NAVIGANT CONSULTING

Proposed Transfer of
Lloyd's 1992 and Prior Business from Lloyd's Names

To

Speyford Ltd

Report of the Independent Expert

8 April 2009

Prepared by:

Allan Kaufman
Navigant Consulting (Europe) Ltd.
Centurion House
24 Monument Street
London EC3R 8AJ
United Kingdom
allan.kaufman@navigantconsulting.com

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1 INTRODUCTION

1.1 PURPOSE

1.1.1 This Report sets out the results of my review of the likely effects on Policyholders and other stakeholders in the event of the Transfer of Lloyd's 1992 and Prior Business (the Transfer) from Lloyd's Names (Names) to Speyford Limited (Speyford).

1.1.2 The Transfer is an insurance business transfer scheme as defined in Section 105 of Part VII of the Financial Services and Markets Act 2000 (FSMA). It is intended that the application for the Transfer will be heard by the High Court of England and Wales (the Court) in June 2009.

1.1.3 This Report has been prepared for purposes of the Transfer in accordance with Section 109 of FSMA.

1.1.4 The Report is subject to the terms and limitations, including limitation of liability, set out in my firm's engagement letter dated 17 July 2008.

1.1.5 A copy of this Report will be sent to the Financial Services Authority(FSA) and will accompany the Transfer application to Court. I am aware that in accordance with the relevant applicable legislation, copies of this Report may be made available to Policyholders as well as to all parties affected by the Transfer. In addition, I note that this Report will be available in the public domain.

1.2 HISTORY

1.2.1 The Equitas Group was formed in 1996 as part of the Reconstruction and Renewal project (R&R) to reinsure the 1992 and prior non-life obligations of Names.

1.2.2 On 10 November 2006, Equitas Limited (EL) and National Indemnity Company (NICO) entered into a reinsurance contract (the NICO Retrocession Agreement) agreed in November 2006 in which NICO reinsured EL's claim obligations up to a limit of $14.4bn. This limit was $5.7bn above the EL reserves net of reinsurance at 31 March 2006 and adjusted for movements to the transaction date ($8.7bn). The NICO Retrocession Agreement also provided that NICO would be responsible for ensuring that claims and certain other run-off functions would be handled by Resolute Management Services Limited (RMSL) in accordance with its provisions of the reinsurance contract and would cover other run-off costs.

1.2.3 The NICO Retrocession Agreement also provided that NICO would provide an additional layer of up to $1.3bn of reinsurance for a premium of up to £40m if EL arranged, on or before 31 December 2009, a transfer of the obligations from the Names[1]. This provision would therefore be trigged by the Transfer.

1.2.4 At the time of the NICO Retrocession Agreement it was not possible to transfer the 1992 and Prior Business of the Names who had ceased to be underwriting members of Lloyd's prior to 24 December 2006, under English Law. The relevant legislation was amended in 2008, and it is now possible to effect such a transfer.

[1] I am advised that EL is authorized to act on behalf of the Names under the provisions of the Equitas Reinsurance Contract and the Equitas Retrocession Agreement and Lloyd's has certified in accordance with the Resolution of the Council of Lloyd's dated 24 September 2008 that EL has authority to act on behalf of the Names for the purposes of the Transfer.

1.3 APPOINTMENT

1.3.1 I, Allan Kaufman, am a Managing Director of Navigant Consulting (Europe) Limited, Centurion House, 24 Monument Street, London EC3R 8AJ, United Kingdom, a subsidiary of Navigant Consulting Inc. (collectively, Navigant).

1.3.2 I have been appointed by EL to serve as the Independent Expert in this proposed Transfer.

1.3.3 EL will meet the costs of the preparation of this Report.

1.3.4 My appointment has been approved by the FSA in a letter dated 16 June 2008.

1.3.5 The conclusions described in this Report are mine. The work was performed by me or under my direct supervision. The team of people assisting me included actuaries, accountants, claim professionals, insolvency practitioners and economists specialising in Asbestos, Pollution and Health Hazard claims. I also had advice from Sidley Austin LLP (Sidley) to assist in my understanding and analysis of legal issues.

1.4 QUALIFICATIONS

1.4.1 I am a Fellow of the Casualty Actuarial Society (since 1974) and an Honorary Fellow of the Institute of Actuaries (since 1997). I have had extensive experience in evaluating insurance assets and liabilities similar to those associated with the Transfer. Details of my experience are included in my curriculum vitae attached as Appendix II.

1.5 SCOPE

1.5.1 I have considered the effect of the Transfer on the Policyholders comprised in the 1992 and Prior Business (the Transferring Policyholders).

1.5.2 I have also considered the effect of the Transfer on Policyholders insured/reinsured in 1993 and subsequent years by Names who were also Names in 1992 and prior years (the Non-Transferring Policyholders).

1.5.3 I have also considered the effect of the Transfer on the following parties:

1. Outwards External Reinsurers;
2. Lloyd's;
3. Other insurers with respect to the way Mesothelioma Claims in England can be made against insurers of employers' liability Policies;
4. Names as Policyholders;
5. Names as parties with respect to their interests other than as Policyholders; and
6. The Financial Services Compensation Scheme.

1.5.4 This Report reflects information provided to me at the time of submission, and future events may require that this Report be updated in order to assist the Court in its determination.

1.5.5 Appendix XIV lists areas in respect of which supporting documentation at the date of this Report, is not yet available to allow me to confirm certain aspects of my analysis. I have been asked to assume that the documentation will be provided in time to consider before the Court hearing and that it will be consistent with my analysis and conclusions.

1.5.6 Prior to the Court hearing I expect to provide a Supplemental Report in which I will address the effect, if any, on the FSCS in the event of a Transfer and the result of my review of the material identified in Appendix XIV.

1.5.7 This Report follows the guidance issued by the FSA on the form of the Scheme Report, as set out in paragraphs 18.2.31G to 18.2.41G of the Supervision Manual contained in the FSA Handbook of Rules and Guidance. Terms of reference for my review have been agreed by EL and seen by the FSA. A copy of these terms of reference is included in Appendix I.

1.5.8 I have not considered any alternative transactions for this business, nor have any been proposed to me.

1.5.9 NICO is providing reinsurance as part of the Transfer. I have not considered the effect of the Transfer on Policyholders of NICO, as the Transfer is not a transfer of business into NICO.

1.5.10 I have considered matters that I believe to be relevant to the interests of Policyholders and other parties listed in paragraph 1.5.3.

1.6 DUTIES

1.6.1 As Independent Expert reporting to the Court I am required to act in accordance with the Civil Procedure Rules. My Expert Declaration is included in Appendix III.

1.6.2 This Report is not required to and does not comply fully with the requirements of Guidance Note 12 of the Board for Actuarial Standards, which provides guidance to members of the UK Actuarial Profession on formal actuarial reports relating to general insurance. The Report does not include all the detail required to allow another actuary to form an assessment of all the key assumptions and judgements as this would require more data than is necessary for the purpose of this Report or is required by Section 109 of FSMA.

1.7 BUSINESS RELATIONSHIP WITH PARTIES

Allan Kaufman

1.7.1 Neither I nor any of my Connected Persons have any personal holding or interest in the Equitas Group, NICO or Speyford.

1.7.2 I have not carried out any work for any company in the Equitas Group, NICO or Speyford in the past three years.

1.7.3 Neither I nor any of my Connected Persons have ever been a Name at Lloyd's.

1.7.4 I am a Non-Executive Director (NED) of Pembroke Managing Agency (Pembroke). Pembroke, the Syndicate it manages, and Pembroke's affiliated companies have no connection to the 1992 and Prior Business. My NED role does not make me a Member of Lloyd's nor does it create any duties for me in the management or governance of Lloyd's. My director fees from Pembroke are £35,000 per annum and are not performance related.

Navigant

1.7.5 Navigant has client relationships with both Equitas and with Policyholders of Names reinsured by Equitas.

1.7.6 Navigant's work for EL and its affiliated companies and RMSL, formerly Equitas Management Services Limited (EMSL), represents less than 1% of Navigant's 2008 total annual revenue of approximately $810 million.

1.7.7 Navigant's revenue from work performed for direct and reinsurance Policyholders of Names reinsured by Equitas is substantially more than the revenue from Equitas.

1.7.8 Navigant has not performed any work for NICO in the past three years, but has done work for other subsidiaries of Berkshire Hathaway.

1.7.9 Navigant's consultants have acted as expert witnesses in cases in opposition to NICO and other subsidiaries of Berkshire Hathaway.

1.8 LIMITATIONS, DISTRIBUTION & USE

1.8.1 This Report has been prepared pursuant to Part VII of FSMA, regarding the Transfer and must not be relied upon for any other purpose.

1.8.2 No liability will be accepted by Navigant or Allan Kaufman as a result of this Report being used for a purpose for which it was not intended.

1.8.3 The review that I conducted does not constitute an audit of the financial resources and liabilities of Equitas, NICO or Speyford.

1.8.4 My obligations and responsibilities in preparing this Report are to be interpreted under the laws of England and Wales.

1.8.5 This Report must be considered in its entirety. Individual sections, if considered in isolation or out of context, may be misleading. Draft versions of this Report must not be relied upon by any person for any purpose. Navigant and I disclaim any liability that may arise if reliance is placed contrary to the guidelines set out in this section 1.8. No reliance should be placed on any advice that is not set out in this Report or any Supplemental Report prepared by me in respect of the Transfer.

1.8.6 In preparing this Report I have relied upon data and information provided by EL, RMSL, Clifford Chance LLP (Clifford Chance) and Baach Robinson & Lewis PLLC (Baach Robinson) on behalf of the Equitas Group. I have not independently verified the accuracy and completeness of any underlying data and information.

1.8.7 I have also used the results of work commissioned by EL from PricewaterhouseCoopers LLP (PwC). The PwC work was prepared on an agreed basis to meet the specific purposes of EL. It was not prepared on the basis that it would be used by me or any other person for the purposes of this Report, or for any other purpose. PwC accept no liability, responsibility or duty of care for my use of their work or for any reliance by any third party on their work. I have held sufficient discussions and performed sufficient work on the findings produced by PwC to satisfy myself that it is reasonable for me to use their findings for the purpose of this Report.

1.8.8 In each section, I indicate the areas in which I have relied on Clifford Chance and Baach Robinson for legal analysis, or Equitas Group or PwC for actuarial and financial analysis, and indicate why I believe that reliance is reasonable.

1.8.9 Appendix IV outlines the information I received.

2 EXECUTIVE SUMMARY

2.1 SUMMARY OF THE TRANSFER

2.1.1 The purpose of the Transfer is to provide legal finality for the Names in respect of their liabilities to Policyholders comprised in the 1992 and Prior Business.

2.1.2 The Transferors are Names at Lloyd's in respect of the 1992 and Prior Business. EL has authority to act on behalf of the Names for the purposes of the Transfer.

2.1.3 The Transferee is Speyford, a wholly-owned subsidiary of Equitas Holdings Limited (EHL).

2.1.4 The transferring business is all of the 1992 and Prior Business at Lloyd's carried on by the Names.

2.1.5 The Transfer involves the following changes in financial security:

1. Names' obligations are transferred to Speyford, a company which will be an authorised insurance company before the date that the Transfer takes effect. My work assumes the authorisation and initial capitalisation will occur on terms consistent with the analysis in this Report;
2. As a matter of English law, in the event of the Transfer, Policyholders will have no claim against Names, including in the event of an insolvency of Speyford; and
3. EL will purchase $1.3bn of additional reinsurance from NICO for a £40m premium. This additional reinsurance is available if the Transfer is effective on or before 31 December 2009.

2.2 PARTIES TO THE TRANSFER/CURRENT STRUCTURE AND CHANGES IN THE EVENT OF THE TRANSFER

2.2.1 In addition to Names, EL and Speyford, the other main parties involved in the Transfer are: Policyholders, Equitas Reinsurance Limited (ERL), NICO and RMSL. The structure currently in place and the current roles of these parties are set out in Figure 2-1. This figure includes the following back-up mechanisms that would most likely only[2] operate in the event of an Equitas Insolvency:

1. Equitas Policyholders Trustee Limited (EPTL);
2. Overseas Trust Funds;
3. Lloyd's bonds and undertakings related to certain Names; and
4. Original Year Names.

2.2.2 The structure that will take effect in the event that the Transfer is sanctioned is set out in Figure 2-2.

2.2.3 Names' obligations are transferred to Speyford, as a matter of English law, and Figure 2-2 shows that Names are replaced by Speyford.

2.2.4 In all other respects, as shown by comparing Figure 2-1 and Figure 2-2, the structure in the event of a Transfer operates in an equivalent manner to the current structure. The back-up mechanisms will be modified prior to the Transfer[3], where necessary, to ensure that Policyholders are not disadvantaged in the event of the Transfer in respect of each of these mechanisms.

2.2.5 In the current structure, Policyholder coverage for claims includes the $13.1bn of remaining reinsurance protection under the NICO Retrocession Agreement as at 31 December 2008. Policyholders can also potentially seek to make recoveries from Names in the event of an Equitas Insolvency.

2.2.6 In the event of the Transfer, the NICO Retrocession Agreement will provide an additional $1.3bn of coverage, but recovery from Names is no longer possible under English law.

[2] Some can operate in the absence of insolvency if a claim is not paid. That does not affect my analysis.

[3] Appendix XIV lists associated documentation that is not yet complete at the date of this Report.

