contract which would, on becoming an Established Liability, be a Protected Liability for the purposes of the Scheme if in the definition of "Protected Liability" the reference to the Trigger Date were a reference to the Record Date, or (c) any Liability of MMI under or arising out of an Insurance Contract (whether or not falling within paragraph (b) of this definition) which (disregarding any Assignment which has been effected on or after the Record Date) is, or would be (but for any such Assignment), a Liability to a Personal Creditor, or

(d) any Liability of MMI under or arising out of an Insurance Contract which is discharged by way of Commutation, or

(e) any Liability of MMI under or arising out of an Insurance Contract which was either written or issued (i) by any branch or agency of MMI in Australia (including, for the avoidance of doubt, the branch trading as Municipal Mutual – Australia) or (ii) through any agency in New Zealand (including, for the avoidance of doubt, the agency of the Farmers' Mutual Group), or

(f) any Liability of MMI under or arising out of an Insurance Contract which was either written or issued or renewed by MMI in favour of Motability Finance Limited (being a company incorporated in England and Wales with registered number 1373876), whether or not falling within paragraphs (b) or (c) of this definition; or

(g) any PPB Liability;

"Initial Scheme Period" — the period beginning on the Effective Date and ending on the day before the Trigger Date;

"Insurance Contract" — any treaty or contract of insurance or reinsurance of any kind whatsoever which was entered into by MMI as insurer or inward reinsurer on or before the Record Date or under which MMI assumed any obligation or Liability on or before the Record Date;

"Levy" — a levy imposed under Part 5 (and "Levies" and "Levied" shall be construed accordingly);

"Levy Notice Date" — shall have the meaning given in Clause 5.5.1;

"Levy Period" — the period beginning on the Trigger Date and ending on the Termination Date;

"Liability" — any obligation or liability whether it is present, future, prospective or contingent, whether or not it is for a fixed or liquidated amount, whether or not involving the payment of money and whether it arises at common law, in equity or by statute in England and Wales, Scotland or in any other jurisdiction or in any other manner whatsoever, including any PPB Liability but excluding any obligation or liability which is statute barred or otherwise unenforceable and, for the avoidance of doubt, a person who does not have a legal obligation or liability under a contract or policy because such contract or policy is void or, being voidable, has been duly avoided will not have a Liability for the purposes of the Scheme;

"Local Authority" — either a "principal council" within the meaning of section 270(1) of the Local Government Act 1972 (as amended) or a "local authority" within the meaning of section 235(1) of the Local Government (Scotland) Act 1973;

"Memorandum of Association" — the Memorandum of Association of MMI from time to time;

"Mentally Disordered"	in relation to the Scheme Administrator, the Deputy Scheme Administrator, a Committee Member, a Nominated Representative, the PPB Representative or the PPB Alternate, where such person becomes mentally disordered and either is admitted to hospital in pursuance of an application for admission for treatment under the Mental Health Act 1983 or, in Scotland, an application for admission under the Mental Health (Scotland) Act 1960 or an order is made by a Court having jurisdiction in matters concerning mental disorder for his detention or the appointment of a receiver or other person to exercise power over his affairs;
"MGI"	Municipal General Insurance Limited (incorporated in England and Wales under the Companies Act 1948 as a company limited by shares on 14th March, 1977 with registered number 1302575);
"MMI"	Municipal Mutual Insurance Limited (incorporated in England and Wales under the Companies Acts 1862 to 1900 as a company limited by guarantee on 13th March, 1903 with registered number 76678);
"Nominated Representative"	shall have the meaning given in Clause 10.4.1;
"Payment Percentage"	the percentage of each Established Scheme Liability payable by MMI to Scheme Creditors in accordance with the provisions of Part 5;
"Personal Creditor"	a creditor of MMI in respect of a Liability under or arising out of any Insurance Contract who or which is:— (a) an individual, or (b) a partnership in respect of which some or all of the partners are individuals, or (c) an unincorporated body of persons all of whom are individuals;
"Policyholders Protection Act"	the Policyholders Protection Act 1975, as amended and in force on the date of this document;
"PPB"	the Policyholders Protection Board, established by the Policyholders Protection Act;
"PPB Liability"	any Liability of MMI to the PPB arising by virtue of Clause 6.1.7 in consequence of payment being made by the PPB to MMI pursuant to Clause 6.1.2;
"PPB Secretary"	the Secretary for the time being of the PPB;
"Protected Compulsory Liability"	a Protected Liability in respect of which the PPB would owe a duty under section 6(4) or 7 of the Policyholders Protection Act;
"Protected Creditor"	in relation to a Protected Liability, any person to whom such Protected Liability is due and who, in addition, is eligible for protection under section 16(9) of the Policyholders Protection Act;

"Protected Liability"	an Established Liability of MMI in respect of which (and to the extent to which) the PPB would owe a duty under section 6, 7 or 8, as the case may be, of the Policyholders Protection Act if MMI were a "company in liquidation" and the Trigger Date were the "beginning of the liquidation", in each case within the meaning of the Policyholders Protection Act, and references in those sections to the amount of any liability were references to the amount as established in the case of an Established Liability (and, for the avoidance of doubt but without limitation, where such a duty would only be owed under that Act in respect of a liability towards a "private policyholder" or under the terms of a "United Kingdom policy", as those expressions are respectively defined in that Act, or a liability of some other description, only an Established Liability which is also such a liability shall be capable of qualifying as a Protected Liability);
"Protected Non-compulsory Liability	a Protected Liability in respect of which the PPB would owe a duty under section 6(6) or 8 of the Policyholders Protection Act;
"Record Date"	30th September, 1993;
"Reimbursement Percentage"	means the figure expressed as a percentage (i) in the case of payments in discharge of Protected Compulsory Liabilities, equal to 100 minus the Payment Percentage and (ii) in the case of payments in discharge of Protected Non-compulsory Liabilities, equal to 90 minus the Payment Percentage (or, if the Payment Percentage is greater than 90, zero);
"Reported Scheme Liability"	a Scheme Liability reported to MMI and recorded in its books at the close of business on the Record Date which had not yet become an Established Scheme Liability;
"Review Date"	31st December of each year (commencing on 31st December, 1994);
"Scheme"	this scheme of arrangement in its present form or as modified in accordance with Clause 2.5.1;
"Scheme Administrator"	the person whose name is set out in Clause 1.3.2.1 or such other person as may be appointed as the Scheme Administrator in accordance with the provisions of the Scheme;
"Scheme Assets"	all the assets of MMI (excluding assets held on trust by MMI to the extent that MMI has no beneficial interest in such assets);
"Scheme Creditor"	a creditor which has become a Scheme Creditor in accordance with Clause 2.3;
"Scheme Liability"	any Liability of MMI under or arising out of any Insurance Contract being a Liability (other than an Excluded Liability) to which MMI was subject on the Record Date or to which MMI has or may become subject after the Record Date by reason of an obligation assumed by MMI before the Record Date;
"Secretary"	the Secretary for the time being of the Creditors' Committee;

"Security Interest"	any mortgage, charge, lien, assignment by way of security or other security interest (other than an assignment to, or other security interest of, the PPB);
"Sterling" and the sign "£"	pounds sterling or any other lawful currency from time to time of the United Kingdom;
"Termination Date"	the date on which the Scheme ceases to have effect in accordance with Clause 12.1;
"Trading Day"	a day (other than a Saturday or Sunday) on which the clearing banks in London are open for foreign currency business in relation to Sterling and the relevant currency to be converted into Sterling;
"Trigger Date"	the first date on which any Trigger Event occurs;
"Trigger Event"	the occasion when the Directors give written notice to MMI and to the Scheme Administrator that:— (a) the Directors have concluded that, without the occurrence of a Trigger Event and the operation of the Scheme in accordance with its terms thereafter, there is no reasonable prospect that MMI will avoid going into insolvent liquidation, or (b) the number of Directors has fallen, and remained for seven days, below two; and
"Voting Creditor"	each Scheme Creditor and the PPB.

1.2 **Interpretation**

1.2.1 Part and Clause headings and the table of contents are for ease of reference only and shall not affect the interpretation of the Scheme.

1.2.2 In the Scheme, unless the context otherwise requires or unless otherwise expressly provided for:—

(a) references to Parts and Clauses are to be respectively construed as references to the parts and the clauses of the Scheme;

(b) references to (or to any specified provision of) the Scheme shall be construed as references to the Scheme (or that provision) as in force for the time being and as modified in accordance with the terms of the Scheme;

(c) the singular includes the plural and vice versa;

(d) words denoting any gender include all genders;

(e) subject, and without prejudice, to the definitions of "Protected Liability" and "Protected Creditor", references to a person shall be construed as including references to an individual, firm, partnership, company, corporation, unincorporated body of persons or any State or any agency thereof; and

(f) references to any statute or statutory provision include the same as re-enacted, amended or extended.

1.3 **Parties other than MMI and the Scheme Creditors**

1.3.1 **The PPB**

The PPB has agreed with MMI to appear by Counsel on the hearing of the petition to sanction the Scheme and to undertake to the Court to be bound thereby and to execute or do, or procure to be executed or done, all such documents, acts or things as may be necessary or as the Court may consider desirable to be executed or done by it or on its behalf for the purpose of giving effect to the Scheme and, subject to the Scheme becoming effective, to be bound thereby.

1.3.2 **The initial Scheme Administrator and initial Deputy Scheme Administrator**

1.3.2.1 The initial Scheme Administrator shall be Gareth Howard Hughes, who has given and has not withdrawn his consent to act as Scheme Administrator from the Effective Date.

1.3.2.2 The initial Deputy Scheme Administrator shall be Nigel James Hamilton, who has given and has not withdrawn his consent to act as Deputy Scheme Administrator from the Effective Date.

1.3.3 **The Current Directors**

Each of the persons whose name is set out below is a Current Director of MMI:—

(a) Maurice Stonefrost
(b) Sir John Lovill
(c) Philip Gregory
(d) John Barber
(e) Allan Castle
(f) Stuart Errington
(g) Illtyd Harrington
(h) Sir Peter Harrop
(i) Lord Merlyn-Rees
(j) Sir David Montgomery
(k) John Morgan
(l) Joe Small

1.3.4 **The Creditors' Committee**

Subject, in the case of (a) to (h) below, to each of the proposed Committee Members obtaining the necessary internal authorisation for it to become a Committee Member, each of the individuals whose name is set out below has given and has not withdrawn his consent to serve as the Nominated Representative of the Committee Member under whose name he is listed (or, in the case of the PPB, as the PPB Representative):-

(a) Gateshead Metropolitan Borough Council
Civic Centre
Regent Street
Gateshead NE8 1HH
Nominated Representative: Michael Bernard Shaw

(b) Hertfordshire County Council
County Hall
Hertford SG13 8DE
Nominated Representative: William John Church

(c) London Borough of Wandsworth
The Town Hall
Wandsworth High Street
London SW18 2DU
Nominated Representative: Martin Barry Ashton Walker

(d) Lothian Regional Council
Regional Headquarters
George IV Bridge
Edinburgh EH1 1QU
Nominated Representative: David Newlands

(e) Nottinghamshire County Council
County Hall
West Bridgford
Nottingham NG2 7QP
Nominated Representative: William James Sulman

(f) Rochester upon Medway District Council
The Civic Centre
Strood
Rochester
Kent ME2 4AW
Nominated Representative: Bernard Graham Clarke

(g) Strathclyde Regional Council
Strathclyde House
20 India Street
Glasgow G2 4PF
Nominated Representative: Stephen Geoffrey Singleton

(h) Leicestershire County Council
County Hall
Glenfield
Leicester LE3 8RP
Nominated Representative: Timothy Harrison

(i) The Policyholders Protection Board
51 Gresham Street
London EC2V 7HQ
PPB Representative: Deryck Wright

(j) National Federation of Housing Associations
175 Gray's Inn Road
London WC1X 8UP
Nominated Representative: Christopher James Cantwell

PART 2

GENERAL

2.1 **Application of the Scheme**

The Scheme shall apply to each creditor of MMI which becomes a Scheme Creditor in accordance with Clause 2.3 and shall apply in respect of all Scheme Liabilities to such Scheme Creditor, including all Scheme Liabilities which do not become Established Scheme Liabilities until after the Record Date.

2.2 **Established Scheme Liabilities**

2.2.1 Subject to Clauses 2.2.2, 4.2, 4.7.1(a)(ii) and 4.8, a Scheme Liability shall be an Established Scheme Liability for the purposes of the Scheme when there has been established (whether before, on or after the Record Date and whether (i) by agreement or (ii) by any arbitration (insofar as the same is provided for under the terms of the Insurance Contract giving rise to the Scheme Liability) or any judicial action or proceeding which is not the subject of any appeal) in relation thereto an obligation on the part of MMI to pay an ascertained sum of money at that time after account has been taken (whether (i) by agreement or (ii) by any arbitration or judicial action or proceeding as aforesaid) of:—

(a) any Security Interest over the assets of MMI which the creditor concerned is entitled to enforce in accordance with Clause 4.4.1(a);

(b) any letter of credit or trust issued or created by or in respect of MMI which the creditor concerned is entitled to enforce in accordance with Clause 4.4.1(b);

(c) any effective right of set-off or cross-claim which may be taken into account in accordance with Clause 4.5;

in each case to the extent not already taken account of in relation to any other Scheme Liability pursuant to this Clause, and

(d) any amount which has been recovered by MMI in respect of the Scheme Liability directly or indirectly from a co-insurer or other third party.

2.2.2 For the purposes of the Scheme, the amount of an Established Scheme Liability shall be the amount at which it is or has been established in accordance with Clause 2.2.1 notwithstanding any payment in respect thereof which has been made (or is treated as having been made) since the Record Date.