Figure 2-1
Current Structure – Including Back-up Mechanisms in the Event of an Equitas Insolvency
Legal Relationships Associated with Claim Payments

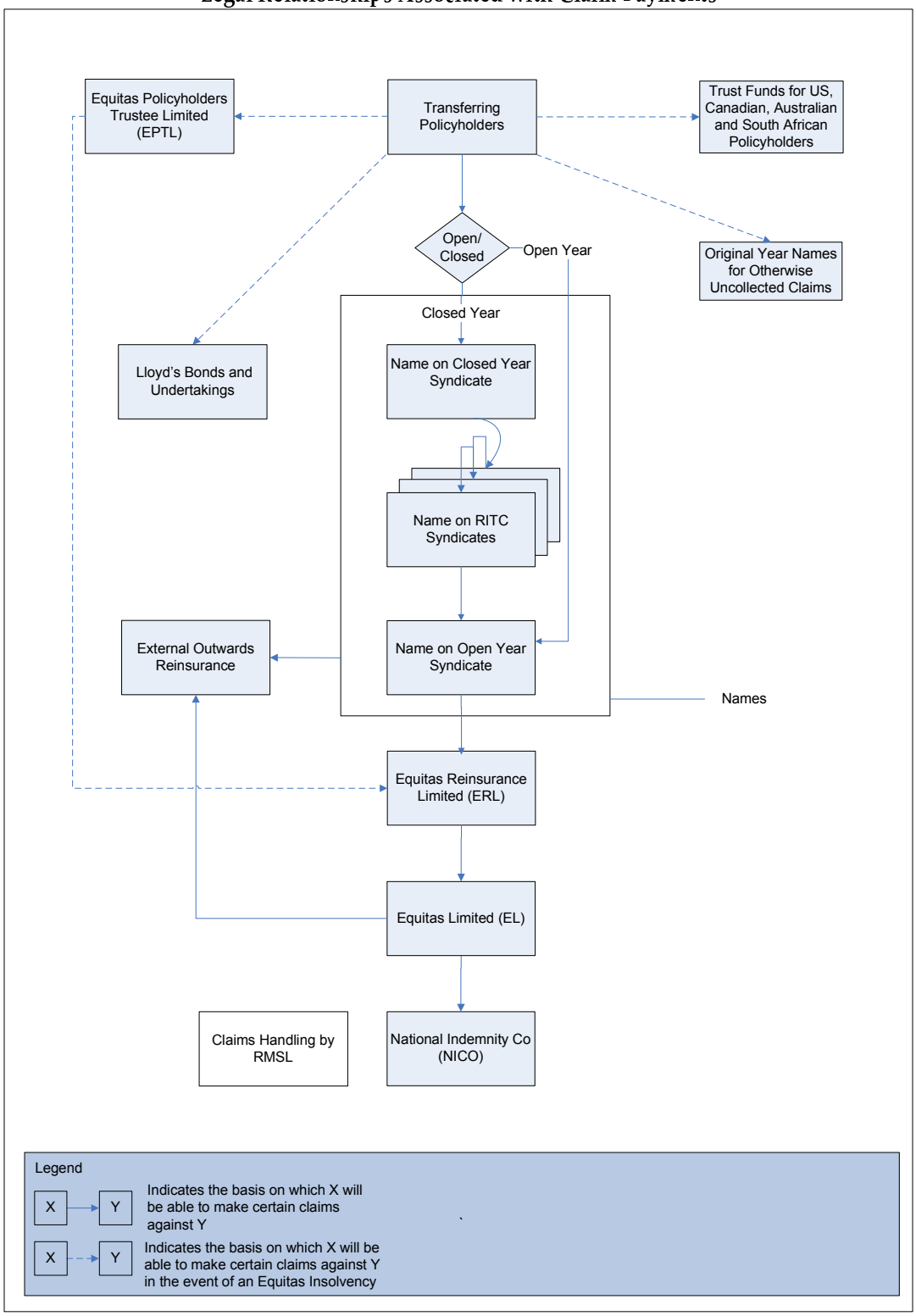
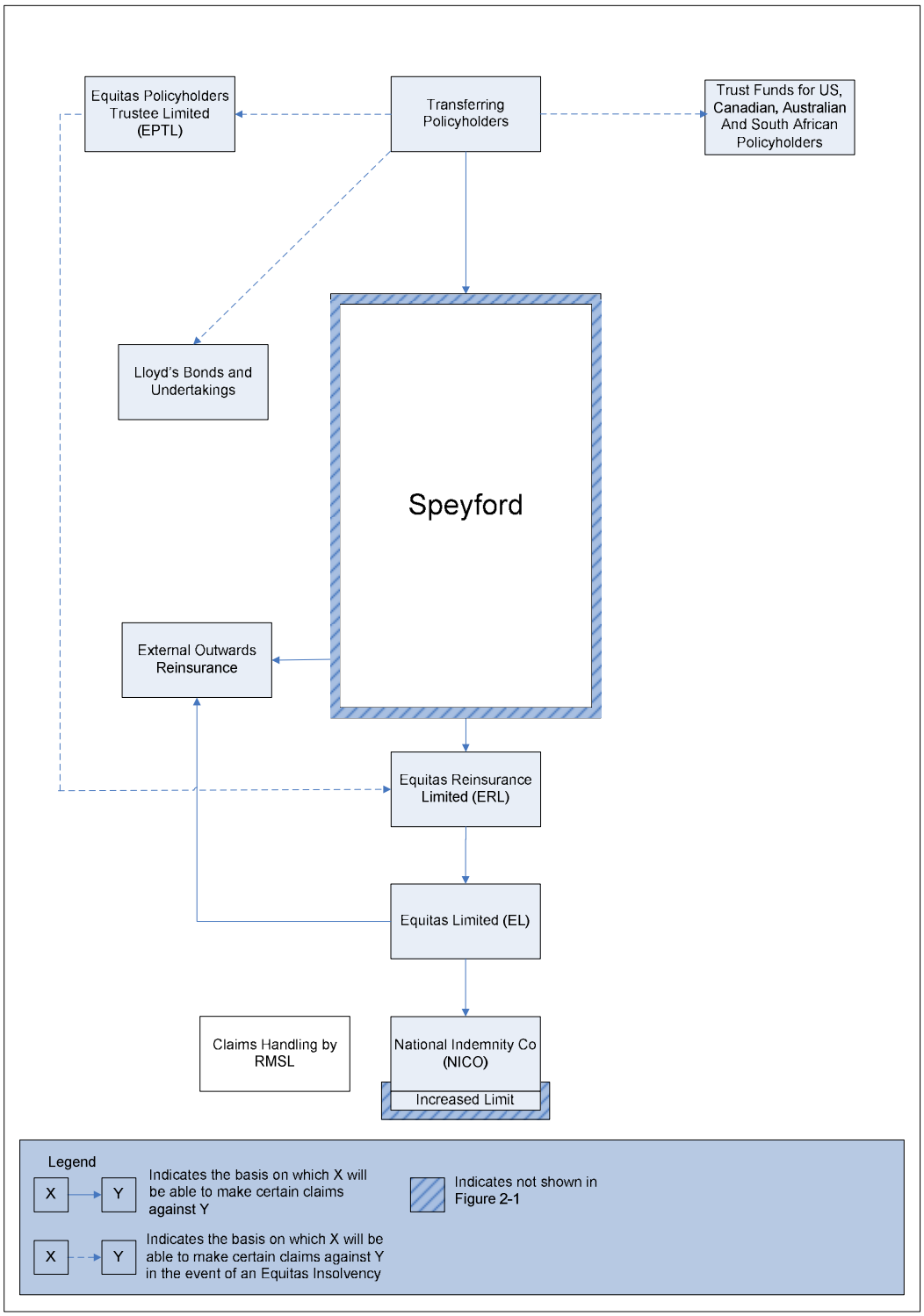


Figure 2-2
Structure in the Event of the Transfer – Including Back-up Mechanisms in the Event of an Equitas Insolvency
Legal relationships Associated with Claim Payments



2.3 ANALYSIS – ASSUMING NO EQUITAS INSOLVENCY

2.3.1 The additional coverage of $1.3bn far exceeds the accumulated value of the £40m premium[4]. Therefore, the Transfer has the following effects:

1. The risk of an Equitas Insolvency is reduced in the event of the Transfer; and
2. In the event of an Equitas Insolvency, Policyholders in total will receive more in the event of the Transfer than they would in the current structure (before any recovery from Names).

2.3.2 To fully examine the effect of the Transfer on Policyholders, it is helpful to first focus on the expected situation where Equitas pays valid claims in full, and then consider the unlikely situation of an Equitas Insolvency.

2.3.3 Absent the unlikely event of an Equitas Insolvency, the aspects of the Transfer that might affect Policyholders are:

1. Claims handling;
2. Credit for Reinsurance for regulatory financial reporting by reinsurance Policyholders (Cedents); and
3. Regulation.

2.3.4 The situation with respect to each of these issues is as follows:

1. RMSL currently handles claims and will continue to do so in the event of the Transfer. Thus, I expect that claims handling will not change in any material respect as a result of the Transfer;
2. US Cedents will be able to continue to take accounting credit for their reinsurance recoverables to the extent Names remain liable as a matter of US law;
3. Regulation remains unchanged except that Names will not have a role in the structure in the event of the Transfer.

2.3.5 Therefore, Policyholders benefit from additional security (paragraph 2.3.1) and there are no disadvantages to Policyholders in the event of the Transfer, assuming no Equitas insolvency.

[4]The accumulated value is the estimated value of £40m as at the projected date at which coverage under the NICO Retrocession Agreement becomes exhausted. £40= $57m (at £1=$1.43, December 2008 exchange rate). The $57m would be held until claims up to $13.1bn were paid, 30 or more years into the future. At that time the accumulated value of $57m is $0.2bn approximately.

2.4 Analysis – In the Unlikely Event of an Equitas Insolvency

2.4.1 To evaluate the effect on Policyholders of the Transfer in the unlikely event of an Equitas Insolvency, it is necessary to estimate the following:

1. The likelihood that claim liabilities occur at various levels;
2. The portion of the claim liability that can be paid by ERL, taking into account coverage from the NICO Retrocession Agreement and funds made available by EHL[5]; and
3. The magnitude of possible recoveries from Names for amounts not covered by item 2.

Actuarial Modelling

2.4.2 I use a Liability Model to assess the likelihood of claim liabilities of various sizes. I then use a Coverage Model to compare the Policyholder position[6] in the current structure to the Policyholder position in the event of the Transfer for each of the claim sizes predicted by the Liability Model.

2.4.3 The models show that in the event of the Transfer, the probability that liabilities can be paid in full without recourse to the back-up mechanisms that would apply in the event of an Equitas Insolvency is estimated at 96.9%, compared to an estimated 95.5% in the current structure[7].

2.4.4 These probabilities show that there is a 4.5% risk of an Equitas Insolvency in the current structure (100% - 95.5%) and a 3.1% (100% - 96.9%) risk of insolvency in the event of the Transfer.

2.4.5 These results mean that in 1.4% of cases (4.5% minus 3.1%) Policyholders would be better off in the event of the Transfer because there would be sufficient cover for their claims to be fully paid whereas their claims would not be fully paid in the event of an Equitas Insolvency under the current structure.

2.4.6 This represents a 30% reduction in the risk of an Equitas Insolvency.

2.4.7 Put another way, these model results mean that in 95.5% of possible outcomes, the Transfer would make no difference to Policyholders; in 1.4% of possible outcomes, Policyholders would be better off in the event of the Transfer (due to

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[5] EHL is not an authorised insurance entity and Policyholders have no rights against EHL. However, in my analysis I assume that EHL assets will be made available by EHL or ERL to pay valid claims.

[6] By Policyholder position I mean the extent to which valid claims are paid from the NICO Retrocession Agreement, plus assets in EL, ERL, EHL and Speyford (in the event of the Transfer), plus recoveries from Names (in the current structure).

[7] These probabilities use the 'base assumptions' for the Liability Model. I test the effect of the Transfer using a range of assumptions. The probability of full payment without recourse to back-up mechanisms is increased in the event of the Transfer regardless of which liability assumption set I use. See Table 7-7 for risk of insolvency with alternative assumptions.

the avoidance of insolvency); and in 3.1% of possible outcomes, further investigation is required to determine whether the Transfer would be beneficial to Policyholders. All the additional work performed herein in connection with comparative outcomes is designed to determine whether, in the 3.1% of possible outcomes in which insolvency would occur both in the current structure and in the event of the Transfer, the Policyholders would be made better or worse off.

2.4.8 EL's track record of measuring liabilities provides some comfort that the low insolvency probabilities are reasonable. In 1996 EL's liabilities gross of External Outwards Reinsurance were estimated at $32.9bn. As at 31 December 2008, $27.0bn of liabilities had been paid and $8.8bn was the estimate for liabilities gross of reinsurance.

2.4.9 Thus, the current estimate of the initial liability is $35.8bn ($27.0+$8.8). Accordingly, after resolving over 70% of the initial liabilities ($27.0/$35.8=70%) the initial estimate has turned out to have been within 10% of the level as estimated at 31 December 2008. The EL position net of External Outwards Reinsurance shows even less adverse movement.

2.4.10 Compared to the 10% unfavourable development observed in the past, the $13.1bn coverage[8] (which is provided on a net of reinsurance basis) provides 67% of margin above the $7.8bn reserve, net of reinsurance, at 31 December 2008.[9]

2.4.11 Increasing the remaining limit of the NICO Retrocession Agreement from $13.1bn to $14.4bn will increase that margin to 84%.

Recovery Rate from Names

2.4.12 It is very unlikely that all Policyholders would fully recover, from Names, any shortfall experienced in the event of an Equitas Insolvency. The recovery from Names (including estates of deceased Names) will be limited by death and bankruptcy of Names, practical and legal impediments to, and costs of, recovery and discounting to take into account the time value of money due to inevitable delays. Moreover, protection from the other back-up mechanisms that would apply on an Equitas Insolvency will have gaps for many Policyholders.

2.4.13 Based on my modelling work, I believe a reasonable Recovery Rate from Names for the average Policyholder is no more than about 20% of the shortfall, and no Policyholder group could reasonably expect a Recovery Rate of more than 30%.

[8] This is the limit remaining for payments from 1 January 2009. It is less than the limit at the time the NICO Retrocession Agreement was agreed because of claim payments through 31 December 2008.

[9] In addition to the NICO cover, claims would be paid from Equitas assets, although the amount from that source is small compared to the NICO cover.

Simple Example

2.4.14 Let us consider a scenario where there is a shortfall of $2.5bn (similar to the average shortfall under the current structure according to the modelling work). Let us then assume that the only assets of Equitas are the $13.1bn of remaining NICO cover and the £40m of funds to be used to purchase the additional cover of $1.3bn. In reality Equitas has other assets, but as these will be unchanged in the event of the Transfer I have ignored them for comparison purposes in this example. The shortfall of $2.5bn corresponds to total claims of $15.8bn ($13.1bn NICO limit plus $0.2bn - see footnote 4) covered by the accumulated value of the £40m not used to purchase the additional cover, plus the $2.5bn shortfall).

2.4.15 In this example, assuming Policyholders might reasonably expect to recover 20% of the shortfall, then Policyholders would recover $0.5bn from Names. The deficit after recovery from Names, which I refer to as the Policyholder deficit, is $2.0bn ($2.5bn minus $0.5bn).

2.4.16 Alternatively, following the Transfer, the Policyholder would expect to receive $14.4bn (the increased limit of the NICO coverage) and the Policyholder deficit would be only $1.4bn ($15.8bn minus $14.4bn), which is less than the Policyholder deficit of $2.0bn in the current structure.

2.4.17 In this example, the Recovery Rate from Names would need to be 44% or more for the Policyholders to be in a better position under the current structure than under the structure following the Transfer[10].

Detailed Analysis

2.4.18 I use the actuarial modelling and the analysis of the Recovery Rate from Names to evaluate the change in Policyholder protection resulting from the purchase of the additional coverage from NICO and the loss of the right under English law to seek recovery of shortfalls from Names.

2.4.19 To assess the change in Policyholder position for all Policyholders combined and for each sub-group of Policyholders, I use the following four measures:

1. The probability of full payment;
2. The difference between the percentage of the time that Policyholders will be better off under the current structure compared with the percentage of time that they will be better off in the event of the Transfer;
3. The difference between average Policyholder deficit as a percentage of total liability amounts (Expected Policyholder Deficit or EPD) in the current structure compared to the structure in the event of the Transfer; and

[10] In this example my analysis ignores back-up mechanisms other than recovery from Names. This is in part to simplify the example and in part because those other mechanisms will generally operate on a similar basis under the current structure and under the structure following the Transfer.

4. The EPD difference with the 0.5% of the most extreme differences being excluded from the calculations (truncated EPD difference).

2.4.20 The change in Policyholder protection in the event of the Transfer varies by type of Policyholder as between:

1. Direct and reinsurance Policyholders;
2. Policyholders for whom claims are currently being paid and Policyholders for whom no claims might be paid for decades into the future. (Short Duration Policyholders vs. Long Duration Policyholders);
3. Policyholders from more recent Years of Account and Policyholders from older Years of Account; and
4. Policyholders who are not covered by Overseas Trust Funds and Policyholders who are covered by such Trust Funds.

2.4.21 I assess the position of each Policyholder group as a whole, and the position of the different types of Policyholder in the Policyholder groups.

2.4.22 Based on my analysis I conclude that:

1. Overall Policyholders gain from the Transfer; and
2. As a result of the change in Policyholder protection no Policyholder group is materially disadvantaged by the Transfer.

2.5 POLICYHOLDER GROUPS AFFECTED BY THE TRANSFER – BACK-UP MECHANISMS

2.5.1 Areas where modifications to the back-up mechanisms have been made or will be made, as listed in Appendix XIV, (as appropriate), to ensure that the Policyholder position is unaltered in the event of an Equitas Insolvency are the following:

1. Set-Off;
2. Access to Trust Funds;
3. Lloyd's guarantees to certain Names which relate to Names' obligations to Policyholders; and
4. Priority of payment between direct and reinsurance Policyholders.

2.5.2 As long as the Equitas Group remains solvent there is no impact on the 1992 and Prior Business.

2.5.3 Table 2-3 below sets out the different Policyholder groups, the aspects of the Transfer that might affect them and reasons why those aspects do not materially disadvantage any Policyholder group. Table 2-3 also references the sections of the Report where the issues are discussed in detail.

Table 2-3

	Policyholder Group or Other Party	Issues	Rationale	Index
1	All Policyholders	Financial effect of increased reinsurance limit and transfer of obligations from Names to Speyford.	A further $1.3bn of reinsurance coverage from NICO ensures Policyholders overall are financially more secure in the event of Transfer than before the Transfer.	sections 5 – 7
2	All Policyholders	NICO security-In the event of a NICO insolvency the effect of the Transfer is to increase the exposure to loss by $1.3bn. In the event of the Transfer Policyholders could no longer seek recovery from Names for shortfalls in the event of a NICO insolvency.	NICO has an insurer financial strength rating of A++ by AM Best and AAA by S&P. Also a review of publicly available financial information indicates that these financial ratings do not appear inappropriate.	section 8
3	All Policyholders	Claims handling and run-off management.	RMSL currently handles claims and will continue to do so in the event of the Transfer. The NICO Retrocession Agreement sets out terms to ensure proper handling of the run-off. The claims handling is not expected to change in any material respect purely as a result of the Transfer.	section 4.2

	Policyholder Group or Other Party	Issues	Rationale	Index
4	All Policyholders	Regulation.	All corporate entities involved in the event of the Transfer structure will be regulated in an equivalent manner to the way in which corporate entities in the current structure are regulated. Names will no longer have a role in the structure in the event of the Transfer, as a matter of English law.	section 4.3
5	All Policyholders/ Speyford	As a corporate entity, Speyford can propose a Scheme of Arrangement while Names are not able to do so under the current state of law.	The purpose of this Report is to report on the terms of the Transfer in accordance with s109 FSMA. Nonetheless, given market interest, I describe how the Transfer gives rise to the ability to implement Schemes of Arrangements.	section 4.4
6	Reinsurance Policyholders	Policyholders' right to Set-Off claims by Names against obligations due to them from Names, particularly for reinsurance Policyholders who are both Policyholders and reinsurers of business of the Names.	Any Set-Off available under the current structure would be available in the event of the Transfer if there is an Equitas Insolvency.	section 4.5

	Policyholder Group or Other Party	Issues	Rationale	Index
7	Reinsurance Policyholders in the USA and certain other jurisdictions	Credit for Reinsurance - Right to record the full value of reinsurance recoveries due for solvency reporting purposes in the USA.	In the event of the Transfer, US Cedents should continue to be allowed to take accounting credit for their reinsurance recoverables to the extent that Names remain liable on such Policies as a matter of US law.	section 4.6
8	Reinsurance Policyholders	Priority of payment in the event of insolvency of Speyford – Speyford assets are subject to the Insurers (Reorganisation and Winding Up) Regulations 2004 that gives priority to direct Policyholders over reinsurance Policyholders. Absent the Transfer, reinsurance and direct Policyholders would be treated equally.	The vast majority of assets would flow through EPTL in the event of an insolvency. Hence the impact of the Directive on reinsurance Policyholders is small, and the Transfer is not disadvantageous to reinsurance Policyholders.	sections 4.7 and 5-7
9	Policyholders of PCW and Warrilow Names	PCW and Warrilow - Extent of the continuation of the benefits of Lloyd's bonds relating to PCW and Warrilow Names and Lloyd's undertaking relating to PCW Names.	Arrangements will have been put in place in order to preserve the benefits currently available to these Policyholders. (Note 1)	section 4.8

	Policyholder Group or Other Party	Issues	Rationale	Index
10	Policyholders of Names benefiting from other Lloyd's Guarantees	Lloyd's Guarantees - beyond those relating to PCW and Warrilow.	Lloyd's will provide an undertaking assuring the same protection to these Policyholders in the event of the Transfer. (Note 1)	section 4.9
11	US, Canadian, Australian and South African Policyholders	Overseas Trust Funds - Extent of continuation of existing benefits from Trust Funds.	In the event of the Transfer, either no special arrangements will be needed or, if they are, arrangements will be put in place in order to ensure that available protections to these Policyholders continue in the event of the Transfer. (Note 2)	section 4.10
12	Non-Transferring Policyholders	Some Names who underwrote 1992 and Prior Business also underwrote in 1993 and subsequent years. Policyholders of those Names might be considered Non-Transferring Policyholders with respect to their 1993 and subsequent Policies.	The Names insuring the Non-Transferring Policyholders will be more secure in the event of the Transfer and so better able to meet any claims by Non-Transferring Policyholders.	section 4.11
13	Names as Policyholders.	RITC and other Inter-Syndicate Reinsurance Policies (ISR).	Names as Policyholders with respect to the RITC and other Inter-Syndicate Reinsurance (ISR). As a matter of English law, the obligations and offsetting benefits from RITC and ISR are both extinguished in the event of the Transfer.	section 4.12

Note 1: The documentation to achieve this objective is not complete. I will review that documentation and provide a Supplemental Report indicating whether it achieves the intended purposes.
Note 2: To the extent that there are further discussions with overseas regulators regarding Overseas Trust Funds or Credit for Reinsurance, I will report on any implications with respect to impact on Policyholders in my Supplemental Report.

2.6 IMPACT OF TRANSFER ON OTHER PARTIES

2.6.1 Other parties who are affected by the Transfer are set out in Table 2-4.

Table 2-4
Identification of Other Parties Who are Affected

	Policyholder Group or Other Party	Issues	Rationale	Index
14	Names as other parties	Names as individuals are affected by the Transfer.	There will be an extinction of any potential liability of Names, as a matter of English law, in the event of the Transfer. The legal position of Names with assets in overseas jurisdictions where the Transfer is not recognised is largely unchanged from the present position under the law of those jurisdictions, but the risk of an Equitas Insolvency is reduced in the event of the Transfer and such Names will have the benefit of an indemnity from Speyford under the terms of the Scheme.	section 4.13
15	External outwards Reinsurers	Reinsurers, particularly those other than ERL, EL, NICO, and Names with respect to Inter-Syndicate Reinsurance.	Essentially all External Outwards Reinsurance has been assigned to ERL/EL at the time of R&R. Any residual interest in the External Outwards Reinsurance will transfer with the liabilities in the event the Transfer is sanctioned. The business will continue to be managed by RMSL on the same basis as at present. Hence there will be no adverse impact on External Outwards Reinsurers.	section 4.14

	Policyholder Group or Other Party	Issues	Rationale	Index
16	Other insurers - Mesothelioma Claims	Mesothelioma Claims-Other insurers may have higher or lower claim costs depending on the extent to which Equitas meets its financial obligations.	Insurers benefit from the increase in the NICO limit. They are not disadvantaged in the event of the Transfer.	sections 4.15
17	FSCS	FSCS does not currently cover claims arising from 1992 and Prior Business.	I will discuss the effect, if any, on the FSCS in the event of the Transfer in a Supplemental Report.	section 4.16
18	Lloyd's	Lloyd's might be affected in various ways.	Lloyd's will be a party to the amendments of various undertakings and arrangements which are currently in place. These amendments are necessary to provide at least the same level of protections for the benefit of Policyholders in the event of the Transfer as they currently enjoy. There is no reason to expect this to adversely impact Lloyd's.	section 4.17

2.7 CONCLUSION

2.7.1 I have considered the Transfer and its likely effect on Policyholders of 1992 and Prior Business written at Lloyd's which is reinsured by ERL.

2.7.2 I have analysed the likely effect of replacing the current structure, including the current security offered by the NICO Retrocession Agreement and the unlimited liability of Names with the limited liability of Speyford plus an additional $1.3bn of coverage under the NICO Retrocession Agreement.

2.7.3 I have analysed the other changes in the structure associated with the Transfer.

2.7.4 I have examined the position of all Policyholders combined, and I have considered the position of each relevant Policyholder group separately.

2.7.5 I have also examined the likely effect on the other parties identified in Table 2-4.

2.7.6 I will provide a Supplemental Report addressing the effect, if any, on the FSCS in the event of a Transfer and the result of my review of the material identified in Appendix XIV.

2.7.7 Subject to the findings in that Supplemental Report, and any other Supplemental Reports, I have concluded that there are no groups of Policyholders, or other parties, listed in Table 2-4, that are materially disadvantaged in the event of the Transfer.

2.8 RELIANCES

2.8.1 This Executive Summary relies on data, information and advice from Clifford Chance, Baach Robinson, Equitas and Lloyd's as specified in each section of the Report.

3 OUTLINE OF THE PART VII TRANSFER OF BUSINESS

3.1 PURPOSE OF THE TRANSFER

3.1.1 This section describes the parties currently involved in the 1992 and Prior Business, the parties that would be involved in the event of the Transfer and the rationale for the Transfer.

Purpose of the Transfer

3.1.2 The purpose of the Transfer is to provide legal finality for the Names in respect of their liabilities to Policyholders comprised in the 1992 and Prior Business at Lloyd's.

Current Structure

3.1.3 Section 3.2 describes the parties that have responsibilities with respect to claim obligations, in the current structure and if assets in Equitas, including reinsurance available under the NICO Retrocession Agreement, are sufficient to pay claims in full.

3.1.4 To the extent that EL assets, including NICO reinsurance, are not sufficient to pay valid claims in full, there are back-up mechanisms that may respond to certain types of claims. Section 3.3 explains these mechanisms.

3.1.5 Section 3.4 describes the reinsurance arrangements and regulatory framework that apply in respect of the current structure.

Changes in the Event of the Transfer

3.1.6 Section 3.5 describes the parties and changes (if any) in responsibility for claim obligations that become relevant in the event that the Transfer occurs.