2.3 **Scheme Creditors**

2.3.1 Subject to Clauses 2.3.2 to 2.3.6, a creditor shall be a Scheme Creditor (and be bound by the Scheme accordingly) if both:—

(a) as at the close of business on the Record Date there were recorded in the books of MMI:—

(i) Scheme Liabilities due to such creditor which had become Established Scheme Liabilities but had not yet been paid; and/or

(ii) Reported Scheme Liabilities reported by such creditor which had not yet become Established Scheme Liabilities but on which an Estimated Value had been placed by MMI

of an aggregate amount and/or Estimated Value equal to or more than £25,000; and

(b) the aggregate amount of Scheme Liabilities to such creditor which are or have become Established Scheme Liabilities, within the meaning of Clause 2.2.1, (together with the aggregate amount of any Elective Defence Costs paid by MMI on its behalf) exceeds £50,000.

2.3.2 A creditor shall be a Scheme Creditor pursuant to Clause 2.3.1 (and be bound by the Scheme accordingly) regardless of the point in time at which it becomes a Scheme Creditor in accordance with Clause 2.3.1.

2.3.3 In determining whether a creditor is a Scheme Creditor:—

(a) account shall be taken of all Scheme Liabilities due to such creditor which are or have become Established Scheme Liabilities within the meaning of Clause 2.2.1 notwithstanding any payment which has been made (or is treated as having been made) in respect of such Scheme Liabilities since the Record Date;

(b) no account shall be taken of any Assignment effected on or after the Record Date of the whole or any part of any Scheme Liability and, accordingly, for the purposes of Clause 2.3.1 the aggregate amount of Scheme Liabilities due to any person at any time shall include both the amounts of Scheme Liabilities due to such person at such time and all amounts of Scheme Liabilities due to persons to whom such Scheme Liabilities have been Assigned by such person on or after the Record Date and the payments in respect of Established Liabilities which will be deemed for the purposes of the Scheme as having been made (or treated as having been made) to such person shall be the aggregate of such payments received (or treated as having been received) by such person and its Assignees.

2.3.4 In determining whether any person (a "successor") to whom an interest in an Insurance Contract (the "Transferred Insurance Contract") has been transferred on or after the Record Date pursuant to any statute, statutory instrument, order or other legislation or subordinate legislation is a Scheme Creditor, account shall be taken of the aggregate amount of all Scheme Liabilities (whether or not under or arising out of the Transferred Insurance Contract) due to the person which transferred such interest (the "transferor"), being Scheme Liabilities which either are Established Scheme Liabilities or have become Established Scheme Liabilities before such transfer is effected, as if such Scheme Liabilities were due to the successor at the time when they became Established Scheme Liabilities together with the aggregate amount of any Elective Defence Costs paid by MMI on behalf of the transferor before such transfer is effected.

2.3.5 For the purposes of Clause 2.3.3 and Clause 2.3.4, no account of the amount of any particular Scheme Liability or Elective Defence Costs shall be taken more than once.

2.3.6 If there is any dispute as to the person to whom any Scheme Liability is or was due or as to the person to whom any Scheme Liability for the purposes of Clause 2.3 is or was to be treated as being due, the question shall be referred to the Scheme Administrator whose decision shall be final. In making his decision, the Scheme Administrator shall obtain such professional advice and consult such relevant experts as he may, in his discretion, think fit and shall act as expert and not as arbitrator.

2.4 Effective Date

2.4.1 The Scheme shall become effective as soon as an office copy of the Court Order shall have been delivered for registration to the Registrar of Companies as provided in section 425(3) of the Act.

Unless the Scheme has become effective on or before 30th April, 1994 or such later date, if any, as the Court may allow, it shall never become effective.

2.5 Modification of the Scheme

2.5.1 Subject to Clause 2.5.2, MMI may consent on behalf of all those concerned at any hearing of the petition to sanction the Scheme in accordance with section 425 of the Act to any modification of, or addition to, the Scheme or any term or condition which the Court may think fit to approve or impose.

2.5.2 Any modification, addition, term or condition as is referred to in Clause 2.5.1 which, in the opinion of the PPB, would directly or indirectly adversely affect the interest of the PPB in the Scheme shall not take effect unless approved by the PPB.

PART 3

THE SCHEME PERIODS

3.1 **During the Initial Scheme Period:—**

3.1.1 All Liabilities of MMI shall be payable in the ordinary course of business as and when they fall due.

3.1.2 Subject as provided in Clauses 7.1 and 7.2, the management and control of the business and affairs of MMI shall be carried on by the Directors.

3.1.3 The Directors shall be subject to the restrictions and duties contained in Clauses 6.3, 7.1, 7.2, 7.4, 9.1.1, 9.1.4, 9.1.6 and 9.1.7, as the case may be.

3.1.4 The powers and duties of the Scheme Administrator shall be as referred to or set out in Clause 8.2.

3.2 **During the Levy Period:—**

3.2.1 All Liabilities of MMI other than Scheme Liabilities to Scheme Creditors shall continue to be payable in the ordinary course of business as and when they fall due.

3.2.2 The rights of Scheme Creditors in relation to Scheme Liabilities shall be modified in the manner provided in Part 4.

3.2.3 Scheme Creditors shall be subject to the Levy provided for in Part 5.

3.2.4 The rights of Scheme Creditors to receive further payments in respect of Scheme Liabilities shall be as provided in Part 5.

3.2.5 The PPB shall be obliged to make payments to MMI in accordance with Part 6.

3.2.6 The Directors shall be subject to the restrictions contained in Clauses 7.1, 7.3, 9.1.1 to 9.1.3 and 9.1.7.

3.2.7 The powers and duties of the Scheme Administrator shall be as set out in Clauses 4.1, 4.6, 4.7, 4.9.2, Part 5, 6.1.4, 6.3, 7.3, 8.3 to 8.5, 9.1.3, 9.1.5, 9.2, 10.7.3, 10.7.4 and Part 11.

PART 4

RIGHTS OF SCHEME CREDITORS IN RELATION TO SCHEME LIABILITIES DURING THE LEVY PERIOD

4.1 **Application of this Part**

As from the commencement of the Levy Period (but not before):—

(a) the rights of Scheme Creditors in relation to Scheme Liabilities shall be modified in the manner provided for in this Part of the Scheme; and

(b) the Scheme Administrator shall have the powers conferred upon him by this Part of the Scheme.

4.2 **Enforcement of Scheme Liabilities**

4.2.1 No payment shall be made to a Scheme Creditor in respect of a Scheme Liability otherwise than in accordance with the Scheme.

4.2.2 Except to the extent that MMI has failed to perform any obligation under the provisions of the Scheme to make a payment in respect of a Scheme Liability to a Scheme Creditor and subject to the rights of Scheme Creditors under Clauses 4.4 and 4.5, no Scheme Creditor shall be entitled during the Levy Period to take any step or proceeding against MMI or its property (whether by way of demand, legal proceedings, execution of judgment, arbitration proceedings or otherwise howsoever) in any jurisdiction whatsoever for the purpose of obtaining payment of any Scheme Liability or any part thereof.

4.2.3 Nothing in the Scheme shall preclude any person from taking appropriate action for the purpose of securing a determination of the question whether MMI is liable in respect of any Scheme Liability and, if so, the amount of such Scheme Liability or otherwise for the purpose of enforcing the terms of the Scheme.

4.3 **Effect of acts prohibited by Clause 4.2.2**

4.3.1 If any Scheme Creditor takes any such action as is prohibited by Clause 4.2.2 it shall be treated for the purposes of the Scheme as having received, on account of its entitlement under Part 5 of the Scheme, a payment under the Scheme equal to the amount or gross value of any money, property, benefit or advantage obtained by it at the expense of MMI as the result of such action and the extent, if any, to which it is entitled to any payment under the Scheme shall be reduced accordingly.

For the purpose of Clause 4.3.1, the gross value of any such property, benefit or advantage shall be conclusively determined by the Scheme Administrator and, without limitation, may include such amount as the Scheme Administrator may consider to be appropriate by way of interest or costs, charges or expenses incurred by MMI as a consequence thereof.

4.4 **Security, letters of credit and trusts**

4.4.1 Nothing in the Scheme shall affect the right of any Scheme Creditor to take any appropriate action to enforce:—

(a) any Security Interest over the assets of MMI which could have been enforced if MMI were being wound up and the order that MMI be wound up had been made on the Trigger Date or which has been created after the Trigger Date in accordance with Clause 7.3.1; or

(b) any letter of credit or trust issued or created (expressly, by implication or by operation of law) by or in respect of MMI and of which such Scheme Creditor is a beneficiary, if such letter of credit or trust was issued or created before the Trigger Date or has been issued or created after the Trigger Date in accordance with Clause 7.3.1.

Nothing in the Scheme shall affect the rights of MMI against any person in respect of any wrongful drawdown or enforcement of any letter of credit or trust issued or created by or in respect of MMI.

4.5 **Set-off**

4.5.1 Subject to Clause 4.5.2, a Scheme Creditor which is under a liability to MMI may, in relation to MMI, rely on any set-off or cross-claim upon which it could have relied if MMI were being wound up and the order that MMI be wound up had been made on the Trigger Date.

4.5.2 For the avoidance of doubt:—

(a) no Scheme Liability which has been Assigned to a person on or after the Trigger Date may be applied in extinguishing or reducing any liability of that person to MMI; and

(b) no liability of a Scheme Creditor to MMI which arises out of an obligation incurred by such Scheme Creditor on or after the Trigger Date may be extinguished or reduced by any Scheme Liability which is due to such Scheme Creditor.

4.6 **Election to Defend Decisions and Elective Defence Costs**

4.6.1 The Scheme Administrator may, if he considers that to do so would be in the best interests of Scheme Creditors, from time to time decide to make an Election to Defend Decision and to pay the Elective Defence Costs.

4.6.2 If, in connection with any Insurance Contract, at any time since the Record Date MMI has paid or agreement has been reached for MMI to pay Elective Defence Costs the following provisions shall apply to limit (but not to increase) the amount payable to the relevant Scheme Creditor under the Scheme in respect of any Established Scheme Liability under or arising out of such Insurance Contract:—

(a) the Scheme Administrator shall calculate:—

(i) the amount which would have been payable by MMI under the Scheme calculated pursuant to Part 5;

(ii) the aggregate of:—

(A) the amount of that Established Scheme Liability; and

(B) the amount of the Elective Defence Costs (less any amounts received from third parties on account of such costs)

(the amount of such aggregate being the "Gross Amount");

(b) the amount payable by MMI under Clause 5.2 (calculated under Clause 4.6.2(a) above) shall not exceed the amount by which the then current Payment Percentage of the Gross Amount exceeds the amount of the Elective Defence Costs; and

(c) the amount payable by MMI under Clause 5.3.5 (calculated under Clause 4.6.2(a) above) shall not exceed the amount by which the Payment Percentage (as increased) of the Gross Amount exceeds the aggregate of:—

(i) the amount in respect of that Established Liability which has previously been paid by MMI; and

(ii) the amount of the Elective Defence Costs.

4.6.3 Where the total amount of the Elective Defence Costs paid exceeds the maximum amount recoverable under the aforementioned Insurance Contract the following shall apply:—

(a) the Established Scheme Liability, in respect of which such payments were made by MMI, will be deemed to have been paid in full under the Scheme and the Scheme Creditor shall not be entitled to any further payments under the Scheme in respect of that Established Scheme Liability; and

(b) the amount by which the Elective Defence Costs exceed the maximum amount recoverable under the Insurance Contract will not be recoverable by MMI from the Scheme Creditor.

4.6.4 Notwithstanding the fact that the Scheme Administrator has made an Election to Defend Decision and MMI has paid or agreement has been reached for MMI to pay Elective Defence Costs, the Scheme Administrator may also, if he

considers that to do so would be in the best interests of the Scheme Creditors from time to time decide to revoke such Election to Defend Decision. If the Scheme Administrator decides to revoke an Election to Defend Decision:—

(a) MMI shall not be responsible for the costs involved in defending the claim which are incurred after the decision to revoke the Election to Defend Decision has been made by the Scheme Administrator;

(b) MMI will remain liable to the lawyer or other adviser or representative for the Elective Defence Costs incurred before, and outstanding to be paid at, the time when the decision to revoke the Election to Defend Decision has been made by the Scheme Administrator and the lawyer or other adviser or representative receives (or is deemed to have received) written notice from MMI of the termination of his instructions; and

(c) MMI shall give written notice to the Scheme Creditor affected of the Scheme Administrator's decision to revoke the Election to Defend Decision as soon as practicable thereafter and shall notify the Scheme Creditor of the effect of such decision.

4.6.5 Any notice delivered by MMI pursuant to Clause 4.6.4 shall be deemed to have been received by the intended recipient two days after the time when it is posted by MMI addressed to the last known address of the intended recipient.

4.7 **Commutations and other arrangements**

4.7.1 Subject to Clause 4.7.2, MMI may:—

(a) enter into:—

(i) Commutations, and

(ii) contractual arrangements (not being Insurance Contracts) with creditors under which all or a part of the total Liability of MMI to the relevant creditor under an Insurance Contract becomes an Established Liability otherwise than as a result of an obligation to pay an ascertained sum of money being established in the normal course

provided that such Commutations and arrangements include terms to the effect that no other claim may be made in respect of the Liability, or that part of the Liability, which is the subject of the relevant Commutation or arrangement; and

(b) enter into contractual arrangements (not being Insurance Contracts) with any of its reinsurers for the discharge in full of any of such reinsurer's liabilities to MMI under reinsurance contracts in consideration for a cash payment to MMI,

provided that the Scheme Administrator considers that to do so would be in the best interests of Voting Creditors (excluding, in the case of Commutations and contractual arrangements entered into pursuant to Clause 4.7.1(a) above with a Scheme Creditor, the Scheme Creditor with whom such Commutation or contractual arrangements are made).

4.7.2 No such Commutation or arrangement as is referred to in Clause 4.7.1(a) shall be entered into unless:—

(a) the Scheme Administrator (having taken advice from actuaries if he considers it appropriate) is satisfied that such Commutation or arrangement will reduce the net Liabilities of MMI;

(b) the Commutation or arrangement will not adversely affect or prejudice MMI's rights under any reinsurance contract, where relevant; and

(c) (except in circumstances in which the creditor concerned has confirmed, in a legally binding form to the reasonable satisfaction of the PPB, that it is not a Protected Creditor in respect of the Liability concerned or that it waives any rights which it may have against the PPB in respect of that Liability and agrees to the discharge of that Liability) the PPB has consented in writing to the Commutation or arrangement.