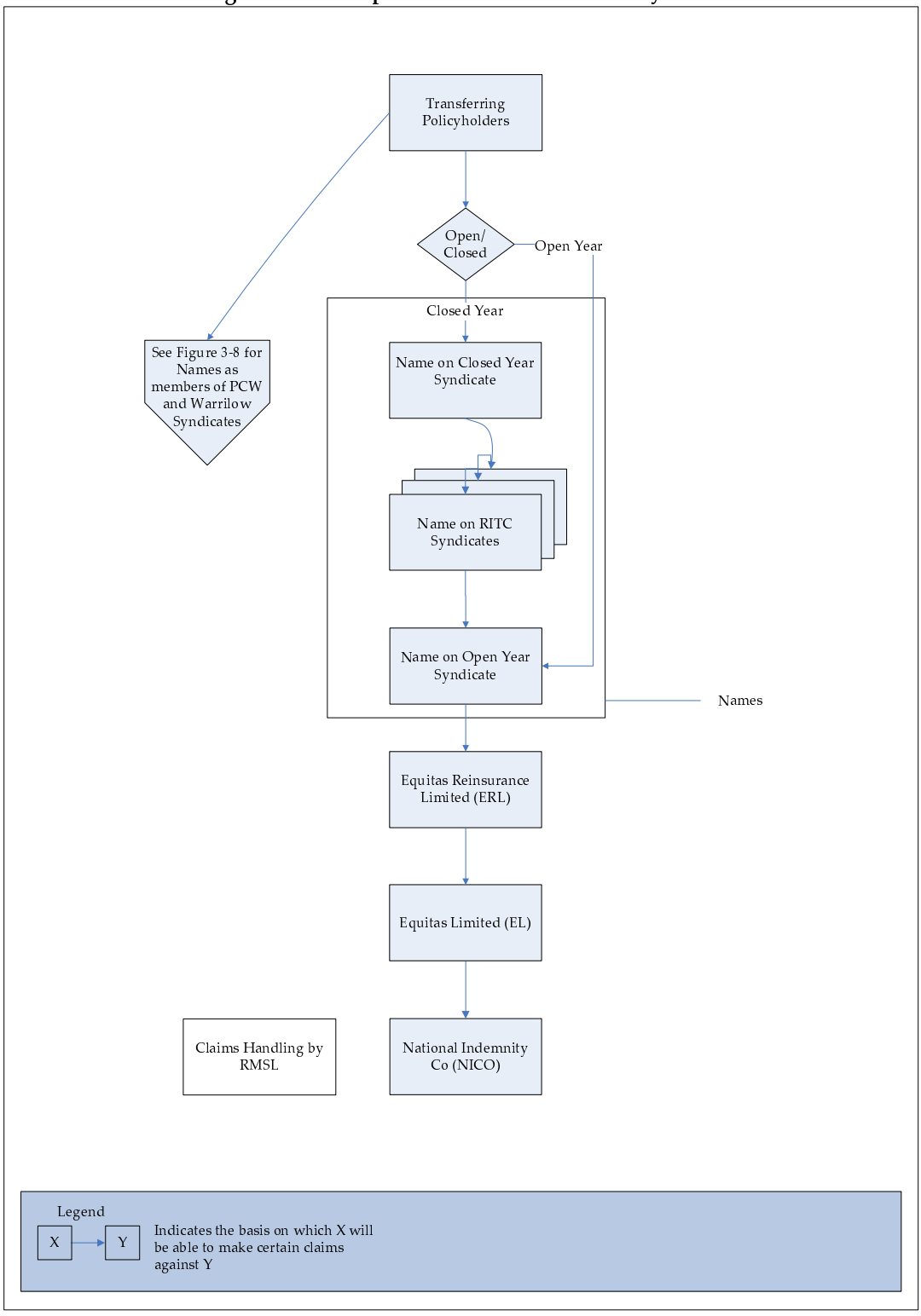
3.2 CURRENT STRUCTURE – ASSETS SUFFICIENT TO PAY CLAIMS IN FULL

3.2.1 The parties associated with the Transfer from a claims perspective are shown on Figure 3-1[11].

3.2.2 The nature of each of these parties is discussed in the sections following Figure 3-1.

[11] For under 10% of the claims there is a somewhat different structure described beginning at paragraph 3.2.40.

Figure 3-1
Current Structure – Assets Sufficient to Pay Claims in Full
Legal Relationships Associated with Claim Payments



Policyholders

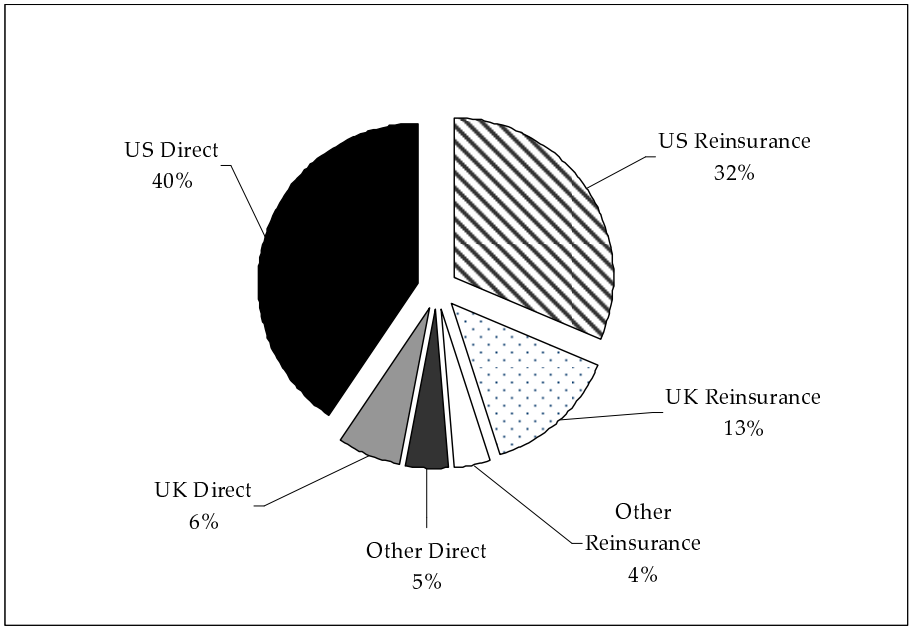
3.2.3 The Transferring Policyholders are represented by the box at the top of Figure 3-1.

3.2.4 In this Report, unless specifically identified otherwise, the term 'Policyholder' includes:

1. Policyholders who are reinsured by the Names, sometimes called Cedents, (in which case the contract is a reinsurance or retrocession contract); as well as
2. Policyholders who have a direct insurance contract with the Names.

3.2.5 Figure 3-2 and Figure 3-3 below show the types of claims that these Policyholders currently have or are expected to have in the future.

Figure 3-2
Unpaid Claims Estimates by Location of Policyholders and Direct vs. Reinsurance Policyholders

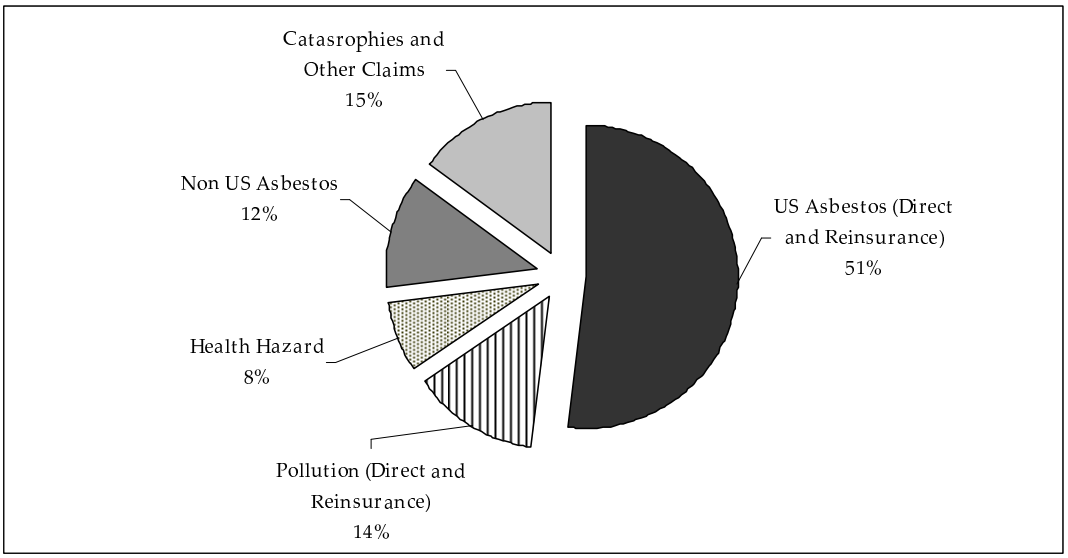


Source: Equitas; Claims Gross of External Outwards Reinsurance as at 31 December 2008.

3.2.6 From Figure 3-2 it can be seen that:

1. 51% of the unpaid claims estimate relate to direct Policies (40% + 6% + 5%), 49% are from reinsurance Policies (32% + 13% + 4%); and
2. 72% of claims are from US Policyholders (40% + 32%), 19% are from UK Policyholders (6% + 13%) and 9% are from Policyholders in the rest of the world (5% + 4%).

Figure 3-3
Unpaid Claims Estimates by Type of Claim



Source: Equitas; Claims Gross of External Outwards Reinsurance as at 31December 2008.

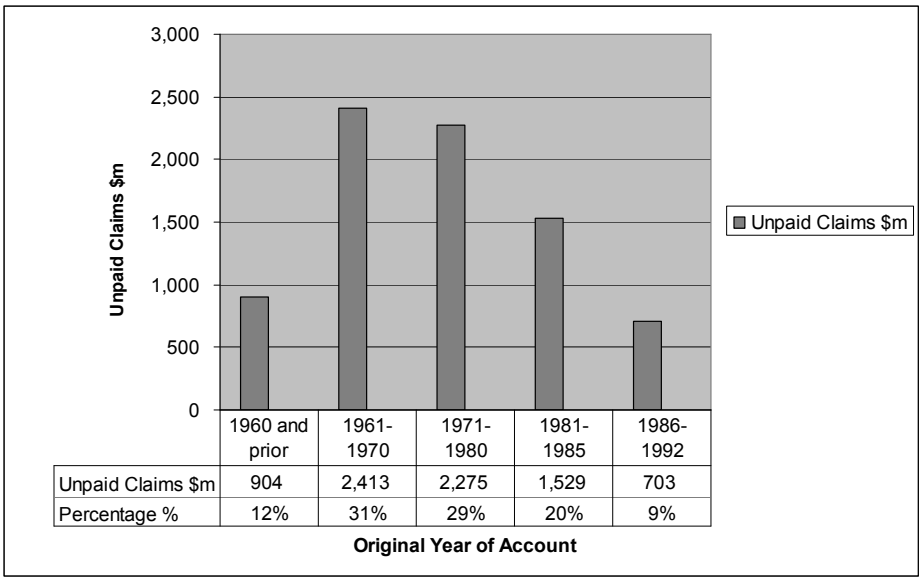
3.2.7 From Figure 3-3 above it can be seen that:

1. 73% of claims relate to Asbestos (US), Pollution and Health Hazard claims (51% + 14% + 8%);
2. 12% to other Asbestos claims; and
3. 15% to all other types of claims including, marine, aviation, motor and Catastrophes.

3.2.8 Pollution and Health Hazard claims are mostly US, and non-US Asbestos claims are mostly UK.

3.2.9 While the Policies that could be affected, in the event of the Transfer, could theoretically extend over a period of a century or more, most of the claims, by value, relate to Policies written during the 40 year period preceding 1992 as shown in Figure 3-4 below.

Figure 3-4
Unpaid Claims Estimate by Original Year of Account



	1960 and prior	1961-1970	1971-1980	1981-1985	1986-1992
Unpaid Claims $m	904	2,413	2,275	1,529	703
Percentage %	12%	31%	29%	20%	9%

Source: Equitas; Claims Net of External Outwards Reinsurance as at 31 December 2008. Percentage total is equal to 101% due to rounding.

Names

3.2.10 The Names are individuals who participate or participated as Members of Lloyd's and acted as underwriters under rules specified by Lloyd's.

3.2.11 The Names operated in groups of underwriting members called Syndicates, in which each Name had a Several (not Joint) share of the Liability arising from insurance and reinsurance contracts underwritten by the Syndicate. Names have unlimited personal liability in respect of these Policies, although subject to the limits applicable to each Policy.

3.2.12 Syndicates operated as a series of one year ventures; each called a Syndicate Year or Year of Account or Syndicate Year of Account.

3.2.13 Thus a Policyholder has a claim against each of the Names on each of the Syndicates for each Year of Account that underwrote the insurance. I refer to these as Original Year Names, in their capacity as such, and I refer to the particular Syndicate Year which underwrote the Policy that covers the claim as the Original Year Syndicate.

3.2.14 The number of Names and Syndicates by year is illustrated in Table 3-5 which follows.

Table 3-5
Number of Names and Syndicates by Years of Account

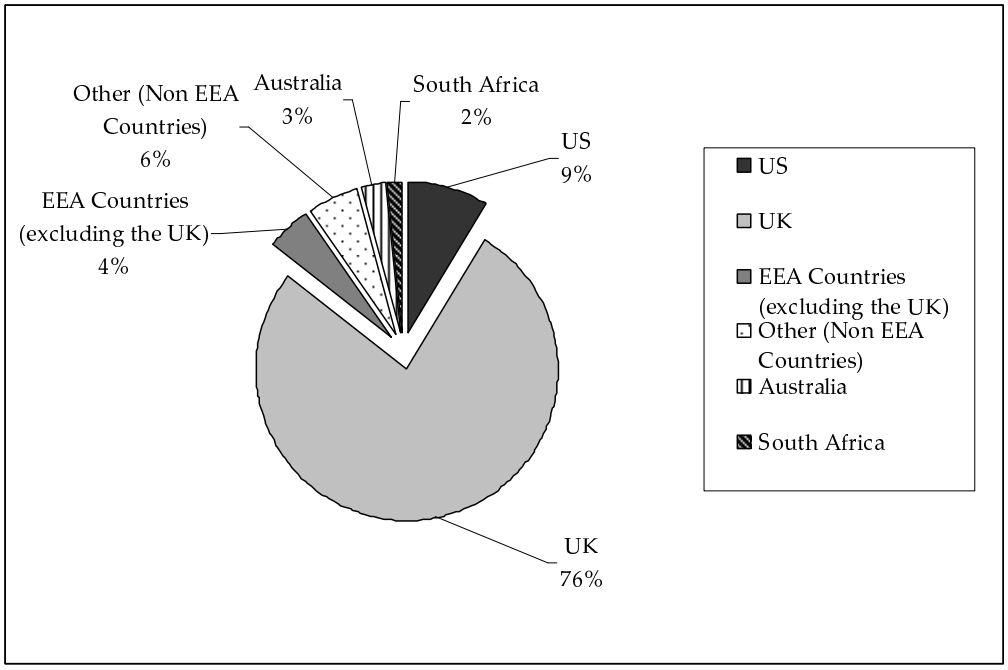
	A	B
Years of Account	**Average Number of Syndicates**	**Average Names/Year**
1950-1960	559	4,059
1961-1970	655	5,699
1971-1980	708	10,396
1981-1985	816	22,068
1986-1992	654	28,644
Average	659	12,678

Note: As a Name was typically a member of a number of Syndicates, the number of Names per Syndicate is greater than the ratio of column B to column A.
Source: Equitas

3.2.15 From 1952 to 1992 there were 41,554[12] people who underwrote business as Names.

3.2.16 Figure 3-6 below shows the geographical distribution of Open Year Names as at 2008.

Figure 3-6
Geographical Distribution of Open Year Names



Source: Equitas; Distribution of Open Year Names addresses

[12] Source: Lloyd's underwriting member statistics

3.2.17 From Figure 3-6, it can be seen that:

1. 80% of Open Year Names are located in the UK and in other EEA (European Economic Area) Countries (76% + 4 %);
2. 9% are located in the USA; and
3. 11% in other geographical locations (Australia 3 % + South Africa 2 % + other Non EEA Countries 6 %).