Without prejudice to Clauses 4.7.1 and 4.7.2, the Scheme Administrator shall consider any request made by a Scheme Creditor, supported by appropriate

actuarial information, for MMI to enter into any such Commutation or contractual arrangements as are referred to in Clause 4.7.1 with such Scheme Creditor.

4.8 **Admissible Interest**

4.8.1 For the purpose of paying or providing for payments under the Scheme, there shall not be included as part of an Established Scheme Liability any interest except interest (hereinafter called "admissible interest") to which a Scheme Creditor is entitled by reason of contract, judgment against MMI, decree or otherwise for a period or periods ending on or before the Trigger Date.

4.8.2 No payment shall be made under the Scheme in respect of any part of an Established Scheme Liability which comprises interest which is not admissible interest.

4.8.3 As from the Trigger Date, MMI shall be discharged from all Liabilities in respect of interest on or in relation to Scheme Liabilities which is not admissible interest.

4.9 **Currency of payment**

4.9.1 Any amount payable to a Scheme Creditor under the Scheme in respect of an Established Scheme Liability due to such Scheme Creditor shall be paid in the currency in which such Established Scheme Liability was incurred (or, where the relevant Insurance Contract allows such Scheme Creditor to elect to make a claim or claims in any other currency and any such election is made in accordance with the terms of such Insurance Contract (but not after an amount in respect of such Established Scheme Liability has already been paid under the Scheme), in that currency).

4.9.2 In determining any set-off or cross-claim in relation to an Established Scheme Liability due to a Scheme Creditor, where the set-off or cross-claim is expressed in a currency other than that of the relevant Established Scheme Liability, the set-off or cross-claim shall, in the absence of agreement otherwise between the Scheme Creditor and MMI, be converted into the currency of the relevant Established Scheme Liability at the rate of exchange specified in the Insurance Contract to which the Established Scheme Liability relates or, if there is no such rate specified, the rate of exchange published in the *Financial Times* for the purchase of such currency at close of business (London time) on the date upon which the Scheme Administrator accepts that the set-off or cross-claim is available to the relevant Scheme Creditor or the set-off or cross-claim is otherwise determined or, if no such rate is published in the *Financial Times* in respect of that currency on that date, the mid-market rate for that currency on such date quoted by National Westminster Bank Plc or, if no such rate is so published or quoted, such rate as may reasonably be determined by the Scheme Administrator.

PART 5

PAYMENTS DURING THE LEVY PERIOD

5.1 Imposition of a Levy

5.1.1 As soon as practicable, and in any event within 90 days, after the occurrence of a Trigger Event, the Scheme Administrator shall complete a review of the assets and liabilities of MMI as at the Trigger Date in accordance with Clause 5.4 and, following such review, a Levy may be imposed in accordance with Clause 5.5 at a rate determined in accordance with Clause 5.4 on all those Scheme Creditors which, at the Levy Notice Date, have been paid (or are treated as having been paid) since the Record Date an amount or amounts in respect of Established Scheme Liabilities which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf since the Record Date, exceed £50,000 in aggregate.

5.1.2 Any Levy imposed on a Scheme Creditor pursuant to Clause 5.1.1 or, as the case may be, Clause 5.3.3 shall be imposed in respect of amounts paid (or treated as having been paid) since the Record Date to or on behalf of such Scheme Creditor in respect of Established Scheme Liabilities or Elective Defence Costs in excess of the first £50,000. No Levy shall be imposed on any Scheme Creditor in respect of the first £50,000 so paid (or treated as having been so paid) to or on behalf of such Scheme Creditor.

5.1.3 In determining the aggregate amount paid (or treated as having been paid) since the Record Date in respect of Established Scheme Liabilities to, or in respect of Elective Defence Costs on behalf of, a Scheme Creditor (a "Successor Scheme Creditor") to whom an interest in an Insurance Contract has been transferred on or after the Record Date pursuant to any statute, statutory instrument, order or other legislation or subordinate legislation, the Successor Scheme Creditor shall be treated as having been paid (in addition to any other amount paid (or treated as having been paid) to or on behalf of such Successor Scheme Creditor in respect of Established Scheme Liabilities or Elective Defence Costs respectively since the Record Date) an amount equal to the aggregate amount paid (or treated as having been paid) since the Record Date in respect of Established Scheme Liabilities or Elective Defence Costs respectively to or on behalf of the person which transferred such interest (the "Transferor").

5.1.4 Without prejudice, and in addition, to any other liability it may have under the provisions of this Part, each Successor Scheme Creditor shall be liable to any Levy imposed under Clause 5.1.1 or, as the case may be, Clause 5.3.3 in respect of any amount treated under Clause 5.1.3 as having been paid to it and, in respect of any particular Transferor, if there are more than one Successor Scheme Creditors they shall be jointly and severally liable for such Levy.

5.2 Payment subject to application of the Payment Percentage

Except for any payment made pursuant to Clause 5.3.5 or Clause 5.6, any payment made on or after the first Levy Notice Date in respect of an Established Scheme Liability due to a Scheme Creditor to which, by, on or subsequent to such Levy Notice Date (and including such payment), there has been paid (or there is treated as having been paid) an aggregate amount in excess of £50,000 since the Record Date in respect of Established Scheme Liabilities or Elective Defence Costs shall, to the extent that such payment when aggregated with other such payments since the Record Date exceeds £50,000 and subject to Clauses 4.3.1 and 5.8.1, be made at the rate of the Payment Percentage prevailing in accordance with this Part of the Scheme.

5.3 Adjustments to the rate of Levy and the Payment Percentage

5.3.1 As soon as practicable, and in any event within 90 days, after each Review Date, the Scheme Administrator shall complete a review of the assets and liabilities of MMI as at the Review Date in accordance with Clause 5.4.

5.3.2 In addition, but without prejudice to, Clause 5.3.1, if at any time after the first Levy Notice Date the Scheme Administrator considers, having regard to the information available to him relating to the financial position of MMI, that the then prevailing Payment Percentage is at a level which is too low or, as the case may be, too high to be in the best interests of Voting Creditors as a whole, the Scheme Administrator may carry out a review of the assets and liabilities of MMI in accordance with Clause 5.4 as at such date (the "Adjustment Date"), being later than the latest of the previous Adjustment Date (if any), the immediately preceding Review Date (if any) and the Trigger Date, as the Scheme Administrator may in his absolute discretion determine Provided that no more than two such reviews may be carried out pursuant to this Clause 5.3.2 in any calendar year and any such review shall be completed within 90 days after its commencement.

5.3.3 If, following any such review as is provided for in Clause 5.3.1 or, as the case may be, Clause 5.3.2 above and after consultation with the Creditors' Committee, the Scheme Administrator concludes that the then prevailing Payment Percentage is at a level which is too high to be in the best interests of Voting Creditors as a whole, a further Levy shall be imposed by MMI in accordance with Clause 5.5 at the rate determined in accordance with Clause 5.4 on each of those Scheme Creditors which, at the Levy Notice Date, have been paid (or are treated as having been paid) since the Record Date an amount or amounts in respect of Established Scheme Liabilities which, together with the amount of Elective Defence Costs (if any) paid by MMI on its behalf since the Record Date, exceed £50,000 in aggregate.

5.3.4 If, following any such review as is provided for in Clause 5.3.1 or, as the case may be, Clause 5.3.2 above and after consultation with the Creditors' Committee, the Scheme Administrator concludes that the then prevailing Payment Percentage is at a level which is too low to be in the best interests of Voting Creditors as a whole, the Payment Percentage may, subject to Clause 5.6.2, be increased in accordance with Clause 5.3.5 to the rate determined in accordance with Clause 5.4.

5.3.5 In the event of an increase in the Payment Percentage under Clause 5.3.4, MMI shall, as soon as reasonably practicable but in any event within 60 days after any such increase, give written notice (a "Payment Percentage Increase Notice") of such increase to those Scheme Creditors in respect of whose Established Scheme Liabilities a Levy has been imposed pursuant to Clause 5.1 or Clause 5.3.3 or which have received any payment in respect of Established Scheme Liabilities subject to application of the Payment Percentage pursuant to Clause 5.2 and to the PPB, and shall pay:—

(a) to such Scheme Creditors (without interest) an amount equal to the difference between:—

(i) the amount of the Payment Percentage, at the rate prevailing immediately following such increase, of each Established Scheme Liability which has been subject to imposition of a Levy or application of the Payment Percentage; and

(ii) the amount of the Payment Percentage, at the rate prevailing immediately prior to such increase, of each such Established Scheme Liability; and

(b) to the PPB (without interest) an amount equal to the difference between:—

(i) the amount of the Reimbursement Percentage, at the rate prevailing immediately following such increase, of each payment made by MMI after the Trigger Date in respect of each Protected Liability to which a PPB Liability relates; and

(ii) the amount of the Reimbursement Percentage, at the rate prevailing immediately prior to such increase, of each such payment.

5.4 **Determination of the rate of Levy and the Payment Percentage**

5.4.1 For the purpose of determining the rate of Levy to be imposed and/or the Payment Percentage to be applied at any time and from time to time, the Scheme Administrator shall obtain and consider such financial and/or actuarial and/or other information and advice as the Scheme Administrator shall, after consultation with the Creditors' Committee, in his discretion think fit.

5.4.2 In carrying out his review of the assets and liabilities of MMI, the Scheme Administrator shall make such provision for MMI to create such reserves as, on the basis of the information and advice referred to in Clause 5.4.1, the Scheme Administrator considers prudent, having regard to the provisions relating to the payment of Established Scheme Liabilities set out in Clause 5.2 above, to enable MMI to meet all Scheme Liabilities which as at the relevant date of review have become Established Scheme Liabilities and are still outstanding or which the Scheme Administrator considers may become Established Scheme Liabilities after such date.

5.4.3 The rate of any and every Levy (which shall be expressed as a percentage) and of the Payment Percentage shall be such as the Scheme Administrator considers will ensure that, having created the reserves referred to in Clause 5.4.2, MMI shall have sufficient Scheme Assets to meet in full all of its Liabilities other than Scheme Liabilities due to Scheme Creditors and PPB Liabilities and other than under Clause 5.6 or 5.7 as and when they fall due;

5.4.4 In considering whether, for the purposes of Clause 5.4.3, MMI has sufficient Scheme Assets, the Scheme Administrator shall be entitled to take into account:—

(a) any monies which Scheme Creditors shall be respectively liable to pay to MMI under Clause 5.1 or Clause 5.3.3 on imposition of any such Levy or further Levy;

(b) all other Scheme Assets including, without limitation, the rights of MMI against reinsurers, whether actual, prospective or contingent (and the prospects of actually successfully enforcing such rights); and

(c) the prospect of future income.

5.4.5 Subject to any increase in accordance with Clause 5.3.4, the rate of the Payment Percentage prevailing from time to time shall be equal to 100 minus the aggregate of the rate of Levy last imposed in accordance with the provisions of the Scheme and all earlier Levies (if any), expressed as a percentage.

5.4.6 Any decrease or increase in the Payment Percentage shall have effect on, and prevail from, the date of issue of the relevant Levy Notice or Payment Percentage Increase Notice respectively.

5.4.7 The Scheme Administrator may, after consultation with the Creditors' Committee, suspend payments to Scheme Creditors in respect of Established Scheme Liabilities for such periods (not exceeding three months) as he considers necessary for him to decide whether or not to impose any Levy and to reduce the Payment Percentage or to increase the Payment Percentage.

5.5 **Mechanics of imposition of Levies**

5.5.1 Notice of each Levy ("Levy Notice") shall be given by MMI in writing specifying:—

(a) the date on which the Levy Notice is issued by MMI (the "Levy Notice Date"), being the date on which such Levy Notice is sent to Scheme Creditors in accordance with Clause 5.5.2;

(b) the amount Levied on the Scheme Creditor upon whom the relevant Levy Notice is served; and

(c) the date on which payment of the Levy is to be made, being no earlier than four weeks after the specified Levy Notice Date.

5.5.2 A Levy Notice shall be served on a Scheme Creditor by sending the same by first class post to the last known address of such Scheme Creditor or to such other

address as may be notified to MMI by the relevant Scheme Creditor from time to time and shall be deemed to be served on the second day after posting.

5.5.3 A copy of each Levy Notice shall be sent to the PPB by first class post to its last known address or to such other address as may be notified to MMI by the PPB from time to time.

5.6 Repayment of amounts Levied and payment of the balance of Established Scheme Liabilities after application of the Payment Percentage

5.6.1 No repayment (in whole or in part) of any amount Levied on a Scheme Creditor or payment of the balance (or part of the balance) of any Established Scheme Liability remaining due to a Scheme Creditor after application of the Payment Percentage shall be made to the Scheme Creditor otherwise than pursuant to Clause 5.3.5 or Clause 5.6.2.

5.6.2 If, after all Scheme Liabilities have become Established Scheme Liabilities, payment in respect of all Established Scheme Liabilities due to Scheme Creditors has been made subject to imposition of any Levy and application of a Payment Percentage pursuant to the provisions of this Part 5 and all of MMI's Liabilities other than Scheme Liabilities due to Scheme Creditors and PPB Liabilities and other than under this Clause 5.6 and Clause 5.7 have been paid in full, MMI has any surplus assets, then, as soon as reasonably practicable thereafter, MMI shall pay to the PPB the PPB Liabilities and pay to Scheme Creditors the balance of Established Scheme Liabilities either unpaid to Scheme Creditors or paid but subsequently repaid to MMI by Scheme Creditors following imposition of any Levy, in all cases to the extent not previously paid or repaid by MMI pursuant to Clause 5.3.5 and without interest. If MMI does not have sufficient surplus assets to pay in full all of the outstanding PPB Liabilities and the balance of Established Scheme Liabilities due to Scheme Creditors and the amounts Levied on Scheme Creditors (to the extent not paid or repaid as aforesaid), then payment shall be made to the PPB and Scheme Creditors *pro rata* to the amounts respectively owed to them.