Reinsurance to Close (RITC) - Closed Year Syndicates and Closed Year Names

3.2.18 Figure 3-1 refers to Names with respect to Closed Year Syndicates, Reinsurance to Close (RITC) and Open Year Syndicates. In this section I explain the concept of RITC; Closed Year Syndicates and corresponding Closed Year Names; and Open Year Syndicates, and corresponding Open Year Names.

3.2.19 The Syndicates operated as a series of annual ventures, each generally referred to as a Syndicate Year of Account, writing contracts for one year. The Syndicate handled and paid claims on that Year of Account for three years. At the end of the third year, it was expected to reinsure its remaining liability, known or unknown.

3.2.20 That RITC was typically reinsured by the next Syndicate Year of Account—usually underwritten by a very similar group of Names. In exchange for premium, the reinsuring Syndicate Year of Account provided reinsurance without limit in time or amount.

3.2.21 The RITC enabled the earlier Syndicate Year of Account to 'close' and make a 'final' accounting of profit or loss. This accounting was 'final' in that it permitted the distribution of profits or allocation of losses to Names but not in the legal sense of terminating the liabilities of the Original Year Name to Policyholders. It did, however, permit any Names with RITC to cease underwriting and resign from Lloyd's if they so chose.

3.2.22 Syndicates having purchased RITC are referred to as 'Closed Year Syndicates', and the Names on them, in their capacity as such, are referred to as 'Closed Year Names'.

3.2.23 Claims outstanding from Original Year Syndicates which have become Closed Year Syndicates by purchasing RITC represent approximately 91% of the claims outstanding[13].

[13] The exact split between Open Year and Closed Year is not available. 91% represents the liability from Years of Account 1985 and prior (Figure 3-4). Some 1985 and prior liabilities were not closed and the Years of Account that did not close may have had larger than average liabilities. However, many 1986 and subsequent Years of Account were closed.

Open Year Syndicates and Open Year Names

3.2.24 Beginning in the 1980's there was a growing and increasingly uncertain liability for Asbestos, Pollution, and other major claims. That made it impossible for some Syndicates to determine an appropriate premium for RITC. Such Syndicates could not close and so remained 'open' beyond the normal three years.

3.2.25 By the end of 1995 there were 770 Syndicates that had not obtained RITC. Syndicates earlier than 1993 would have been expected to have closed by this point, yet around 20% of the Syndicates that had not obtained RITC were 1991 Syndicates, around 20% were 1990 Syndicates, 9% were 1989 Syndicates, and there were also a number of prior year Syndicates.[14][15]

3.2.26 These Syndicates are referred to as '1992 and Prior Year Open Year Syndicates', or simply 'Open Year Syndicates'. The Names on those Syndicate Years, in their capacity as such, are referred to as 'Open Year Names'.

3.2.27 Each Name would typically be a member of several Syndicates. Thus a Name might be a Closed Year Name with respect to some Syndicates and an Open Year Name on other Syndicates.

Names and Policyholders

3.2.28 A typical Policy will have been underwritten by a number of Syndicates and each Syndicate would have been comprised of a number of Names.

3.2.29 If a Policy was renewed from year to year, as was typical, Original Year Names participating on each year of coverage would be similar but would change, albeit slowly, from year to year.

3.2.30 Each of those Original Year Names would normally be party to a RITC contract with a subsequent year's set of Names. Once RITC was purchased these Original Year Names become Closed Year Names with respect to these Original Year contracts. Those Names providing reinsurance cover under the RITC (RITC Names) would have RITC with a further set of Names, and so on, until either there was no succeeding Year of Account or the point was reached when Syndicate-based RITC was no longer available. The Names on that 'open' year – that is the unreinsured year - in their capacity as such, are called Open Year Names. These Open Year Names were only able to purchase RITC with Equitas as described below beginning at paragraph 3.2.33.

[14] Some of these were open because in R&R Lloyd's prohibited the normal RITC of many open years which could have been closed by normal RITC, because Lloyd's wanted all 1992 and prior business to be reinsured by the same reinsurer, i.e. ERL

[15] Source: Equitas

3.2.31 Initially, the RITC Names are likely to overlap significantly with the group of Original Year Names. Over time, successive years of RITC Names would be increasingly composed of new Names.

3.2.32 Notwithstanding the relationships created between Names by virtue of RITC, RITC does not create an obligation to Policyholders although the Syndicate Year providing RITC handled their claims and made payment in respect of them. The arrows in Figure 3-1 show that, for example, Original Year Names on the Original Syndicate Year have an obligation to Policyholders and that RITC Names on an RITC contract have an obligation to the Names purchasing the RITC. That does not mean that RITC Names, in their capacity as such, have an obligation to Policyholders of the Original Year Names.

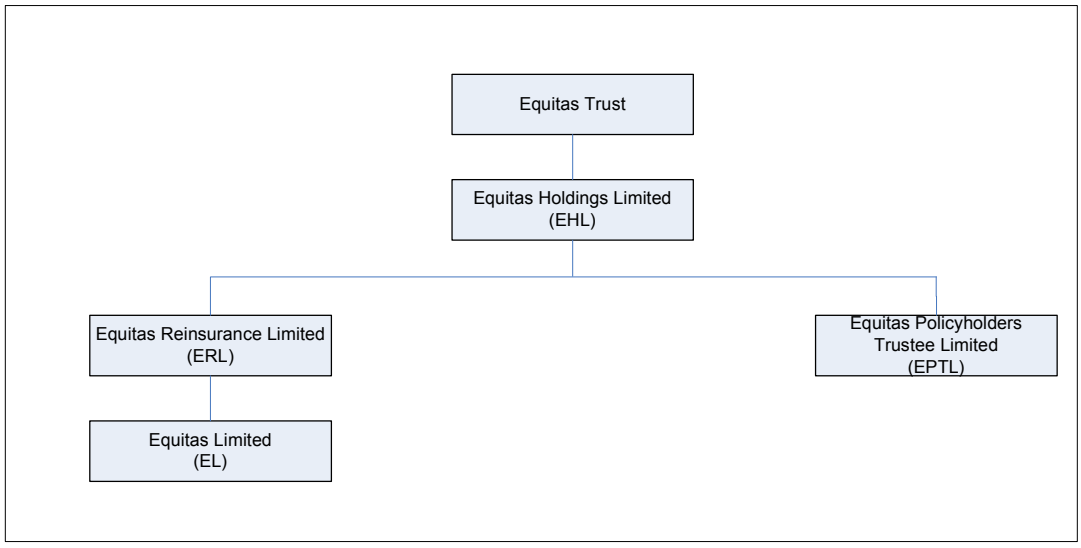
Equitas Group

3.2.33 As many Syndicate Years of Account were unable to close, in 1996 a plan to fund and manage their obligations was implemented. This is referred to as Reconstruction & Renewal or R&R.

3.2.34 As part of R&R, the Equitas Group, composed of EL, ERL, EPTL and EHL, was created.

3.2.35 Figure 3-7 sets out the current Equitas Group corporate structure. Figure 3-1, shown previously, only shows ERL and EL, as these are the relevant parties with respect to claims unless there is an Equitas Insolvency.

Figure 3-7
Current Equitas Group Corporate Structure



3.2.36 The Open Year Names at 31 December 1995, in respect of 1992 and Prior Business, were reinsured by ERL (under the Equitas Reinsurance Contract) and ERL was then in turn reinsured by EL (under the Equitas Retrocession Agreement). The Closed Year Names were also reinsured under the Equitas Reinsurance Contract, in that the Closed Year Names are indemnified by

ERL/EL if their RITC were to fail or be set aside[16]. The Equitas Reinsurance Contract gave ERL responsibility for handling claims against Closed Year Names and Open Year Names by their Policyholders. The Equitas Retrocession Agreement delegated that responsibility to EL.

NICO

3.2.37 NICO is shown as the last box of the chain in Figure 3-1. In March 2007 EL retroceded its reinsurance obligations to NICO under the NICO Retrocession Agreement. The premium comprised Equitas Group assets less £172m, plus £72m from Lloyd's. The NICO Retrocession Agreement covers payments of up to $14.4bn from 1 April 2006. This is a cover of $5.7bn above the $8.7bn Equitas net reserves at 31 March 2006.

3.2.38 In addition, NICO took on responsibility for the costs and management of the run-off. In the ordinary course, unless EL exercises rights to handle claims on its own, NICO's claims handling responsibility ends only when claims are fully settled or when the NICO Retrocession Agreement limit is fully exhausted. This run-off obligation is otherwise unlimited in duration and amount.

3.2.39 Prior to March 2007 claims staff and other staff were employed to handle the run-off of the 1992 and Prior Business by a subsidiary of EHL originally called Equitas Management Services Limited (EMSL). As part of the NICO Retrocession Agreement, this company was acquired by a subsidiary of Berkshire Hathaway and renamed Resolute Management Services Limited (RMSL). RMSL was appointed to manage the run-off of 1992 and Prior Business pursuant to the NICO Retrocession Agreement.

PCW and Warrilow Syndicates and Intermediate Reinsurers

3.2.40 Prior to R&R, Names belonging to certain Syndicate Years of Account, referred to as the PCW Names and the Warrilow Names, had (directly or indirectly) reinsured their liabilities in respect of such Syndicate Years of Account into Lioncover Insurance Company Limited[17] (Lioncover) and Centrewrite Limited (Centrewrite), respectively. This is illustrated in Figure 3-8.

3.2.41 Lioncover is an FSA authorised reinsurance company, incorporated in 1987 and a Lloyd's subsidiary. It reinsured the liabilities of a number of Syndicates formerly managed by PCW Underwriting Agencies Limited, and referred to as PCW Syndicates. The PCW Syndicates participated in underwriting Policies generating long-tail claims. Long-tail claims are typical of Equitas' business.

[16] The indemnification is a commitment by ERL, not a commitment by the Open Year Names.
[17] Originally, Syndicate 9001 was a Syndicate formed for the purpose of providing RITC to the PCW Syndicates and the Syndicate 9001 business was reinsured by Lioncover. In 1999, following a novation of Syndicate 9001 liabilities to Lioncover, Lioncover became the reinsurer of the PCW Syndicates and Syndicate 9001 was removed from the reinsurance chain.

3.2.42 Centrewrite is an FSA authorised insurer incorporated in 1991 and is also a Lloyd's subsidiary. It conducted the following business:

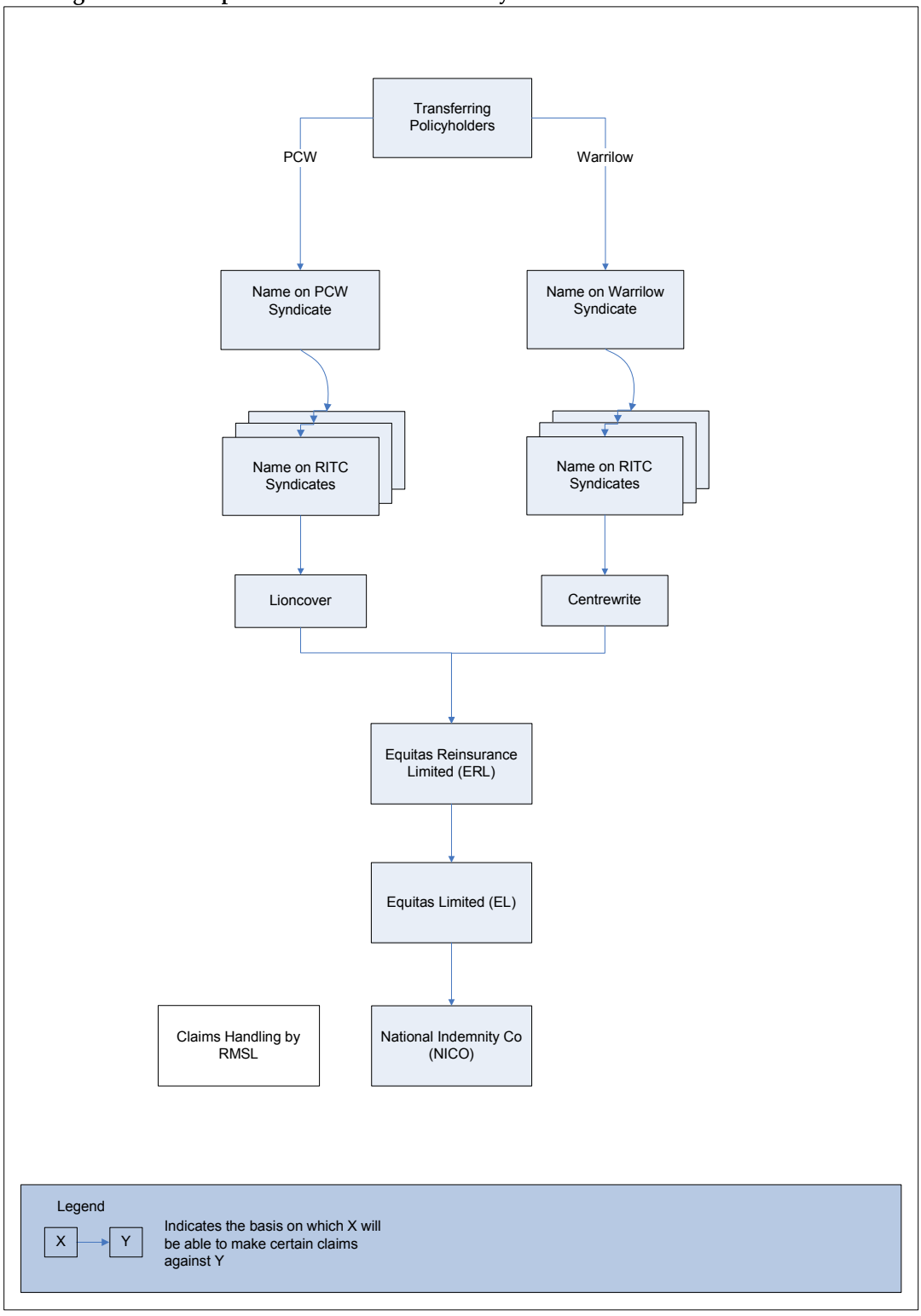
1. Reinsured 1985 and 1987 Years of Account of Warrilow Syndicate 553;
2. Provided Estate Protection Plan (EPP) coverage; and
3. Wrote individual whole account Policies for Names with respect to 1992 and Prior Business, including such Policies which were written during the 1993 and 1994 Years of Account.

3.2.43 Liability of the PCW Names and Warrilow Names, reinsured by Lioncover and Centrewrite respectively, was retroceded into ERL (and hence to EL) under the Lioncover Reinsurance Contract and Centrewrite Reinsurance Contract respectively[18].