5.7 Commission payable to Voting Creditors

5.7.1 If all Liabilities under or arising out of an Insurance Contract have become Established Liabilities and MMI has paid in full all such Established Liabilities, all Liabilities arising under the Scheme and all other Liabilities of MMI (other than under this Clause 5.7) then the Scheme Creditors and the PPB shall be entitled to be paid the Commission in the proportions and on the basis provided below.

5.7.2 The Commission shall be payable to Scheme Creditors and to the PPB in proportion to the aggregate amounts of Established Scheme Liabilities and PPB Liabilities paid to each of them respectively since the Record Date.

5.7.3 If MMI does not have sufficient Scheme Assets, after payment in full of all Established Scheme Liabilities, all Liabilities arising under the Scheme and all other Liabilities (except for any Liability arising under this Clause 5.7), to pay to Scheme Creditors and the PPB the Commission in full, then there shall be a *pro rata* reduction in the payment of such Commission to each Scheme Creditor and the PPB.

5.8 Failure to pay a Levy and interest

5.8.1 If any Scheme Creditor fails to pay any amount of any Levy imposed on it in accordance with Clause 5.1 or, as the case may be, Clause 5.3.3 on the date specified for payment thereof in the Levy Notice served in respect thereof on such Scheme Creditor, then:-

(a) interest shall accrue on the amount of such Levy remaining outstanding after such date at the rate of 4 per cent. above the base lending rate from time to time of National Westminster Bank Plc, such interest to accrue on a daily basis; and

(b) until such Levy has been paid by the Scheme Creditor in full, such Scheme Creditor shall not under the Scheme be entitled to receive from MMI any payment in respect of any Scheme Liability.

5.8.2 No interest shall be paid by MMI either in respect of any amount repaid to MMI pursuant to Clause 5.1 or, as the case be, Clause 5.3.3 following imposition of any Levy or further Levy or in respect of any amount not paid to any Scheme Creditor by reason of the reduction in payment of any Established Scheme Liability due to such Scheme Creditor by virtue of the application of the Payment Percentage pursuant to Clause 5.2.

5.9 **Mechanics of payments**

5.9.1 All payments made by MMI to any Scheme Creditor in respect of Established Scheme Liabilities or under Clause 5.2, 5.3.5, 5.6 or 5.7 may be made:—

(a) by cheque in favour of the Scheme Creditor or as it may direct and sent through the post at the risk of the Scheme Creditor to the last known address of the Scheme Creditor or to such other address as the Scheme Creditor may from time to time notify to MMI in writing; or

(b) at MMI's option (but only if so requested by the Scheme Creditor) and at the expense of the Scheme Creditor (which expense may be deducted from the amount of the relevant payment), by telegraphic transfer to such bank account as the Scheme Creditor may from time to time notify to MMI in writing; or

(c) in such other manner as the Scheme Administrator may from time to time determine.

5.9.2 All payments made to MMI under the Scheme by Scheme Creditors shall be made:—

(a) by cheque in favour of MMI or as MMI may direct and sent through the post at the risk of the person making payment to the address for the time being of the registered office of MMI or to such other address as MMI may notify to the relevant Scheme Creditor; or

(b) at the expense of the person making payment, by telegraphic transfer to such bank account as MMI may from time to time notify to such person.

5.9.3 Payment of any cheque by the banker on whom it is drawn shall be satisfaction of the monies in respect of which it was drawn and receipt of the amount of such telegraphic transfer into such account shall be satisfaction of the monies in respect of which it was paid.

5.9.4 The Scheme Administrator may determine that any payment under the Scheme of less than a certain amount (not being greater than £50 or its equivalent in any other currency from time to time or such greater amount as the Scheme Administrator may reasonably determine from time to time (the "*de minimis* amount")) shall not be sent to a Scheme Creditor or the PPB because of the costs involved in making and/or receiving such payment, in which case any such amount shall be retained for the benefit of such Scheme Creditor or, as the case may be, the PPB, such Scheme Creditor or the PPB shall be notified by MMI of any such retention and such amount shall be paid to such Scheme Creditor or, as the case may be, the PPB upon the earlier of demand made or such time as the aggregate of sums owed to such Scheme Creditor or, as the case may be, the PPB under the Scheme exceeds the *de minimis* amount.

5.10 **Payments on termination and winding-up**

5.10.1 If the Scheme terminates in the circumstances referred to in Clause 12.1, all Liabilities of MMI (whether they are Scheme Liabilities, Liabilities arising under the Scheme (including PPB Liabilities) or otherwise) which are then outstanding shall, subject to Clause 4.8 and Clause 5.10.2, be payable (and, in the case of PPB Liabilities, shall be payable forthwith upon such termination) in full by it without being limited by reference to the Scheme.

5.10.2 The following provisions shall apply in a winding-up of MMI:—

(a) the assets of MMI shall be applied in discharge of:—

(i) first, all Liabilities of MMI to which preference is given in the winding-up of MMI by virtue of the Insolvency Act 1986;

(ii) second, all Liabilities of MMI, other than Scheme Liabilities due to Scheme Creditors and PPB Liabilities, which are proved in the winding-up of MMI; and

(iii) third, all Scheme Liabilities due to Scheme Creditors and PPB Liabilities

(and to the extent that any such Liabilities are in excess of the amount of MMI's assets, they shall be paid in the order set out in this Clause 5.10.2 and rateably within each category of Liabilities referred to above);

(b) the entitlement to dividends in the winding-up of MMI of each Scheme Creditor which has received a payment or payments under the Scheme in respect of any Established Scheme Liability shall be determined as follows:-

(i) without prejudice to the right to prove for any other amount for which it is entitled to prove, the amount of any Scheme Creditor's proof shall, if and to the extent necessary, be adjusted so that such Scheme Creditor shall be treated as having proved in the winding-up in respect of each such Established Scheme Liability for an amount equal to such Established Scheme Liability increased by any amount paid by MMI on its behalf in respect of Elective Defence Costs;

(ii) such Scheme Creditor shall be treated as having received by way of dividend in the winding-up an amount equal to the aggregate amount of payments made to it in respect of such Established Scheme Liability (less the aggregate amount (if any) repaid by it to MMI following imposition of any Levy or Levies), any amount paid by MMI on its behalf in respect of Elective Defence Costs and any amounts which it is treated as having been paid under the Scheme; and

(iii) such Scheme Creditor shall not be entitled to any further dividend in the winding-up unless and until all other Scheme Creditors proving in the winding-up have received an equivalent percentage dividend; but

(iv) subject thereto, such Scheme Creditor shall be entitled to receive dividends in the winding-up (calculated by reference to the amount for which it is treated as having proved) *pari passu* with all other Scheme Creditors and with the PPB.

PART 6

THE POLICYHOLDERS PROTECTION BOARD

6.1 Payments by the PPB

6.1.1 Save as otherwise provided in Clause 6.3, the provisions of this Part 6 shall apply if, but only if, a Trigger Event has occurred, in which event the PPB has agreed to be bound under the Scheme to make reimbursement to MMI in respect of payments made by MMI in discharge of Protected Liabilities as provided below.

6.1.2 Subject to the provisions of this Part 6, the PPB shall, after receipt of a copy of any Levy Notice pursuant to Clause 5.5.3, pay to MMI:—

(a) the Reimbursement Percentage, at the rate prevailing immediately following the issue of such Levy Notice, of all payments, to the extent that the aggregate amount of such payments exceeds £50,000 both:—

(i) which have been made by MMI after the Trigger Date but on or before the Termination Date in discharge of Protected Liabilities due to Protected Creditors; and

(ii) in respect of which there has not previously been any reimbursement by the PPB under this Clause 6.1.2; and

(b) in the event of an increase in the Reimbursement Percentage as a result of the imposition of a further Levy pursuant to Clause 5.3.3, the Increase Percentage (being the difference between the Reimbursement Percentage at the rate prevailing immediately following such increase and the Reimbursement Percentage at the rate immediately prior to such increase) of all payments both:—

(i) which have been made by MMI after the Trigger Date but on or before the Levy Notice Date relating to such further Levy in discharge of Protected Liabilities due to Protected Creditors; and

(ii) in respect of which (and to the extent to which) there has previously been reimbursement by the PPB under this Clause 6.1.2.

6.1.3 Reimbursement by the PPB in accordance with Clause 6.1.2 in respect of any Protected Liability shall be conditional on payment having been made by MMI of all amounts owed by it in respect of that Protected Liability and shall be made as soon as reasonably practicable and, in any event, no more than thirty days after whichever is the latest of:—

(a) the date on which the Scheme Administrator delivers certification to the PPB in respect of such payment pursuant to Clause 6.1.4 below;

(b) the date on which the PPB agrees or it is otherwise determined (so as to bind the PPB) that the Liability concerned is a Protected Liability;

(c) in the case of reimbursement pursuant to Clause 6.1.2(a), the first Levy Notice Date or, if later, the date which is 30 days after the Trigger Date and, in the case of reimbursement pursuant to Clause 6.1.2(b), the Levy Notice Date relating to the Levy giving rise to the obligation to make such reimbursement; and

(d) in any case where it appears to the PPB that the funds available to it fall short of what it requires to make the reimbursement in question and to meet its other responsibilities under or pursuant to the Policyholders Protection Act (as in force at any time) or otherwise, the date on which it appears to the PPB that its funds are adequate for those purposes.

6.1.4 The Scheme Administrator shall certify in writing to the PPB (having made all enquiries of MMI, Scheme Creditors or other persons necessary for the purposes of such certification) in relation to all payments made by MMI in respect of which reimbursement is claimed from the PPB pursuant to Clause 6.1.2:—

(a) the amount and date of such payment by MMI;

(b) the name and address of the person to whom such payment was made;

(c) the form of policy giving rise to the payment and the nature of the claim under it;

(d) that the person to whom or on whose behalf or at whose direction the payment was made by MMI was a Protected Creditor or some other person in whose favour the PPB would have been entitled to secure payment under the Policyholders Protection Act if MMI were a company in liquidation;

(e) that the payment was made in discharge of a Protected Liability;

(f) the proportion (if any) of the payment previously reimbursed to MMI by the PPB; and

(g) that all conditions, limitations, qualifications and other provisions referred to in Clause 6.1.9 (except for section 13(3) in its application to the Scheme) to which any reimbursement obligation of the PPB under Clause 6.1.2 is subject have been satisfied or complied with in relation to that Protected Liability

provided that such certification shall not in any respect bind the PPB or restrict it in its determination as to whether any Established Liability is a Protected Liability and provided further that no such certification need include, in relation to any such payment, details which have previously been included in certification under this Clause 6.1.4 in respect of that payment.

6.1.5 If, following receipt of certification in respect of any Liability pursuant to Clause 6.1.4, the PPB does not agree (including by virtue of not having information it considers sufficient to enable it to come to a decision) that it is a Protected Liability, the PPB shall as soon as reasonably practicable (and, in any event, within 90 days) inform the Scheme Administrator of, and its reasons for, the absence of such agreement.

6.1.6 In making its determination as to whether any Established Liability is a Protected Liability for the purposes of the Scheme the PPB shall so far as reasonably practicable interpret the definition of Protected Liability in a manner consistent, in all material respects, with that which it would adopt, in like circumstances, in determining whether any liability of a company in liquidation (within the meaning of the Policyholders Protection Act) is one in respect of which it owes a duty under section 6, 7 or 8 (as the case may be) of that Act.

6.1.7 Each payment made by the PPB to MMI in respect of a Protected Liability under Clause 6.1.2 shall give rise to a Liability of the same amount which shall constitute a debt owed by MMI to the PPB and payable in accordance with the provisions of Clauses 5.3.5, 5.6.2, 5.10.1 and 5.10.2.

6.1.8 The provisions of Clauses 5.9.2 and 5.9.3 shall apply to the making of payments to the PPB by MMI under Clauses 5.6.2 and 5.7 and this Part 6 as if references to MMI were references to the PPB and references to Scheme Creditors or the relevant Scheme Creditor were references to MMI and shall apply to the making of payments by the PPB to MMI under this Part 6 as if references to Scheme Creditors or the relevant Scheme Creditor were references to the PPB.

6.1.9 Any obligation of the PPB under this Part 6 to make a payment to MMI in respect of a Protected Liability shall be subject to the same conditions, limitations, qualifications and other provisions *(mutatis mutandis)* contained or referred to in, or capable of being imposed under, sections 9, 13(1) to (3) and 14 of the Policyholders Protection Act (disregarding for the purposes of section 14 in its application to the Scheme, but not otherwise, any payment made by MMI in respect of such Protected Liability and, for the avoidance of doubt, so that for the purposes of section 13(3) in its application to the Scheme the PPB shall be entitled to have regard both to its obligations under the Scheme and to its responsibilities otherwise than under the Scheme) as the duty which the PPB would have had under sections 6 to 8 of that Act to secure the making of a payment to any policyholder or any other person in respect of that Protected Liability if MMI had been a company in liquidation (as defined in the Policyholders Protection Act).

6.1.10 For the avoidance of doubt, the PPB shall not be liable in respect of any interest comprised in or otherwise payable in relation to a Protected Liability except to the extent that it is payable under the terms of an Insurance Contract in respect of any period or periods ending on or before the Trigger Date.

6.1.11 Subject to Clause 6.1.12, nothing in the Scheme shall impose any greater obligation on the PPB in respect of any creditor or Liability of MMI (or in relation to reimbursement of any payment by MMI in respect thereof) than it would have had if MMI had been a company in liquidation (as defined in the Policyholders Protection Act), the beginning of the liquidation (as so defined) had been the Trigger Date and, in relation to any Protected Liability, the amount in respect thereof to be paid by the PPB at any time had been no greater than the Reimbursement Percentage prevailing at that time (as reduced by any Reimbursement Percentage prevailing immediately before that Reimbursement Percentage unless the former has not resulted in reimbursement pursuant to Clause 6.1.2 in respect of such Protected Liability) of the amount of such Protected Liability; and no right of, or condition imposed by, the PPB under the Scheme in relation to reimbursement by the PPB to MMI of any payment by MMI to a Protected Creditor shall be limited or restricted by virtue of any obligation of the PPB in relation to the payment made by MMI to that Protected Creditor being less than the obligation which the PPB would have had to such Protected Creditor if MMI had been a company in liquidation (as so defined).