3.2.44 The reinsurance chain of responsibility for claims from PCW and Warrilow Syndicates into ERL, EL, and NICO is shown in Figure 3-8.

[18] The Warrilow 1985 and 1987 Year of Account were also reinsured by the Equitas Reinsurance Contract. The fact that the retrocessions occurred via the two routes does not affect my analysis.

Figure 3-8
Current Structure – Assets Sufficient to Pay Claims in Full
Legal Relationships Associated with Claim Payments – PCW and Warrilow Business



3.3 CURRENT STRUCTURE INCLUDING BACK-UP MECHANISMS IN THE EVENT OF AN EQUITAS INSOLVENCY

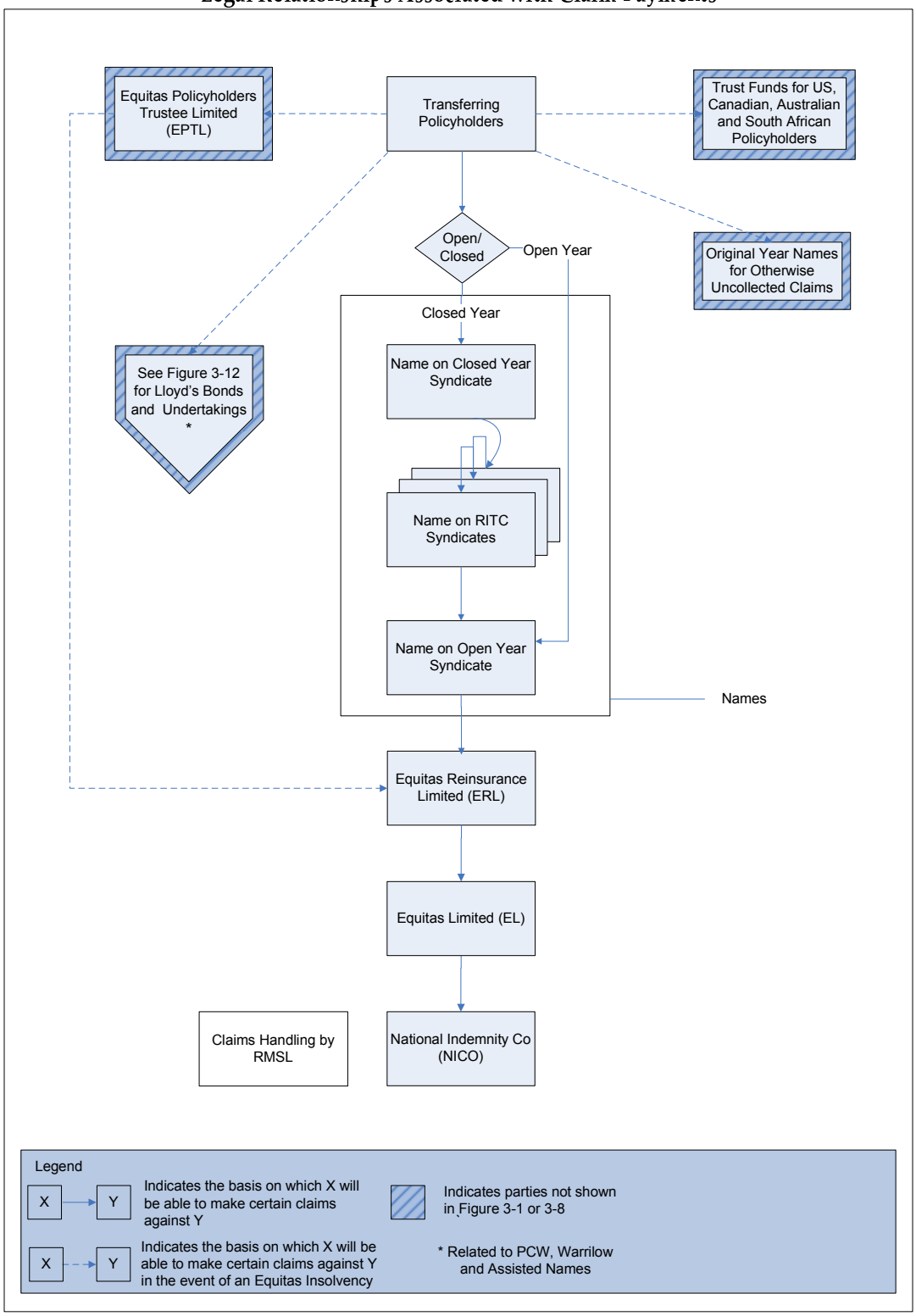
3.3.1 Figure 3-9, below, repeats the information from Figure 3-1 and further includes four back-up mechanisms that could be utilized in the event of an Equitas Insolvency (although they would apply outside of an Equitas Insolvency if claims were not paid). These are:

1. EPTL, part of the Equitas Group;
2. Trust Funds;
3. Names, with respect to otherwise uncollected claims; and
4. Lloyd's bonds related to liabilities underwritten by PCW and Warrilow Syndicates; Lloyd's undertaking to certain PCW Names; and other Lloyd's commitments to Names.

3.3.2 These mechanisms are discussed below. The details of the operation of each of these mechanisms will be affected by the circumstances at the time of any Equitas Insolvency, if that were to arise. Therefore, I discuss the role in general and the concepts that would be likely to affect their operation in an Equitas Insolvency.

3.3.3 In addition, I discuss the extent to which there are any further Lloyd's obligations.

Figure 3-9
Current Structure – Including Back-up Mechanisms in the Event of an Equitas Insolvency
Legal Relationships Associated with Claim Payments



EPTL

3.3.4 Under the Equitas Reinsurance Contract, Names assigned the rights they had against ERL in respect of its reinsurance obligations to them to EPTL.[19]

3.3.5 EPTL holds these rights in trust. If funds are adequate to pay claims in full, then EPTL is inactive provided funds are paid. In the event of an Equitas Insolvency, EPTL is required to use the reinsurance proceeds paid to it by ERL to pay the claims of underlying creditors (i.e. Policyholders).

3.3.6 The mechanism for EPTL payments in the event of an Equitas Insolvency will depend on the actual circumstances at the time. For the purposes of the analysis which follows I assume the following:

1. The process is triggered when financial analysis determines that assets available to pay Policyholders are insufficient, and an Administrator[20], [21] is appointed to manage the Equitas Group in the interests of its creditors;
2. RMSL continues to determine appropriate values for claims, until available assets are exhausted. This seems likely as NICO is responsible for funding claims handling costs until the NICO Retrocession Agreement limit is exhausted;
3. NICO continues payments (either directly or indirectly via EL and ERL) to EPTL, in respect of 100% of valid claims, up to the limit as provided in the NICO Retrocession Agreement;
4. Claims payments on behalf of Policyholders are held in abeyance until such time as a suitable distribution methodology is determined. Funds would accumulate with investment returns in EPTL during that time; and

[19] EPTL does not currently cover PCW business.. The terms of the Transfer and related changes to Lloyd's underwriting bonds with respect to Lioncover will not disadvantage Policyholders or Names as discussed in section 4.8.

[20] The only available procedures would be liquidation, provisional liquidation or administration. Administration is generally considered the most appropriate choice for a reinsurance insolvency. I do not believe that the precise form of insolvency is material in my analysis.

[21] The R&R Retrocession has a provision called 'proportionate cover' which would allow Equitas to reduce its insurance obligation to Names and to make payments on their behalf accordingly. In the event of an insolvency, it is unlikely that the Equitas board would seek to implement the contractual proportionate cover provisions without also invoking a traditional insolvency procedure given the complex and unprecedented issues that would arise in such circumstances. Administration is generally considered the most appropriate procedure. It is likely that any ultimate distribution and final settlement arrangement following Administration would make payments which would broadly reflect what would happen under the proportionate cover provisions, as explained in paragraph 5.2.6 (17). My analysis assumes that Equitas will go into Administration rather than proceeding on the basis of proportionate cover provisions alone. I do not believe that the precise form of insolvency is material to my analysis.

5. When a distribution methodology is determined, EPTL distributes to Policyholders interim partial payments. EPTL will invest the difference between the amount it receives from NICO (100% of the claims) and the amount it pays to Policyholders by the way of partial interim distribution. In insolvencies it is not unusual for there to be interim distributions before a final distribution rate can be determined or an overall settlement agreed.

3.3.7 Figure 3-9 shows the contingent obligation of ERL to make payments to EPTL and the related obligation of EPTL to make payments to Policyholders.

Trust Funds - US

3.3.8 The main characteristics of the US Trust Funds are described in Table 3-10 below.

Table 3-10
US Trust Funds

Protection	Scope
LATF	The Lloyd's American Trust Funds (LATF) applies to 1992 and prior[22] USD denominated business at Lloyd's. The LATFs are not a single fund but rather constitute separate Trust Funds for each underwriting member of Lloyd's. The LATFs are available to pay claims on USD denominated business, regardless of the location of the Policyholder.

125[22] The LATF was modified in March 2009. It previously applied to business prior to 1 August 1995.

Protection	Scope
US EATF	The US Equitas American Trust Fund (US EATF) is available to protect pre-1993 direct and reinsurance Policyholders under Policies with premium and/or limits in USD. Funds available in the US EATF amount to $2.5bn at 31 December 2008 ($3.1bn at 31 December 2007). In addition to these invested assets, the EATF also has rights to reinsurance recoverable on claims paid to date. Reinsurance recoverable on claims that will be paid in the future reduce the liabilities of the EATF. For financial reporting purposes assets of the US EATF include a share of the NICO Retrocession. As claims are paid on Policies covered by the US EATF, NICO can withdraw those amounts from the US EATF. Thus, US EATF asset levels are reduced by claim payments. The New York Insurance Department (NYID) can permit withdrawals by NICO if the assets in the EATF (excluding also the assets of certain reinsurance receivables and the reinsurance credit from NICO) exceed the liabilities of the Trust Fund by an agreed margin. In the normal course there is no 'top-up' requirement if the amount in the US EATF drops below the liabilities secured by such Trust Fund, whether on account of decreases in value of the assets therein, or deterioration of the liabilities so covered or for any other reason. In the event of a NICO downgrade or material default NICO must provide a LOC, or establish a trust, and the EATF allocation of the LOC or trust is outlined in paragraph 9.1.15. The amount of assets held in the US EATF does not increase or decrease the NICO limit. The US EATF protects Policyholders in two ways. It assures that covered Policyholders will receive at least a minimum amount of the coverage available to EL under the NICO Retrocession. It also provides a minimum protection for covered Policyholders if NICO were to become insolvent. In section 9 I illustrate the manner in which the Trust Fund protects Policyholders and the relationship between the coverage limit in the NICO Retrocession Agreement and the Trust Fund amounts. Since the completion of the NICO Retrocession Agreement, the US EATF is sometimes called the NICO American Trust Fund (NATF). In this Report, I refer to it as the EATF or US EATF.

Protection	Scope
JATFs	There are two Joint Asset Trust Funds (JATFs). Each has funds amounting to $112m (December 2008). The JATFs support not only the business written by the Names reinsured by Equitas but also the 1993 and later year business. As such they support Lloyd's status as an accredited insurer and reinsurer in the USA. If EATF funds were fully used by Policyholders of Names reinsured by Equitas, JATF funds could be used to further support those Policyholders. If Lloyd's did not 'top up' the JATFs, then the status of Lloyd's as an accredited insurer and reinsurer in the USA could be in jeopardy. Moreover, the JATF for US Cedents (JATF-R) supports Lloyd's Underwriter's status as reinsurers for whom US Cedents may take accounting credit for it in the USA. If EATF funds were fully used by Policyholders of Names reinsured by Equitas, JATF-R funds could be used to further support US Cedent Policyholders. If Lloyd's did not maintain the JATF-R at the then required level (currently $100m), then the status of Lloyd's Underwriter's as reinsurers for whom US Cedents may take accounting credit for in the USA could be in jeopardy. The relationship of the JATF's and Lloyd's Underwriter's status in the USA as an insurer/reinsurer and as a reinsurer for whom accounting credit is permitted in the USA might change in the future. For example, reciprocal international recognition of insurance entities might make Trust Funds unnecessary.
Illinois Trust Fund (ILTF)	$140m at December 2008. Applies to certain business written in Illinois. Unlike the US EATF it needs to be 'topped-up' if estimated liabilities exceed assets. Unlike the US EATF, claims cannot be paid from ILTF assets.

Note: Source: Equitas

3.3.9 The LATF, US EATF and JATF trust agreements contain provisions setting out when these Trust Funds are deemed "inadequate". For the purposes of the EATF one of the circumstances which would result in the New York regulator taking the fund into conservation is where an order is made by a competent court, or resolution passed, for the winding up of ERL or a provisional liquidator or Administrator is appointed in respect of ERL.

3.3.10 The JATF Trust Deed provides that where all the JATF funds are placed into conservation no Policyholder claims will be paid during a 12 month period unless a court orders otherwise. The New York regulator may order the trustee to transfer to him the trust assets and he may distribute them in accordance with New York insurance company liquidation law. There is no provision in the Trust Deeds for distribution of the trust assets by the trustee in the case of an insolvency, recognising the fact that the New York regulator would do so in accordance with New York law.

Trust Funds - Other

3.3.11 There are also Trust Funds in Australia, Canada and South Africa. Their main features are described in Table 3-11 below.

Table 3-11
Other Trust Funds

Trust Fund	Features
Australia	Letter of Credit (LOC) AUD$150m at December 2008 (AUD$155m at December 2007) The LOC amount is set by the Australian Prudential Regulation Authority (APRA) annually.
Canada	CAD$34m at December 2008 (CAD$35m at December 2007) Regulated by The Office of the Superintendent of Financial Institutions (OSFI). Amount is reset annually.
South Africa	14.5m ZAR – Funded by Lloyd's

Note: Source: Equitas

Trust Funds Overall

3.3.12 For Policyholders eligible for Trust Fund protection a dividend ratio would be determined taking into account Trust Fund assets and related liabilities.

3.3.13 Policyholders might receive different levels of protection in different countries. In the event of an Equitas Insolvency, there could be different dividend rates; one for each of five Trust Funds - USA, Canada, Australia, South Africa and 'all other'. Nonetheless, no creditor would receive less than the percentage applicable to 'all other'.