6.1.12 For the purpose of Clause 6.1.11 it shall be assumed that:-

(a) the currency of payment by the PPB in respect of any Liability would be the same on a liquidation of MMI as under the Scheme; and

(b) the amount of any liability of MMI on a liquidation would, in the case of an Established Liability, be the amount of that Established Liability.

6.1.13 For the avoidance of doubt, and without prejudice to the generality of Clause 6.1.11, the PPB shall have no obligation under this Part 6 to make a payment to MMI in respect of any Liability of MMI to the extent that it relates to any part of a period of cover under an Insurance Contract after the Trigger Date.

6.1.14 The PPB shall not have an obligation to make a payment in accordance with Clause 6.1.2 in respect of any Protected Liability if it appears to the PPB that such a payment would result in a material benefit being conferred on either:—

(a) any person who was a member of MMI at the date application was made to the Court under section 425 of the Act for the sanctioning of the Scheme, in his capacity as such; or

(b) any person who had any responsibility for or who may have profited from the circumstances giving rise to the financial difficulties of MMI,

provided that there shall be disregarded for the purposes of paragraphs (a) and (b) above any benefit which might accrue to such persons therein mentioned who are or who have been policyholders of MMI in their capacity as such.

6.1.15 Any obligation of the PPB to make a payment to MMI under Clause 6.1.2 shall, unless the PPB otherwise consents in any case, be conditional on (a) MMI being entitled and able to assign to the PPB all the rights and claims mentioned in Clause 6.2 free from any lien, charge, prior assignment, equity, encumbrance or other third party right and (b) without prejudice to any other rights the PPB may have against any person, there having occurred no breach by the Scheme Administrator of the terms of the Scheme (i) which has not been remedied and (ii) which materially and adversely affects the interest of the PPB in the Scheme.

6.2 Assignment to the PPB

6.2.1 Immediately upon any payment being made by the PPB to MMI in respect of a Protected Liability there shall automatically be assigned to the PPB without any further act or document (insofar as the same are capable of assignment) all rights and claims which MMI may have in respect of that Protected Liability against the Protected Creditor concerned and all rights and claims which MMI

may have against any other persons in respect of any event giving rise to that Protected Liability (whether such rights and claims arise by assignment, contract, subrogation or otherwise), in each case by way of security for the payment to the PPB by MMI of the amount of the relevant PPB Liability.

6.2.2 To the extent that the rights and claims of MMI referred to in Clause 6.2.1 shall not be capable of assignment to the PPB, then following a payment by the PPB in respect of a Protected Liability MMI shall exercise such rights and pursue such claims in accordance with directions given to it from time to time by the PPB (which shall reimburse any costs or expenses reasonably incurred by MMI as a result of such directions) and shall hold any amounts received by it attributable to such rights and claims (to the extent that such amounts do not exceed the amount of the relevant PPB Liability) on trust for, and to the order of, the PPB.

6.2.3 Without prejudice to Clause 6.2.1, following a payment by the PPB in respect of a Protected Liability, MMI shall do such acts and things and execute such deeds and documents and, in particular, such forms of assignment, transfer or assurance, as the PPB may from time to time require to vest in it fully and effectively all rights and claims of MMI against the Protected Creditor or other persons in respect of the Protected Liability to which such payment relates, or to perfect or evidence the vesting in the PPB of the same. MMI hereby irrevocably and unconditionally appoints the Chairman of the PPB for the time being to be its attorney and agent and on its behalf and in its name or otherwise to do such acts and things and execute such deeds and documents as may be required to give effect to this Clause 6.2.3, if MMI fails to comply promptly with its obligation hereunder.

6.2.4 Without prejudice to Clause 6.2.1, any obligation of the PPB to reimburse MMI under Clause 6.1.2 in respect of a Protected Liability shall, if the PPB so elects, be conditional on there first being assigned to it, in such form as it may request, all such rights and claims as are mentioned in Clause 6.2.1 (but as if the references there to Protected Creditor or to Protected Liability were references to the Protected Creditor or Protected Liability in respect of whom or which the election is made) or such of those rights and claims as the PPB may determine. Where any such obligation is so conditional, Clause 6.1.3 shall apply as if after Clause 6.1.3(d) there were added "; and (e) the date when the condition imposed under Clause 6.2.4 is satisfied." and the word "and" were deleted from the end of Clause 6.1.3(c).

6.2.5 A PPB Liability shall be reduced by any amount (net of costs and expenses) recovered by the PPB from a Protected Creditor or other person pursuant to Clause 6.2.1 to 6.2.3 above in respect of the Protected Liability payment in respect of which by the PPB gave rise to such PPB Liability.

6.2.6 As soon as reasonably practicable after discharge in full of any PPB Liability, the PPB shall re-assign (at MMI's cost and expense) to MMI all rights and claims against the Protected Creditor concerned or other persons in relation to the Protected Liability in connection with which such PPB Liability arose which may have been assigned to the PPB pursuant to Clause 6.2.1 to the extent that such rights and claims have not already been exercised or enforced.

6.3 **Information to be provided to the PPB**

6.3.1 Each of MMI and the Scheme Administrator shall promptly provide the PPB with all such information in their respective possession or under their respective control or the possession or control of their respective agents (as the case may be) as the PPB may from time to time request:—

(a) during the Levy Period, in order to establish whether (or the extent to which):-

(i) any Established Liability is a Protected Liability, or

(ii) any person is a Protected Creditor, or

(iii) any payment has been made by MMI in respect of a Protected Liability; or

(b) after the Effective Date and before the Termination Date, otherwise for the purpose of enabling or assisting the PPB to perform its obligations or exercise its rights under the Scheme or to carry out its functions or responsibilities under the Policyholders Protection Act as in force from time to time.

MMI shall also, so far as it is able, authorise and instruct any third party with any such information as is referred to in this Clause 6.3.1 to disclose it to the PPB on the PPB making any such request as is referred to in this Clause 6.3.1. The PPB shall pay the reasonable costs of MMI, the Scheme Administrator and their respective agents and such third parties in providing such information provided that MMI shall pay the costs of providing so much of such information as would normally be requested of a creditor by the PPB by means of a questionnaire for the purpose of determining whether he is eligible for protection under the Policyholders Protection Act as in force from time to time.

6.3.2 The obligations set out in Clause 6.3.1 and Clause 7.4 (other than under paragraphs (a) to (e) thereof) shall not extend to any information which MMI or, as the case may be, the Scheme Administrator are under a legal duty not to disclose but, after the Effective Date, neither MMI nor the Scheme Administrator shall, without the prior written consent of the PPB, enter into any agreement or incur any obligation which precludes or restricts disclosure to the PPB of any such information as is reasonably capable of being the subject of a request under Clause 6.3.1 or, as the case may be, Clause 7.4.

6.3.3 Subject to receiving reasonable notice in any case, MMI shall, for the purposes referred to in Clause 6.3.1, permit (and, so far as it is able, authorise and instruct its agents to permit) any person authorised by the PPB to have access to, and to be provided with copies of, all or any of the books and records of MMI and, in so far as they relate to MMI, of such agents, during normal business hours. Such obligation shall not extend to any such information which MMI or any such agent is under a legal duty not to disclose. The PPB shall pay the reasonable costs of providing such copies.

6.3.4 The PPB may, at any time when the Scheme Administrator is not exercising general powers of management pursuant to Clause 8.3, require such of the Chairman and Controllers of MMI as it may nominate to attend a meeting with a member or members of the PPB or with its professional advisers for the purpose of discussing the conduct of the management of MMI and its business and affairs and the Chairman and Controllers so nominated shall co-operate fully with the PPB and its advisers in responding to such questions as may be put to them at such a meeting.

PART 7

CARRYING ON OF INSURANCE BUSINESS

7.1 Restrictions on MMI from the Effective Date

7.1.1 Save as provided below, MMI shall not from the Effective Date until the Termination Date:—

(a) enter into any further insurance or reinsurance contracts, or renew, replace or extend any existing Insurance Contract or vary the same in a manner which would increase the total amount of any Liability of MMI to any person under such contract except, with the consent of the Scheme Administrator if a Trigger Event has occurred, (i) contracts of insurance protecting MMI or its Directors, officers, employees or agents against usual business risks and (ii) contracts of reinsurance in relation to Liabilities to which MMI is subject on the Effective Date;

(b) carry on any business except in connection with, and for the purpose of carrying out, the Scheme and all other matters which are incidental thereto (for which purpose MMI may, in particular, carry on the management and, subject to Clause 7.2, disposal or development of property held by it at the Effective Date); or

(c) save as provided in Clauses 6.2.2, 7.3.1 and 7.3.2, create or cause or permit to be created, any trust of or in relation to any Scheme Asset (including, without limitation, any cash deposit) or appropriate or set aside any Scheme Asset to meet any of its Liabilities (otherwise than in accordance with the terms of the Scheme or in circumstances where such trust, appropriation or setting aside is created or made in connection with the establishment of any escrow arrangement or the deferral of payment of consideration in connection with a disposal of any asset by MMI on arms' length commercial terms).

Nothing in this Clause 7.1.1 shall prohibit the transfer to MMI of liabilities which have arisen or which may arise under or out of any treaty or contract of insurance or reinsurance of any kind whatsoever which was entered into by MGI as insurer or inward reinsurer or the creation of any trust of or in relation to any Scheme Asset in connection therewith provided that the prior written consent of the Scheme Administrator and the PPB to such transfer or trust (as the case may be) has been obtained.

7.1.2 Neither MMI nor the Scheme Administrator shall apply to the Court (and the Directors and the Scheme Administrator shall procure so far as they are respectively able that MMI shall not so apply) for any determination in relation to the interpretation or construction of any provision of the Policyholders Protection Act (as in force at any time) whether as such or as it applies to the obligations of the PPB under, or as otherwise incorporated into, the Scheme unless the PPB, in its absolute discretion, consents (but, for the avoidance of doubt, nothing in this Clause 7.1.2 shall affect enforcement of the obligation imposed on the PPB by Clause 6.1.6).

7.2 Additional restrictions on MMI and the Directors during the Initial Scheme Period

During the Initial Scheme Period, MMI shall not, and the Directors shall procure that MMI shall not:—

(a) sell or otherwise dispose, of any Scheme Asset (or sell or dispose, either by one transaction or a series of related transactions, of any number of Scheme Assets) recorded in the books of MMI as having a value (or an aggregate value) in excess of £3,000,000;

(b) enter into any Commutation in respect of any Liability under which MMI agrees to make a cash payment in excess of £250,000; or

(c) incur expenditure of more than £500,000 on the development of any site,

unless MMI has first obtained from an individual qualified to act as an insolvency practitioner in accordance with section 390 of the Insolvency Act 1986 written advice that

such sale, disposal, Commutation or, as the case may be, development, will not be prejudicial to the interests of the creditors of MMI as a whole.

7.3 **Additional restrictions on MMI and the Directors during the Levy Period**

7.3.1 During the Levy Period, MMI may, if the Scheme Administrator considers that to do so would be in the best interests of Voting Creditors, arrange for the issue or creation of new letters of credit, trusts, bonds or other instruments or security over any Scheme Asset:—

(a) in order to replace existing letters of credit or trusts; or

(b) in order to secure Liabilities incurred after the Effective Date; or

(c) to provide security for the purpose of any litigation, arbitration or other proceedings whatsoever in relation to any Liabilities of MMI

but (subject to Clause 6.2) not otherwise; and in any such case as is referred to in (b) or (c) above, the amount secured by any such letter of credit, trust, bond or other instrument or security shall (subject to Clause 6.2) be limited to the entitlement which any person in whose favour the same is given would have under the Scheme (on the assumption that its claim becomes an Established Liability) and MMI may renew or permit to be renewed any existing letter of credit.

7.3.2 During the Levy Period, any power conferred on MMI or its officers, whether by statute or by the Memorandum and Articles of Association, which could be exercised in such a way as to interfere with the exercise by the Scheme Administrator of his powers in relation to MMI conferred by Clause 8.3 shall not be exercisable except with the consent of the Scheme Administrator, which may be given either generally or in relation to particular cases (provided that nothing in this Clause 7.3.2 shall relieve the Directors from their duty to act in accordance with the Act).

7.4 **Provision of information**

At any time when the Scheme Administrator is not exercising general powers of management pursuant to Clause 8.3, MMI shall promptly provide the Scheme Administrator and the PPB with all information in MMI's possession or under the control of it or its agents as the Scheme Administrator or the PPB respectively shall from time to time request in order to satisfy himself or, as the case may be, itself that the management of MMI is being prudently conducted, such information to include, without limitation:—

(a) copies of MMI's annual report and accounts;

(b) quarterly management accounts (including the aggregate amount of insurance claims paid by MMI during the period to which such accounts relate and the aggregate amount of insurance claims outstanding as at the end of such period, distinguishing between claims made by "personal lines" creditors and claims made by "commercial lines" creditors, each as recorded in MMI's books of account);

(c) all accounts, balance sheets, abstracts or statements deposited by MMI with the Secretary of State pursuant to section 22 of the Insurance Companies Act 1982;

(d) copies of all board agendas and minutes; and

(e) copies of such advice as is referred to in Clause 7.2.

The PPB shall pay the reasonable costs of MMI and its agents in providing such information to the PPB.

PART 8

THE SCHEME ADMINISTRATOR

8.1 **The Scheme Administrator, qualifications, resignation and removal**

8.1.1 The initial Scheme Administrator shall be the person whose name is set out in Clause 1.3.2.1.

8.1.2 There shall be a Scheme Administrator having the powers and duties conferred upon him by the Scheme. In exercising his powers and carrying out his duties under the Scheme, the Scheme Administrator shall act *bona fide* and with due care and diligence in the interests of Voting Creditors as a whole and shall use his powers under the Scheme for the purpose of ensuring that the Scheme is operated in accordance with its terms.

8.1.3 The Scheme Administrator shall be an individual qualified to act as an insolvency practitioner in accordance with section 390 of the Insolvency Act 1986 who has consented, and not withdrawn his consent, to become a member of MMI.

8.1.4 The Scheme Administrator may resign his appointment at any time by giving not less than six months' notice in writing to MMI and to the Creditors' Committee.