Names

3.3.14 Figure 3-9 shows the Original Year Names in two capacities. In the normal course, if there is no Equitas Insolvency, valid claims are paid in full with funds from ERL, EL and NICO. This is represented by the arrows in the centre of the Figure 3-9 extending from Policyholders to Names, ERL, EL and NICO.

3.3.15 If there were an Equitas Insolvency payment from ERL, EL and NICO would be partial and would be made through EPTL as shown on the left side of Figure 3-9.

3.3.16 In the event of an Equitas Insolvency, Policyholders could pursue further recoveries from Original Year Names. That right is represented by the arrow from Transferring Policyholders to Original Year Names shown on the right side of Figure 3-9.

3.3.17 My analysis does not include the Personal Stop Loss (PSL) or EPP mechanisms that many Names used to protect themselves against calls for additional funds. Under the Equitas Reinsurance Contract, coverage from PSL Policies was used to fund Equitas. Thus, no coverage is available from these PSL Policies for future claims. EPP Policies include time limits on coverage that have expired and in any event these Policies terminated when RITC was obtained[23]. Hence these Policies provide no further coverage.

[23] The Equitas reinsurance is treated as RITC for this purpose

Lloyd's Bonds and Undertakings Relating to PCW and Warrilow Syndicates and Assisted Names

3.3.18 The position of the Policyholders (in the current structure) of Names who underwrote the PCW and Warrilow Syndicate business is illustrated in Figure 3-12. Figure 3-12 shows their position and the back-up mechanisms which would take effect in the event of an Equitas Insolvency.

3.3.19 Before R&R, Lloyd's provided an undertaking and two bonds in respect of PCW and Warrilow Syndicates.

1. Lloyd's issued an undertaking to certain PCW Names to protect them against further calls for funds. This is shown at (A) on Figure 3-12;
2. Lloyd's provided a bond to Lioncover to guarantee the adequacy of the reserves for Lioncover. This bond is shown as (B) on Figure 3-12; and
3. Lloyd's also provided a bond to Centrewrite to guarantee the adequacy of the reserves for Centrewrite. This bond is shown as (B) on Figure 3-12.

3.3.20 Of the total Equitas unpaid claims estimates, approximately 8% relates to PCW Syndicates and less than 1% relates to Warrilow Syndicates.

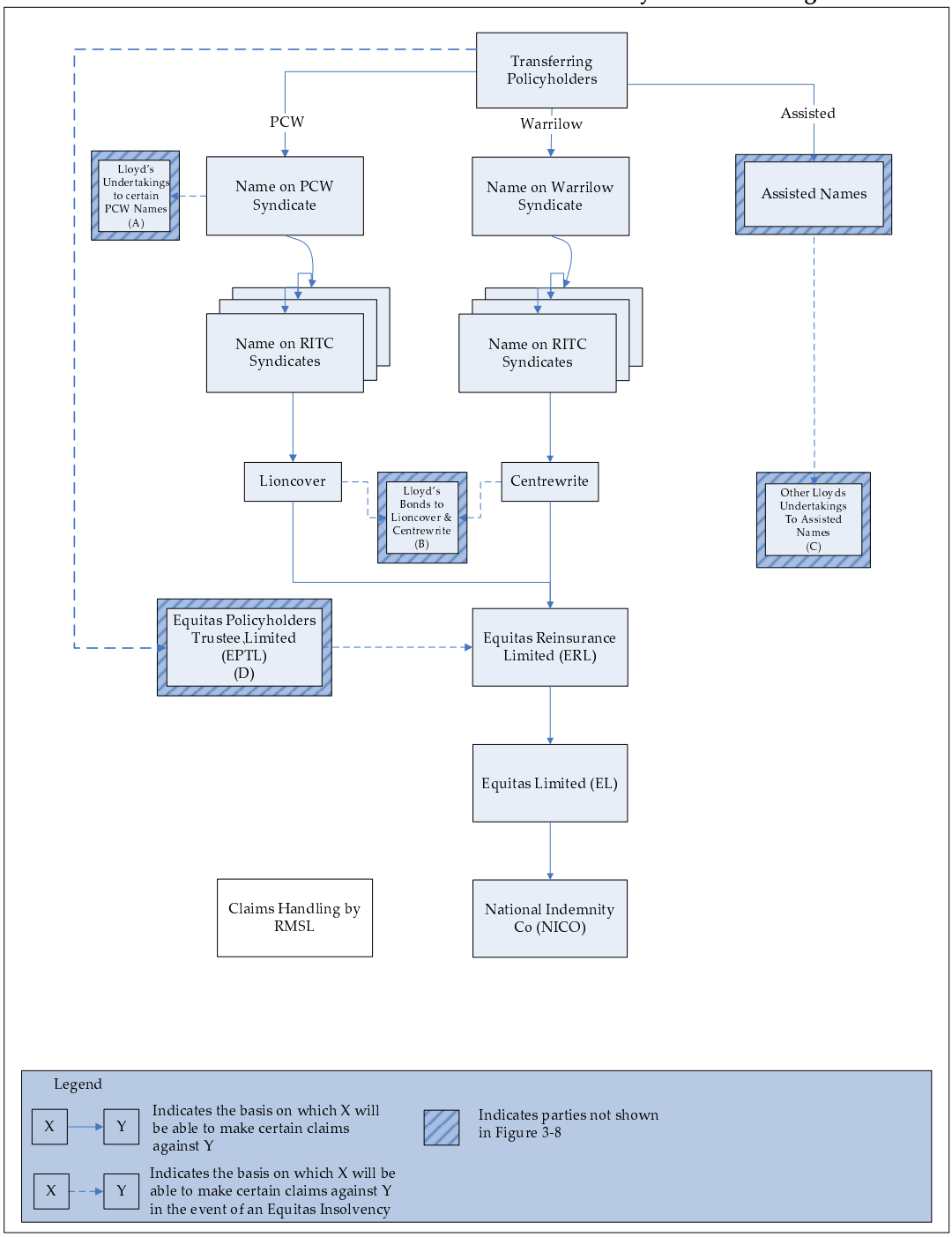
3.3.21 These bonds and the undertaking do not benefit Policyholders directly. They benefit Policyholders only to the extent that there are claims which are covered by the Lioncover or Centrewrite reinsurance (and which are not paid by EL).

3.3.22 Lloyd's has also issued a number of undertakings to certain Names including Names in various Hardship Agreements or otherwise. These undertakings commit Lloyd's to protecting the Names from further calls for funds. Some of the undertakings can terminate if the Name's financial condition changes or at the option of Names, but the undertakings are otherwise unlimited in amount and duration. Many, but not all of the undertakings have been terminated. I refer to these as the Assisted Names Undertakings and they are shown as (C) on Figure 3-12.

3.3.23 Any call under the Lloyd's bonds or undertakings would be met by Lloyd's assets at the time of such call. Lloyd's could seek to levy an assessment on Lloyd's members, but such assessments are subject to approval through Lloyd's procedures and are not assured. The Lloyd's bonds and undertakings are therefore subject to practical financial limits[24]

[24] This is the position in respect of Lloyd's New Central Fund. The Old Central Fund also requires criteria to be met before payment can be made.

Figure 3-12
Current Structure – PCW and Warrilow and Business with Lloyd's Undertakings and Bonds



3.3.24 These bonds and the undertaking issued by Lloyd's are unlimited in amount and duration.

3.3.25 The solid connecting lines running down the centre of Figure 3-12 show that except in the unlikely event of an Equitas Insolvency, Policyholder obligations

associated with PCW Names, Warrilow Names and Assisted Names will be covered by ERL, EL and NICO in a similar manner to all other Policyholder obligations.

3.3.26 In the unlikely event of an Equitas Insolvency, Figure 3-12 also shows that Policyholder obligations associated with Warrilow Names and Assisted Names would be met, in part, by EPTL (shown as (D)). EPTL does not cover PCW business in the current structure, as EPTL was not interposed in the PCW-EL reinsurance chain). This contingent relationship to EPTL is shown by the dotted lines connecting Policyholders to EPTL and then to ERL.

3.3.27 Figure 3-12 also shows that the Lloyd's undertaking to PCW Names (labelled A) and the Lloyd's undertakings to Assisted Names (labelled C) would be triggered by Policyholder claims against those Names. Figure 3-12 also shows that the Lloyd's bonds to Centrewrite and Lioncover (labelled B) would be triggered if Lioncover or Centrewrite were unable to meet their obligations to PCW Names or Warrilow Names respectively, as a result of Policyholder claims against those Names. As those relationships are contingent on an Equitas Insolvency, they are shown in dotted lines on Figure 3-12.

3.3.28 I am informed by Lloyd's that:

1. They are not aware of any guarantee, undertakings or bonds from them to Names other than those referred to in paragraphs 3.3.19 - 3.3.27**;**
2. Lloyd's has no legal obligation to make payments specifically to address a general shortfall in Equitas assets; and
3. In particular, any obligations of Lloyd's that might otherwise change as a result of this Transfer will be retained through the mechanisms described in section 3.5**.**

3.3.29 Commercially, Lloyd's is connected to the 1992 and Prior Business in two ways:

3.3.30 Firstly, the Policies were issued through Lloyd's, and preserving a long history of paying all valid claims in full has commercial value (although Lloyd's has no legal obligation in this regard).

3.3.31 Secondly, for US situs Policyholders covered by the JATFs, there is a further possible connection as described in Table 3-10.

Lloyd's Obligations—To Assist Policyholders in Other Ways

3.3.32 With respect to administrative help in pursing recoveries from Names, under the terms of the R &R settlement arrangements, Lloyd's agreed that it would not pursue Accepting Names (the vast majority of Open Year Names) for further contributions to pay claims.

3.3.33 There is no such agreement with respect to Closed Year Names who were not also Open Year Names, but Lloyd's has only limited authority over those Names as they, like most of the Open Year Names, are no longer members of Lloyd's. (This is not to say that Policyholders could not pursue relevant Closed Year

Names or Open Year Names but any Lloyd's Market Reorganization Order (LMRO) would apply to them.)

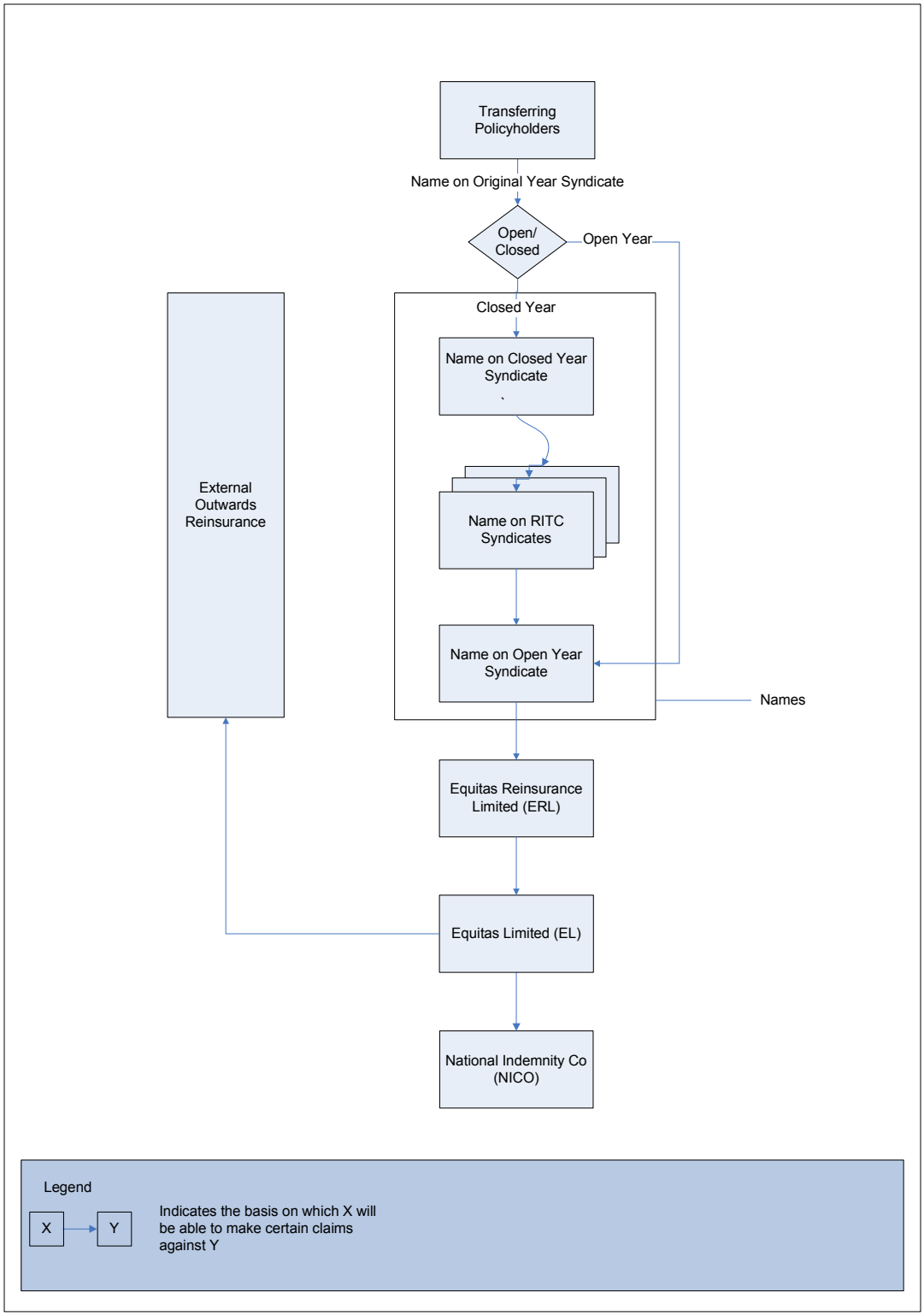
3.4 REINSURANCE AND REGULATION IN THE CURRENT STRUCTURE

Reinsurance

3.4.1 The reinsurance that currently applies to the 1992 and Prior Business, illustrated on Figure 3-13, can be categorised as follows:

1. The NICO Retrocession Agreement (risks retroceded from EL to NICO);
2. The Equitas Reinsurance Contract, Lioncover Reinsurance Contract and Centrewrite Reinsurance Contract (from Open Year Names, Lioncover and Centrewrite, respectively, to ERL) and the Equitas Retrocession Agreement (from ERL to EL);
3. Reinsurance provided by entities external to Names and Syndicates (External Outwards Reinsurance);
4. Inter-Syndicate Reinsurance (Reinsurance amongst the Names) including:
    a. The RITC to subsequent year Syndicates; and
    b. Other Inter-Syndicate Reinsurance (this is not shown in Figure 3-13).
5. Reinsurance from PCW and Warrilow Syndicates into Lioncover and Centrewrite respectively and hence into ERL (not shown in Figure 3-13).