8.1.5 The Scheme Administrator shall, with effect from the Effective Date, ensure that there is in force such bond as would have had to be in force if MMI had been wound up in England on such date and he had been appointed its liquidator.

8.1.6 The office of the Scheme Administrator shall be vacated if the Scheme Administrator:—

(a) dies;

(b) resigns his office by giving notice in writing to MMI and the Creditors' Committee in accordance with Clause 8.1.4 or when called upon to do so by the Creditors' Committee in accordance with Clause 10.10.6;

(c) becomes bankrupt;

(d) becomes Mentally Disordered;

(e) is convicted of an indictable offence;

(f) is no longer a person qualified to act as an insolvency practitioner in accordance with section 390 of the Insolvency Act 1986; or

(g) ceases to be a member of MMI.

8.1.7 Immediately (and, in any event, within 30 days) after (a) the resignation of the Scheme Administrator or (b) the vacation of the office of Scheme Administrator pursuant to Clause 8.1.6, the Creditors' Committee shall be entitled to appoint a person to be the Scheme Administrator provided that such person is qualified to act as such in accordance with Clause 8.1.3.

8.1.8 The Voting Creditors shall be entitled:—

(a) to remove the Scheme Administrator by a Creditors' Resolution at a meeting of the Voting Creditors at which the Scheme Administrator has been given an opportunity to be heard; and

(b) upon removal of the Scheme Administrator by a Creditors' Resolution, to appoint any person qualified to act as such in accordance with Clause 8.1.3 in his place.

8.1.9 If at any time the Scheme Administrator is unable to exercise his powers or carry out his duties under the Scheme or the office of Scheme Administrator is vacant, then the Deputy Scheme Administrator shall have full power and authority under the Scheme to exercise such powers or carry out such duties until such time as the Scheme Administrator is able to resume his functions or a new Scheme Administrator is appointed (as the case may be). The initial Deputy Scheme Administrator shall be the person whose name is set out in Clause

1.3.2.2. The provisions of the Scheme relating to the Scheme Administrator shall apply *mutatis mutandis* to the Deputy Scheme Administrator whilst he is carrying out such functions so that references to the Scheme Administrator (including, for the avoidance of doubt, in the definition of the Scheme Administrator) shall be construed as references to the Deputy Scheme Administrator for such period. Clauses 8.1.2, 8.1.3, 8.1.4, 8.1.6, 8.1.7, 8.1.8 and 8.6 shall apply to the Deputy Scheme Administrator throughout his term of office as if references to the Scheme Administrator were to the Deputy Scheme Administrator.

8.2 **Functions of the Scheme Administrator during the Initial Scheme Period**

During the Initial Scheme Period, the Scheme Administrator shall be entitled:—

(a) to receive from the Directors, at six monthly intervals commencing on the Effective Date, reports on the affairs of MMI;

(b) to convene, no more than twice in each year (the first year commencing on the Effective Date and ending on the day before the anniversary thereof), a meeting of the Directors for the purpose of obtaining information concerning the affairs of MMI,

and shall have the powers and shall be subject to the duties provided for in Clauses 6.3, 7.1, 7.4, 8.1, 8.4.1(a), 8.4.3, 8.5.4 to 8.5.6, 9.2, 10.7.3, 10.7.4 and 10.10.3 and Part 11.

8.3 **Functions of the Scheme Administrator during the Levy Period**

8.3.1 During the Levy Period, the Scheme Administrator shall:—

(a) manage the run-off of MMI's business;

(b) hold and, in due course, realise the assets of MMI and apply them for the benefit of the Voting Creditors and other creditors of MMI in accordance with the Scheme and the terms on which they are held by MMI; and

(c) supervise and ensure the carrying out of the Scheme.

8.3.2 On and after, but not before, the occurrence of a Trigger Event, the Scheme Administrator shall have general powers of management and control of the business, affairs and assets of MMI for the purpose of implementing, and in accordance with the terms of, the Scheme, together with such other powers as are specifically conferred on him by Clause 8.3.3, all of such powers being in substitution for, and to the exclusion of, the powers of the Directors.

8.3.3 During the Levy Period and without prejudice to the generality of Clause 8.3.2, the Scheme Administrator shall be entitled:—

(a) to agree claims and process reinsurance recoveries as part of the run-off of MMI's business;

(b) to take possession of, collect, get in and hold all the property and assets (of whatever nature) to which MMI is or appears to be entitled and to do all such things as may be necessary for the realisation in due course of any such property or assets;

(c) to have full access at all times to all books, papers and other documents of MMI, to receive all such information as he may require in relation to its affairs and to receive notice of and attend all meetings (if any) of the Board;

(d) to do all things which may be necessary or expedient for the protection of MMI's assets (or of any assets that appear to belong to MMI);

(e) to bring or defend any action or other legal proceedings in the name and on behalf of MMI or otherwise;

(f) to be remunerated in accordance with Clause 8.6 for the carrying out of his functions and to be reimbursed for all expenses properly incurred by him in connection therewith;

(g) to employ and remunerate accountants, actuaries, lawyers and other advisers or agents in connection with the conduct of his functions under the Scheme;

(h) to give directions to the Directors in relation to the exercise by them of their rights and powers in connection with MMI;

(i) to do all acts and to execute in the name and on behalf of MMI any deed, receipt or other document and to use MMI's seal;

(j) to borrow and to make any payment which is necessary or incidental to the performance of his functions and to give a valid discharge for amounts received by MMI;

(k) to delegate to any person qualified to act as mentioned in Clause 8.1.3 and approved for the time being by the Creditors' Committee for the purposes of this Clause 8.3.3, all or any of the powers and duties conferred upon the Scheme Administrator under the Scheme and from time to time to revoke any such delegation, provided that the Scheme Administrator shall be personally responsible for any act or omission of any such delegate to the same extent as if he had expressly authorised it;

(l) to the extent that the court has jurisdiction and subject to Clause 7.1.2, to apply, or to cause MMI to apply, to the court for directions in relation to any particular matter arising in the course of the Scheme; and

(m) to attend meetings of the Creditors' Committee.

8.4 **Powers of the Scheme Administrator as a member of MMI**

8.4.1 After consultation with the Creditors' Committee, the Scheme Administrator shall be entitled, in accordance with the Articles of Association, to exercise such powers as may be conferred upon him by the Articles of Association:—

(a) both during the Initial Scheme Period and the Levy Period to exercise such voting or other rights as may be conferred upon him by the Articles of Association in order to ensure compliance with Part 9 of the Scheme (other than Clause 9.1.4 thereof) or to defeat any resolution put to the members of MMI to wind MMI up voluntarily or to alter any provision of the Articles of Association containing any of the powers referred to in this Clause 8.4 or any provision of the Memorandum of Association; and

(b) during the Levy Period to:—

(i) appoint any person who is willing to act as a director of MMI and remove any person as a director of MMI and to block any other such resolution put either by the Directors or other members of MMI; and

(ii) pass a resolution to wind-up MMI voluntarily when directed to do so by a Creditors' Resolution.

8.4.2 The Scheme Administrator shall, unless authorised not to do so by a resolution of the Creditors' Committee in favour of which the PPB voted, exercise such powers as may be conferred upon him by the Articles of Association to ensure that no amendment is made to the Memorandum of Association or Articles of Association which would, in the opinion of the PPB, directly or indirectly adversely affect the interest of the PPB in the Scheme.

8.4.3 During the Initial Scheme Period, the Scheme Administrator shall, unless (and only unless) authorised in writing by the PPB not to do so, exercise such powers as may be conferred upon him by the Articles of Association in order to ensure compliance with Clause 9.1.4.

8.5 **Specific duties of the Scheme Administrator**

8.5.1 During the Levy Period, the Scheme Administrator shall not less than once each calendar year review the rate of Levy and the Payment Percentage and either adjust it in accordance with Clause 5.3 or decide that the current Payment Percentage is correct and no further Levy need be imposed, in which latter case the Payment Percentage will remain unchanged until adjusted at a later date (if at all).

8.5.2 The Scheme Administrator shall within 90 days after the rate of Levy and the Payment Percentage has been set in any year in accordance with Part 5, and within 90 days of any adjustment of the rate of Levy and Payment Percentage, prepare a report on the affairs of MMI and the operation of the Scheme during the period since the last such report was prepared or, in the case of the first such

report, the Trigger Date. Such report shall contain such information and particulars concerning the last calculation of the rate of Levy and the Payment Percentage, the value of Established Liabilities, the estimated value of Scheme Liabilities and other Liabilities of MMI, the payments made to Scheme Creditors, the investments held by or on behalf of MMI as at the last Review Date, the conduct of MMI and the operation of the Scheme as the Creditors' Committee may reasonably require.

The Scheme Administrator shall send a copy of the report prepared under Clause 8.5.2 above to each member of the Creditors' Committee and to each of the Directors at the time the report is completed. The Scheme Administrator is not under a duty to provide a copy of the report to a Scheme Creditor unless that Scheme Creditor has specifically requested the Scheme Administrator in writing to send to it a copy of the report.

8.5.4 The Scheme Administrator shall give to the Creditors' Committee all such reasonable information in his possession concerning the affairs of MMI or the operation of the Scheme as the Creditors' Committee shall from time to time resolve to seek from the Scheme Administrator and in respect of which a written request shall have been received by the Scheme Administrator pursuant to Clause 10.10.5.

8.5.5 Nothing in Clause 10.10.5 shall require the Scheme Administrator to provide to the Creditors' Committee information the release of which he determines would be detrimental to the interests of MMI and the Voting Creditors as a whole. If the Scheme Administrator refuses to provide information under this Clause, he must give to the Chairman of the Creditors' Committee reasons for his decision.

8.5.6 In exercising his powers and carrying out his duties under the Scheme, the Scheme Administrator shall consult with, and take account of the views expressed by, the Creditors' Committee on matters material to the Scheme (which, for the avoidance of doubt, include the imposition of any Levy, any increase in the Payment Percentage and any appointment or removal of Directors).

8.6 Scheme Administrator's costs, charges and expenses

Subject to obtaining the prior approval of the Creditors' Committee, MMI shall pay all reasonable costs, charges and expenses incurred by the Scheme Administrator in the course of exercising his powers and carrying out his duties under the Scheme, including (for the avoidance of doubt) but not limited to:—

(a) the cost of remunerating the Scheme Administrator and his staff; and

(b) the costs incurred by the Scheme Administrator in employing agents and advisers to assist him in exercising his powers and carrying out his duties under the Scheme.

PART 9

THE DIRECTORS

9.1 **The Directors**

9.1.1 The Board of Directors shall consist of not more than eleven Directors.

9.1.2 On the Effective Date, the Board will consist of the Current Directors with the exception of Maurice Stonefrost.

9.1.3 During the Levy Period, the Current Directors may be dismissed and other Directors may be appointed or dismissed only by, or by agreement of, the Scheme Administrator in pursuance of Clause 8.4.

9.1.4 During the Initial Scheme Period, no Controller of MMI shall be appointed or removed without the prior written consent of the PPB.

9.1.5 The Scheme Administrator shall during the Levy Period ensure that the composition of the Board complies with the Act.

9.1.6 During the Initial Scheme Period, the Directors shall, at six monthly intervals commencing on the Effective Date, produce reports on the affairs of MMI and send the same to the Scheme Administrator.

9.1.7 Without prejudice to the Articles of Association, a Director may be a creditor of MMI or a director or shareholder of, or otherwise interested in, a person which is a creditor of MMI, but in carrying out his duties as a Director of MMI he shall not be entitled to any confidential information in MMI's possession relating to any matter where that creditor has an interest in conflict with MMI.

9.2 **Compliance with this Part 9**

The Scheme Administrator shall exercise his powers, whether under this Scheme, the Articles of Association or otherwise, to ensure compliance with the provisions of this Part.

PART 10

THE CREDITORS' COMMITTEE

10.1 Constitution of the Creditors' Committee

10.1.1 There shall be a Creditors' Committee for the purposes mentioned in the Scheme.

10.1.2 The Creditors' Committee shall consist of not less than four nor more than ten members (each a "Committee Member") of whom one shall be the PPB and one shall be a person which is not a Local Authority.

10.1.3 The following shall be eligible for appointment as a Committee Member:—

(a) any Scheme Creditor (whether a body corporate or otherwise);

(b) the PPB; and

(c) any other person with the written consent of the Scheme Administrator.

10.2 Membership of the Creditors' Committee

10.2.1 The initial Committee Members shall be the persons whose names and addresses are set out in Clause 1.3.4, subject, in the case of (a) to (h) thereof, to each of the proposed Committee Members obtaining the necessary internal authorisations for it to become a Committee Member. The Company Secretary of MMI for the time being shall act as Secretary.

10.2.2 The Creditors' Committee may resolve at any time, by a majority of two-thirds of the Committee Members present, to appoint any person who is eligible to be appointed as a Committee Member, and who is not disqualified to act in accordance with Clause 10.3, to be a Committee Member, whether to fill a vacancy or as an additional Committee Member, but so that the total number of Committee Members shall not exceed the maximum number specified in Clause 10.1.2. In appointing replacement or additional members, the Creditors' Committee shall endeavour to ensure that the composition of the Creditors' Committee is such as to secure a proper balance of the interests of Scheme Creditors.

10.2.3 The Voting Creditors may by Creditors' Resolution remove any Committee Member (other than the PPB) from office and, without prejudice to the Creditors' Committee's powers under Clause 10.2.2, may, subject to Clause 10.2.4, by Creditors' Resolution appoint any person who is eligible to be appointed under Clause 10.1.3 to be a Committee Member either to fill a casual vacancy or as an addition to the existing Committee Members but so that the total number of Committee Members shall not exceed the maximum number specified in Clause 10.1.2.

10.2.4 No person shall be appointed or reappointed as a Committee Member at any meeting of Voting Creditors unless:—

(a) he is recommended by the Creditors' Committee; or

(b) not less than fourteen and no more than thirty-five clear days before the date appointed for the meeting, a notice executed by a Scheme Creditor qualified to vote at the meeting has been given to the Creditors' Committee of the intention to propose that person for appointment or reappointment together with a notice executed by that person of his willingness to be appointed or reappointed.

10.3 Ceasing to be a Committee Member

10.3.1 The office of a Committee Member (other than the PPB) shall be vacated if that Committee Member:—

(a) resigns by notice in writing addressed to the Secretary of the Creditors' Committee;

(b) is removed from office by a resolution passed by all of the Committee Members (excluding the Committee Member resolved to be removed);

(c) is removed from office by a Creditors' Resolution passed by the Voting Creditors;

(d) is convicted of an indictable offence;

(e) in the case of an individual:—

(i) dies; or

(ii) becomes Mentally Disordered; or

(iii) becomes disqualified from acting as a director under English law; or

(iv) becomes subject to a bankruptcy order; or

(f) in the case of a body corporate or partnership, is dissolved.

10.3.2 The PPB may resign by notice in writing to the Secretary of the Creditors' Committee and signed by the Chairman for the time being of the PPB. Such notice shall be deemed to have been received by the Secretary on delivery by hand to the Secretary at MMI's registered office or, if sent by post addressed to the Secretary at MMI's registered office, 48 hours after the notice is posted.

10.4 Appointment of representatives and a PPB Alternate

10.4.1 Each Committee Member (other than the PPB) which is a body corporate or a joint authority, board or committee or a partnership may, by notice in writing to the Secretary, appoint a senior officer or executive or, in the case of partnerships, a partner as its representative ("Nominated Representative") to represent that Committee Member at meetings of the Creditors' Committee.

10.4.2 The PPB shall be entitled to appoint one person (the "PPB Representative") to represent it at meetings of the Creditors' Committee. The PPB may from time to time remove the PPB Representative and appoint another person in his place by written notice to the Secretary signed by the Chairman for the time being of the PPB.

10.4.3 The Chairman for the time being of the PPB or the PPB Representative shall be entitled to appoint any person as an alternate (the "PPB Alternate") to attend and vote at any meeting of the Creditors' Committee in place of the PPB Representative.

10.5 Powers of Nominated Representatives, the PPB Representative and the PPB Alternate

Any Nominated Representative shall have the same powers and shall be subject to the same duties and limitations as the Committee Member whom the Nominated Representative represents. The PPB Representative shall have the same powers and shall be subject to the same duties and limitations as the PPB. The PPB Alternate shall have the same powers and be subject to the same duties and limitations as the PPB or the PPB Representative.

10.6 Revocation of appointment of Nominated Representatives, the PPB Representative and the PPB Alternate

10.6.1 The appointment of the PPB Alternate may from time to time be revoked by the Chairman for the time being of the PPB or the PPB Representative by giving written notice of such revocation to the Secretary.

10.6.2 Any person entitled to appoint a Nominated Representative may from time to time revoke that appointment and appoint another Nominated Representative by notice in writing to the Secretary.

10.6.3 The appointment of a Nominated Representative shall terminate automatically if:—

(a) his appointment is revoked by his appointor;

(b) the person whom that Nominated Representative represents ceases to be a Committee Member;

(c) the Nominated Representative ceases to be a senior officer or executive or, as the case may be, a partner of the Committee Member whom he represents; or

(d) the Nominated Representative dies, becomes Mentally Disordered, becomes subject to a bankruptcy order or is disqualified from acting as a director under English law.

10.6.4 The appointment of a PPB Representative shall terminate automatically if:—

(a) his appointment is revoked by the PPB;

(b) the PPB ceases to be a Committee Member; or

(c) the PPB Representative dies, becomes Mentally Disordered, becomes subject to a bankruptcy order or is disqualified from acting as a director under English law.

10.7 **Proceedings of the Creditors' Committee**

10.7.1 Subject to the provisions of the Scheme, the Creditors' Committee may regulate its proceedings as it sees fit.

10.7.2 The Creditors' Committee shall from time to time elect one of the Committee Members as Chairman, who shall preside at their meetings, but if no Chairman is elected or if at any meeting he is not present within 15 minutes after the time appointed for holding the meeting, the Committee Members present may choose one out of their number to be Chairman of the meeting.

10.7.3 The Creditors' Committee shall meet at least once in each calendar year (commencing in 1994) for the purpose of receiving a report from the Scheme Administrator on the affairs of MMI and operation of the Scheme. The Creditors' Committee shall hold such further meetings as shall seem desirable for the purpose of performing its functions under the Scheme.

10.7.4 The Scheme Administrator or any Committee Member may at any time request the Secretary to summon a meeting of the Creditors' Committee.

10.7.5 The Secretary shall call a meeting of the Creditors' Committee as soon as practicable after receiving a request to do so in accordance with Clause 10.7.4.

10.7.6 The Secretary shall procure that written notice of any Creditors' Committee meeting (setting out the time, date and venue (which shall be in Great Britain) of such meeting and indicating the nature of business to be transacted at such meeting) shall be given to each member of the Creditors' Committee, the Scheme Administrator and each of the Directors.

10.7.7 Except with the consent of all Committee Members and the Scheme Administrator, no meeting of the Creditors' Committee may be called upon less than 14 clear days' notice and no business may be transacted at any such meeting other than that set out in the notice to that meeting.

10.7.8 The quorum necessary for the transaction of business shall be three Committee Members. If a quorum is not present within half an hour from the time appointed for a meeting, or if during a meeting such a quorum ceases to be present, the meeting shall stand adjourned to such time and place as the Chairman of the meeting may determine and the Committee Members present at any such adjourned meeting shall constitute a quorum.

10.7.9 The Creditors' Committee may act notwithstanding any vacancy in its body but if and so long as the number of Committee Members does not exceed three, the continuing Committee Members may act for the purpose of convening a meeting of Voting Creditors, filling the vacancy or vacancies in the number of Committee Members or filling any vacancy in the office of Chairman, but for no other purpose.

10.7.10 Each Committee Member shall have one vote and, except as otherwise provided, matters arising at any meeting shall be decided by a majority of votes of the Committee Members. A Committee Member shall not be entitled to vote or to form part of the quorum in relation to any matter in which it is in any way interested (other than a general interest arising by reason only of its status as a Voting Creditor) and shall absent itself from the meeting for so long as such matter is discussed and voted upon and shall not receive any information

relating thereto. The Chairman of the meeting shall have a second or casting vote. The Scheme Administrator and each Director shall be entitled to attend and speak, but not to vote, at all meetings of the Creditors' Committee.

10.7.11 Other than in relation to such a resolution as is referred to in Clause 10.10.6(a), a resolution in writing signed by all Committee Members for the time being (or their respective Nominated Representative or, in the case of the PPB, the PPB Representative or the PPB Alternate) shall be as valid and effective as if passed at a meeting of the Creditors' Committee duly convened and held.

10.7.12 The Chairman of the Creditors' Committee shall cause proper minutes to be kept of all proceedings of the Creditors' Committee and such minutes shall at all reasonable times be open to inspection by (subject to Clause 10.7.10) any Committee Member or by the Scheme Administrator or any member of the Board. Copies of such minutes shall be sent as soon as practicable after their preparation to the Scheme Administrator.

10.8 **Validation**

All acts done by the Creditors' Committee, a Committee Member, Nominated Representative, PPB Representative, PPB Alternate or any meeting of the Creditors' Committee shall, notwithstanding that it is afterwards discovered that there was some defect in the appointment of the Committee Member or any person acting as aforesaid, or that any of them were disqualified, be as valid as if every such person had been duly appointed and qualified.

10.9 **Expenses**

MMI shall pay all the reasonable costs of summoning meetings of the Creditors' Committee (irrespective of who requests the meeting) and the reasonable out-of-pocket expenses of the Committee Members and the Scheme Administrator and the Directors in attending meetings of the Voting Creditors and all the reasonable costs of sending out all notices to be given by the Creditors' Committee under the Scheme.

10.10 **Functions of the Creditors' Committee**

10.10.1 The Creditors' Committee shall be responsible for monitoring the implementation of the Scheme (including, without limiting the generality of the foregoing, providing their view on any matter relating to the Scheme, if so requested by the Scheme Administrator) and for the supervision of the Scheme Administrator in the performance of his functions under the Scheme.

10.10.2 The Creditors' Committee shall consider and, if thought fit, approve (such approval not to be unreasonably withheld or delayed), on behalf of MMI, the level and payment of the fees and expenses of the Scheme Administrator from time to time (and so that such function may, with the prior written consent of the Scheme Administrator, be delegated to one or more members of the Creditors' Committee).

10.10.3 The Creditors' Committee and the Scheme Administrator may from time to time agree between themselves how they intend the monitoring and supervisory role of the Creditors' Committee and the relationship between the Scheme Administrator and the Creditors' Committee under the Scheme to operate in practice. No person may become a member of the Creditors' Committee or the Scheme Administrator unless it or he has first agreed with the then current members of the Creditors' Committee and the then current Scheme Administrator to abide by any then current agreement between the Creditors' Committee and the Scheme Administrator under this Clause 10.10.3.

10.10.4 The Creditors' Committee shall, so far as it is able, ensure that there is a Scheme Administrator in office at all times after the Effective Date.

10.10.5 The Creditors' Committee may from time to time resolve what information it is desirable to seek from the Scheme Administrator concerning the affairs of MMI and the operation of the Scheme and may delegate any one Committee Member to apply in writing to, and receive from, the Scheme Administrator all such information as may be specified in such application.

10.10.6 The Creditors' Committee shall be entitled:—

(a) by a resolution passed by at least three-quarters of all of the Committee Members for the time being at any time to call upon the Scheme Administrator to resign, provided that the Scheme Administrator has been given at least twenty-eight days' notice of the proposed resolution and of the reasons why the resolution is to be put to the Creditors' Committee and has been given a reasonable opportunity to make representations at the meeting at which the resolution is proposed (and, if the Scheme Administrator declines to resign, a resolution requiring his removal shall be put before the next meeting of Voting Creditors); and

(b) upon removal of the Scheme Administrator or if the Scheme Administrator ceases to hold office for any other reason, by resolution passed by a majority of Committee Members present and voting at the relevant meeting of the Creditors' Committee to appoint any person qualified to act under Clause 8.1.3 to be the Scheme Administrator in his place (and a resolution requiring ratification of such appointment shall be put before the next meeting of Voting Creditors pending which the appointee shall have full power to act as the Scheme Administrator) save that if a resolution is passed at a meeting of Voting Creditors requiring the removal of the Scheme Administrator pursuant to Clause 10.10.6(a) such appointment may be made by the Voting Creditors at such meeting.

10.10.7 Each member of the Creditors' Committee shall be entitled at any time to raise questions or to request a meeting with the Scheme Administrator in connection with the performance of his responsibilities and, subject to his duties under the Scheme, the Scheme Administrator shall use reasonable endeavours to respond to such questions or to comply with any such request for a meeting.

10.11 **Duties of Committee Members**

10.11.1 Each member of the Creditors' Committee shall, in performing its functions as such, act *bona fide* in the best interests of the Voting Creditors as a whole.

10.11.2 Each Committee Member shall use its best endeavours to avoid conflicts of interest in performing its duties under the Scheme. It shall be the duty of each Committee Member which is in any way, whether directly or indirectly, interested in a contract or proposed contract with MMI to declare (or procure that its Nominated Representative or, in the case of the PPB, the PPB Representative or PPB Alternate shall declare) the nature of his or its interest at a meeting of the Creditors' Committee. For this purpose a general notice given to the Creditors' Committee to the effect that a Committee Member is associated (within the meaning of section 435 of the Insolvency Act 1986) with a specified company or firm and is to be regarded as interested in any contract with that company or firm is deemed a sufficient declaration of interest in relation to any such contract.

10.11.3 Each Committee Member (other than the PPB) shall, and shall procure that any Nominated Representative and its officers and employees shall, preserve the confidentiality of all information concerning MMI and the operation of the Scheme and shall use such information only for the purpose of performing their responsibilities and functions under the Scheme unless they have obtained the prior written approval of the Scheme Administrator.

10.11.4 Notwithstanding Clause 10.11.3, each Nominated Representative shall be entitled to report to the Committee Member appointing him on the proceedings of the Creditors' Committee and, so far as necessary for that purpose, to disclose confidential information of MMI to those officers and employees and professional advisers of that Committee Member who need to know it in connection with the performance of its responsibilities as a Committee Member, provided that such information does not to his knowledge, after making due and careful enquiry, relate to any matter where such appointor has an interest in conflict with MMI (other than a general conflict arising as the result of the status of the Committee Member as a Scheme Creditor).

10.11.5 Notwithstanding Clause 10.11.3, the PPB Representative or the PPB Alternate, as the case may be, shall be entitled to report to the PPB on the proceedings of the Creditors' Committee and, so far as necessary for that purpose, to disclose confidential information of MMI to the members of the PPB, the PPB Secretary and the members of the staff and professional advisers and consultants of the PPB and they or any of them shall be entitled to use the same for the purpose of fulfilling their functions under the Policyholders Protection Act (including their functions under the Scheme), provided that such information does not to its knowledge, after making due and careful enquiry, relate to any matter where the PPB has an interest in conflict with MMI (other than a general conflict arising by reason of the PPB's status as a creditor).

10.11.6 Other than in respect of any information provided to the PPB pursuant to Clause 6.3, the PPB shall, and shall procure that its members, officers and employees, the PPB Secretary, the PPB Representative, any PPB Alternate and any professional adviser or consultant of the PPB shall, preserve the confidentiality of such information and shall use such information only for the purpose of performing their responsibilities and functions in relation to the PPB's obligations, duties and powers as a Committee Member unless the PPB has obtained the prior written approval of the Scheme Administrator.

PART 11

THE VOTING CREDITORS

11.1 **Meetings of Voting Creditors**

11.1.1 The Scheme Administrator shall convene a meeting of the Voting Creditors upon receipt at MMI's registered office of a request in writing that such a meeting be held from either (a) not less than seventy Voting Creditors or (b) any Voting Creditor, or Voting Creditors together, which represent the requisite value for the purposes of this Clause. A Voting Creditor, or Voting Creditors together, will represent the requisite value if the aggregate of:—

(a) Scheme Liabilities due to such Voting Creditor(s) (including Established Scheme Liabilities in respect of which payment has been made by MMI, in full or in part, since the Record Date); and

(b) in the case of the PPB, PPB Liabilities for the time being outstanding or paid,

shall exceed £80 million. The PPB shall for the purpose of convening a meeting of Voting Creditors be counted as a separate Voting Creditor in respect of each PPB Liability (provided that where more than one PPB Liability has arisen in respect of the same Protected Creditor, such PPB Liabilities shall be counted as one for such purpose).

11.1.2 For the purposes of this Clause, the value of Scheme Creditors' Scheme Liabilities shall, where Established, be assessed in accordance with the amount agreed or settled with MMI, or where the Scheme Liability has not been Established, the amount as estimated by the Scheme Creditor, subject to a determination by the Scheme Administrator. For the purposes of this Clause, the value of PPB Liabilities shall be the aggregate of amounts either outstanding from, or paid by, MMI to the PPB as at the relevant time. All Scheme Liabilities and PPB Liabilities denominated in currencies other than Sterling shall be converted into Sterling at the average of the rates respectively quoted by National Westminster Bank Plc for the purchase and the sale of Sterling with or for the relevant currency at or around 11 a.m. on the last Trading Day preceding the date of the request and, if not quoted on that day, then so quoted on the nearest preceding day.

1.1.3 In the event that a Scheme Creditor disputes the value which has been put on its Scheme Liability pursuant to Clause 11.1.2, the dispute shall be referred to the President for the time being of the Society of Practitioners in Insolvency or such other individual or individuals qualified to act as an insolvency practitioner in accordance with section 390 of the Insolvency Act as he may nominate who shall consult with such relevant experts as he thinks appropriate and who shall act as an expert not an arbitrator and whose decision (including as to who should bear the costs of such referral) shall be final (but only as regards the convening of the meeting on that occasion).

1.4 Any such written request, as is referred to in Clause 11.1.1, must specify the purpose for which the meeting is required and it shall be the duty of the Scheme Administrator to give such notice of the meeting as is necessary to enable such purpose to be carried out effectively in accordance with the provisions of the Scheme.

11.1.5 The Scheme Administrator may also convene a meeting of the Voting Creditors whenever and for whatever purposes as the Scheme Administrator may think fit.

11.2 **Notice of meeting**

11.2.1 At least 28 days' notice in writing of every meeting of Voting Creditors, specifying the time and place of the meeting and the general nature of the business to be transacted at the meeting, shall be given to every Voting Creditor at the last known address (if any) of such Voting Creditor or such other address as it may have given to MMI for the service of such notices upon it.

11.2.2 Every such notice may be sent by pre-paid post and the accidental omission to send any such notice to, or the non-receipt of notice by, any Voting Creditor entitled to receive the same, shall not invalidate the proceedings in any meeting.

11.2.3 The Scheme Administrator may also, to the extent he considers appropriate, cause to be published in such place or places as he deems fit, notices or advertisements of the proposed meeting of Voting Creditors.

11.2.4 Proof that an envelope containing a notice was properly addressed, pre-paid and posted shall be conclusive evidence that the notice was given. A notice shall be deemed to be given at the expiration of forty-eight hours after the envelope containing the same was posted.

11.3 Voting at meetings

11.3.1 Every Scheme Creditor present in person or by proxy shall have one vote for every pound Sterling of Scheme Liabilities which, if Established Scheme Liabilities, will be the amount agreed or settled with MMI or, if not Established Scheme Liabilities, the amount estimated by the Scheme Creditor, subject to a determination (for voting purposes only) by the Scheme Administrator. The PPB shall have one vote for every pound Sterling of PPB Liabilities outstanding, or paid by MMI, to the PPB as at the day before the relevant meeting of Voting Creditors and shall, for the purpose of voting on a resolution of Voting Creditors to remove the Scheme Administrator or the Deputy Scheme Administrator from office or to appoint a person qualified to act in accordance with Clause 8.1.3 in his place, be counted as a separate Voting Creditor in respect of each PPB Liability (provided that where more than one PPB Liability has arisen in respect of the same Protected Creditor, such PPB Liabilities shall be counted as one for such purpose). In the case of Scheme Liabilities or PPB Liabilities denominated in currencies other than Sterling, such Scheme Liabilities or, as the case may be, PPB Liabilities shall be converted into Sterling at the average of the rates respectively quoted by National Westminster Bank Plc for the purchase and the sale of Sterling with or for the relevant currency at or around 11 a.m. on the last Trading Day preceding the date of the meeting and, if not quoted on that day, then so quoted on the nearest preceding day. In the event that a Voting Creditor disputes the amount for which its vote should be counted, the question shall be referred to the Chairman of the meeting whose decision shall be final but only as regards the vote on that occasion.

11.3.2 Every Voting Creditor entitled to vote shall have the right to appoint any person as its proxy to attend and vote instead of it. The instrument appointing a proxy may be in any form which the Chairman of the meeting may approve and must be lodged at the place specified in the notice of the meeting for the lodging of proxies prior to or at the meeting at which it is to be used.

11.4 Quorum required for meetings

No business shall be transacted at a meeting of Voting Creditors unless a quorum is present when the meeting proceeds to business. The PPB shall, for the purpose of calculating whether a quorum is present, be counted as a separate Voting Creditor in respect of each separate PPB Liability (provided that where more than one PPB Liability has arisen in respect of the same Protected Creditor, such PPB Liabilities shall be counted as one for such purpose). Twenty Voting Creditors present in person or by proxy and having the right to vote at the meeting shall constitute a quorum. All resolutions put to the vote of any meeting shall be decided on a poll.

11.5 Chairman of Voting Creditors' meetings

The Scheme Administrator shall be the Chairman of all meetings of the Voting Creditors except if a resolution is proposed at the meeting directly concerning the Scheme Administrator, in which case the Chairman of the Creditors' Committee shall preside. If there is a vacancy in the office of Chairman or if the Chairman is not present within fifteen minutes after the time appointed for opening the meeting or is unwilling to preside, the Voting Creditors present in person or by proxy shall choose a member of the

Creditors' Committee, or, if no such member is present or if all such members present decline to preside, one of themselves to be Chairman of the meeting.

11.6 **Powers of the Voting Creditors in general meeting**

A meeting of the Voting Creditors shall have power by a Creditors' Resolution:—

(a) to remove any Committee Member (other than the PPB) from office and to appoint a person to be a Committee Member pursuant to Clause 10.2.3;

(b) to remove the Scheme Administrator or the Deputy Scheme Administrator from office and appoint a person qualified to act in accordance with Clause 8.1.3 in his place; and

(c) to terminate the Scheme pursuant to Clause 12.1.1(d).

PART 12

DURATION OF THE SCHEME

12.1 Termination of the Scheme

12.1.1 Subject to Clause 4.8 and Clause 5.10 (which shall continue to apply in the winding-up of MMI), the Scheme shall terminate if:—

(a) all of the Liabilities of MMI are discharged in full;

(b) MMI is ordered to be wound up by an order made by the Court;

(c) a voluntary winding-up of MMI is commenced under the Insolvency Act 1986;

(d) a Creditors' Resolution that the Scheme shall be terminated and MMI wound up is passed at a meeting of the Voting Creditors; or

(e) the Scheme Administrator, with the agreement of the Directors and of the Creditors' Committee, gives notice in writing to MMI at its registered office that, after due enquiry, he has concluded that the Scheme is no longer in the interests of the general body of Voting Creditors.

12.1.2 If the Scheme shall terminate otherwise than under Clause 12.1.1(a), the provisions of Clauses 4.8, 5.10.1, 5.10.2 and 6.2 shall continue to apply and the obligations of the PPB under the Scheme (except under Clause 6.2) shall cease.

12.1.3 If the Scheme shall terminate under Clause 12.1.1(a), the provisions of Clause 4.8 shall continue to apply.

12.2 Notice of termination of the Scheme

As soon as practicable following the Termination Date, the Creditors' Committee shall cause notices stating that the Scheme has terminated to be announced in the *Financial Times* or such newspapers and publications as the Scheme Administrator deems appropriate for one day a week for three consecutive weeks following the Termination Date. The cost of placing the announcements shall be payable out of the assets of MMI as at the Termination Date.

PART 13

MISCELLANEOUS

13.1 **Indemnity**

13.1.1 In this Clause 13.1:—

(a) "Employee" means any partner in the same firm as the Scheme Administrator or any individual employed, whether under a contract of service or a contract for services, by that firm or by any company owned by that firm, who is employed by the Scheme Administrator in accordance with Clause 8.3.3(g) in connection with the carrying out of his functions under the Scheme; and

(b) "Delegate" means any person to whom the Scheme Administrator may delegate any of his powers and duties under Clause 8.3.3(k).

13.1.2 No Voting Creditor shall be entitled to challenge the validity of any act done or omitted to be done in good faith and with reasonable care by the Scheme Administrator, the Deputy Scheme Administrator, any Director or the Company Secretary of MMI, any Committee Member (or any Nominated Representative, PPB Representative or PPB Alternate) or any other Voting Creditor in accordance with, and to implement, the provisions of the Scheme or the exercise or the purported exercise by any such person in good faith and with reasonable care of any power conferred on him for the purpose of the Scheme, if exercised or purported to be exercised in accordance with, and to implement, the Scheme.

13.1.3 Subject to the Act, no person mentioned in Clause 13.1.2 shall be liable for any loss, unless such loss is attributable to his own negligence, default, breach of duty, breach of trust, fraud or dishonesty (or, in the case of the Scheme Administrator and Deputy Scheme Administrator, to that of any Employee or Delegate).

13.1.4 No Voting Creditor shall be entitled to challenge the validity of any act done or omitted to be done in good faith and with reasonable care by any Employee in accordance with, and to implement, the provisions of the Scheme if exercised in accordance with, and to implement, the provisions of the Scheme and no Employee shall be liable for any loss unless such loss is attributable to his own negligence, default, breach of duty, breach of trust, fraud or dishonesty.

13.1.5 No Voting Creditor shall be entitled to challenge the validity of any act done or omitted to be done in good faith and with reasonable care by any Delegate in accordance with, and to implement, the provisions of the Scheme or the exercise by such Delegate in good faith and with due care of any power conferred upon the Scheme Administrator for the purposes of the Scheme if exercised in accordance with, and to implement, the provisions of the Scheme and no Delegate shall be liable for any loss unless such loss is attributable to his own negligence, default, breach of duty, breach of trust, fraud or dishonesty (or to that of any Employee).

13.1.6 Subject to the Act, MMI shall indemnify the persons mentioned in Clause 13.1.2 (other than Voting Creditors) and each Employee and Delegate all in their respective capacities as such against any liability incurred by them in defending any proceedings, whether civil or criminal, brought against them in relation to their respective responsibilities under the Scheme in which judgment is given in their favour or which is discontinued before judgment is given or in which they are acquitted or in connection with any application in which relief is granted to them by the Court from liability for negligence, default, breach of duty, breach of trust, fraud or dishonesty.

13.2 **Governing law and jurisdiction**

The Scheme shall be governed by, and construed in accordance with, English law and all the parties to it irrevocably submit to the jurisdiction of the Court.

Dated 15th November, 1993

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PART III

NOTICE OF COURT MEETING

IN THE HIGH COURT OF JUSTICE **No. 009528 of 1993**
CHANCERY DIVISION
MR. REGISTRAR BUCKLEY

IN THE MATTER OF MUNICIPAL MUTUAL INSURANCE LIMITED

- and -

IN THE MATTER OF THE COMPANIES ACT 1985

NOTICE IS HEREBY GIVEN that, by an Order dated 9th November, 1993 made in the above matters, the Court has directed that a meeting be convened of the creditors of Municipal Mutual Insurance Limited (the "Company") as to each of which both:—

(a) as at the close of business on 30th September, 1993 there were recorded in the books of the Company:—

(i) Scheme Liabilities due to such creditor which had become Established Scheme Liabilities but had not yet been paid; and/or

(ii) Reported Scheme Liabilities reported by such creditor which had not yet become Established Scheme Liabilities but on which an Estimated Value had been placed by the Company

of an aggregate amount and/or Estimated Value equal to or more than £25,000; and

(b) either:—

(i) the aggregate amount of Scheme Liabilities due to such creditor which have become Established Scheme Liabilities (together with the aggregate amount of any Elective Defence Costs paid by the Company on its behalf) exceeds £50,000; or

(ii) such creditor considers that it has (or may have) claims against the Company, including claims which have been reported but not agreed or otherwise established and claims based on losses which have been incurred but not reported, of an aggregate amount which would, if established, result in the provisions of sub-paragraph (b)(i) above being satisfied

(where the defined terms used herein have the same respective meanings as they are given in the Scheme of Arrangement hereinafter mentioned) for the purpose of considering and, if thought fit, approving (with or without modification) a Scheme of Arrangement proposed to be made between the Company and its Scheme Creditors (as defined in such Scheme of Arrangement) and that such meeting will be held at Central Hall, Storey's Gate, London SW1 at 2.00 p.m. on Wednesday, 5th January, 1994 at which place and time all such creditors so entitled are requested to attend.

A copy of the Scheme of Arrangement and a copy of the Statement required to be furnished pursuant to section 426 of the Companies Act 1985 are incorporated in the document of which this Notice forms part.

Creditors entitled to attend and vote at the meeting may vote in person at the meeting or they may appoint another person, whether a creditor or not, as their proxy to attend and vote in their place. A Voting and Proxy Form for use at the said meeting is enclosed herewith.

It is requested that the Form of Proxy contained in the Voting and Proxy Form should be lodged with The Company Secretary, Municipal Mutual Insurance Limited, 22 Old Queen Street, Westminster, London SW1H 9HW by 2.00 p.m. on 31st December, 1993 but if a Form of Proxy is not so lodged it may be handed to the Chairman at the meeting.

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By the said Order, the Court has appointed Sir John Lovill or, failing him, Philip Gregory or, failing him, Joseph Small to act as Chairman of the said meeting and has directed the Chairman to report the result thereof to the Court.

The Scheme of Arrangement will be subject to the subsequent sanction of the Court.

DATED 15th November, 1993

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