Figure 3-13
Current Structure - External Outwards Reinsurance



3.4.2 In the normal course, the net effect of the reinsurance (referred to in paragraph 3.4.1(4) above) on ERL, EL and NICO is nil as there are off-setting amounts between Syndicates. However, on some occasions the Inter-Syndicate Reinsurance can affect External Outwards Reinsurance not placed with Names and Syndicates (paragraph 3.4.1(3) above).[25]

Regulation

3.4.3 RMSL is regulated as an insurance intermediary for claims handling and related work[26]; and

3.4.4 EL, ERL, Lioncover and Centrewrite are FSA regulated (re)insurers.

3.4.5 The Names (Open Year, Closed Year, PCW and Warrilow) are subject to FSA regulation as follows:

1. For Names who ceased to be underwriting members of Lloyd's earlier than 24 December 1996 the requirement to be authorised under FSMA was disapplied in respect of their Lloyd's business under the FSMA 2000 (Exemption) Order 2001. Thus, these Names are currently not subject to supervisory rules. Names who had ceased underwriting prior to 1992 and who had no Open Year Syndicates that were reinsured directly into Equitas generally fall into this category.
2. Names who ceased to be underwriting members of Lloyd's on or after 24 December 1996 but prior to the date on which FSMA came into force obtained revocable section 68 orders under the Insurance Companies Act 1982 (ICA) which disapplied certain requirements of ICA such as routine financial reporting and solvency requirements. These Names in common with Names who ceased to be underwriting members of Lloyd's after the date on which FSMA come into force, are now subject to s320(1) of FSMA which allows such a Name to carry out contracts of insurance he has written at Lloyd's whether or not he is an authorised person. However, they are also subject to s320(3) of FSMA, which enables the FSA to impose such requirements on Names to protect Policyholders as it considers appropriate.
3. Continuing Names (i.e. Names who underwrote 1993 and subsequent business as well as 1992 and Prior Business) and who are still Lloyd's members, are subject to section 316 of FSMA, by virtue of which the general prohibition does not apply to them unless so directed by the FSA. This means that such Names are neither authorised not exempt under FMSA unless the FSA directs otherwise. The FSA has so far deemed it unnecessary

[25] Per Equitas. I have not sought to identify any such transactions. A simple example is where Syndicate A provides direct insurance. Syndicate B reinsures Syndicate A. External reinsurer C provides retrocession cover to Syndicate B. The relationship between A and B, a transaction amongst Names,affects the claims covered by external reinsurer C.

[26] Article 39A of Regulated Activities Order.

to apply the general prohibition to insurance business at Lloyd's, but has applied some of the core provisions of FSMA to Lloyd's members.

3.4.6 NICO is a regulated insurer in the USA[27].

3.4.7 The Trust Funds are regulated in their home jurisdictions (USA, Canada, Australia and South Africa).

[27] NICO is regulated in Nebraska, its state of domicile, and also in the other states where it is licensed.

3.5 STRUCTURE IN THE EVENT OF THE TRANSFER - INCLUDING BACK-UP MECHANISMS

3.5.1 Figure 3-14 overleaf, shows new parties and changes in legal relationships (under English law) relating to claims payments if the Transfer is approved.

3.5.2 The changes in the event of the Transfer are described below.

Speyford

3.5.3 Speyford is a limited company registered in England and Wales. I have been advised that Speyford will be authorised as an insurance company with terms of authorisation consistent[28] with my analysis in the Report before the Transfer is sanctioned;

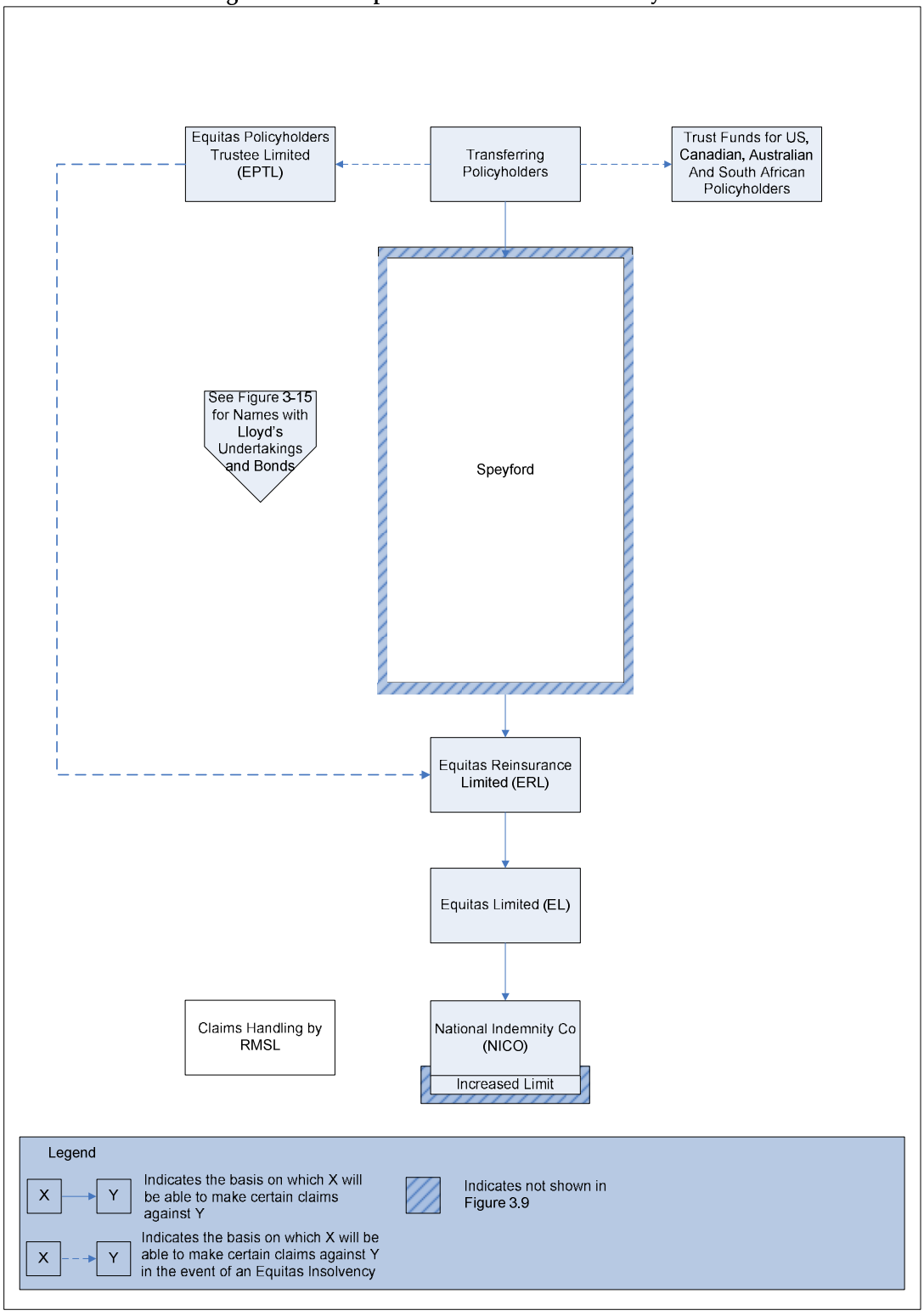
3.5.4 Names' obligations are transferred to Speyford;

3.5.5 By virtue of the Court order giving effect to the Transfer, Policyholders no longer have a right of action under English law against Names, and therefore have no recourse against Names for unpaid claims in the event of an Equitas Insolvency in respect of the Transferring Policies.

3.5.6 EL plans to capitalise Speyford at the level of the minimum capital requirement (MCR) of approximately (£16m), subject to FSA approval.

[28] The terms are: Speyford capital is not materially larger than £20m assumed in the Actuarial modelling; EHL, EL or ERL commitments to provide further capital to Speyford are limited in amount to the extent that the modelling analysis is not materially affected; Speyford authorisation is largely limited to 1992 and Prior Business.

Figure 3-14
Structure in the Event of the Transfer – Including Back-up Mechanisms in the Event of an Equitas Insolvency
Legal Relationships Associated with Claim Payments



NICO

3.5.7 The limit on the NICO coverage will be increased by $1.3bn.[29]

EPTL, PCW, Warrilow and Assisted Names

3.5.8 As explained in paragraph 3.3.20, before R&R, Lloyd's provided an undertaking and two bonds in respect of the PCW and Warrilow Syndicates. Arrangements will be put in place so that, following the Transfer, Names or the Syndicates and Policyholders are not in a worse position. To this end the position in the event of the Transfer in relation to the new arrangements (including three new trusts created within EPTL for the PCW and Warrilow business) is illustrated in Figure 3-15.

3.5.9 These three additional trusts to be created within EPTL are called the Lloyd's EPTL Trust, the PCW EPTL Trust, and Warrilow EPTL Trust.

3.5.10 With respect to Centrewrite and Warrilow Names:

1. The Lloyd's bond to Centrewrite will remain in place as shown in Figure 3-15; and
2. The existing Centrewrite reinsurance will transfer to Speyford. Speyford will assign its rights against Centrewrite to EPTL to hold on trust under, the Warrilow EPTL Trust, in favour of Warrilow Policyholders. Figure 3-15 shows the contingent claim EPTL has against Centrewrite. However, the assignment is not depicted on Figure 3-15.

3.5.11 With respect to Lioncover and PCW Names:

1. The Lioncover bond from Lloyd's will be replaced by an undertaking from Lloyd's to EPTL for EPTL to hold subject to the Lloyd's EPTL Trust (Lioncover Substitute Undertaking). The Lioncover Substitute Undertaking will be for the benefit of the PCW Policyholders. Lioncover will no longer have any obligations in the event of the Transfer (the intention of Lloyd's being to dissolve Lioncover), and, therefore, Lioncover is not shown in Figure 3-15;
2. Speyford will assign its rights against ERL in respect of the PCW business to be held subject to the PCW EPTL Trust; and
3. The undertaking by Lloyd's to assenting PCW Names that they would no longer be called upon to pay or provide as members of the PCW Syndicates further monies towards underwriting liabilities or incurred by them as such will remain in force.

3.5.12 As regards the Assisted Names Undertakings, Lloyd's has agreed to undertake in favour of relevant Policyholders that in the event of an Equitas Insolvency, where a Policyholder formerly of a Name with the benefit of such an

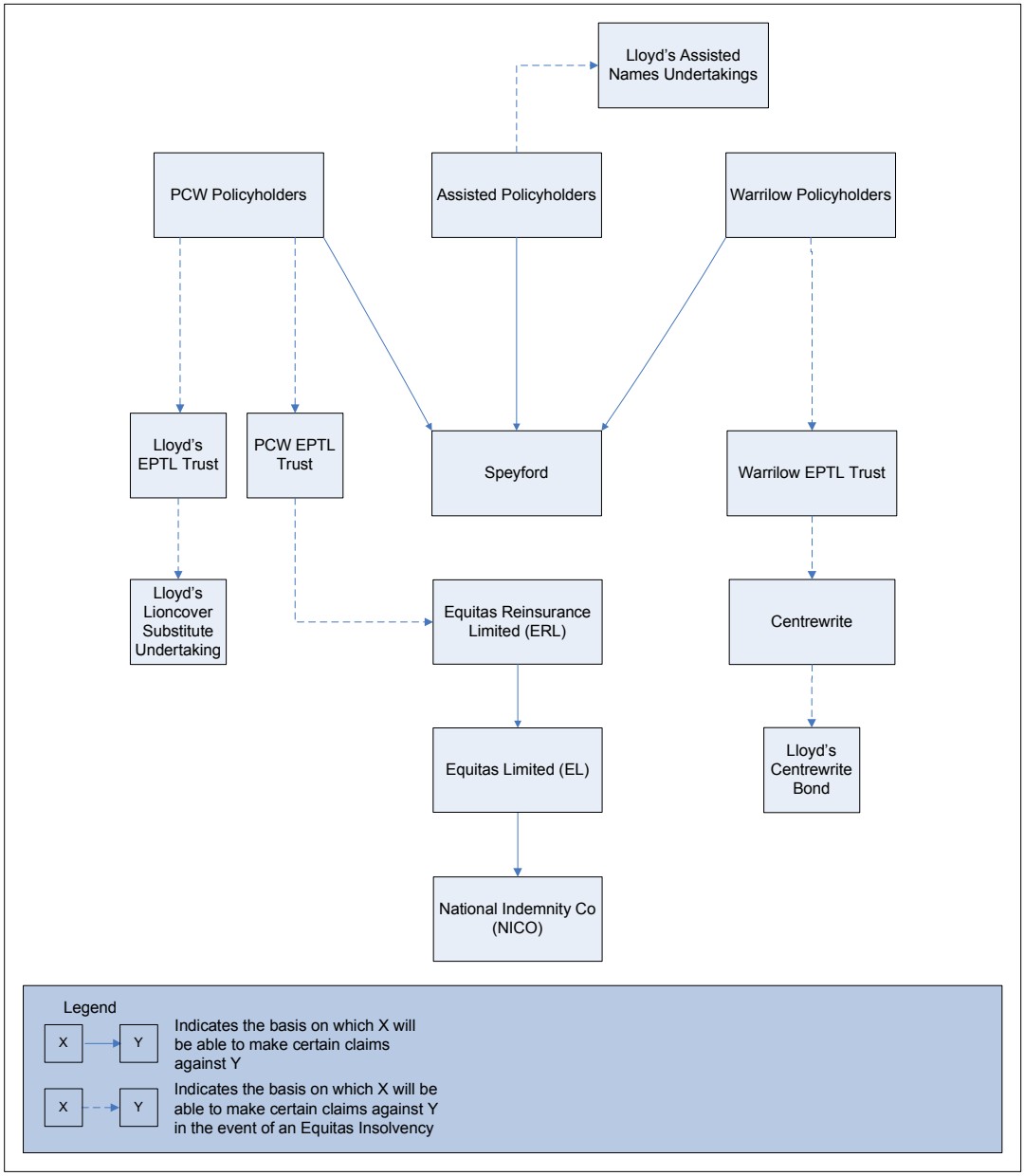
[29] Provided the Transfer is sanctioned by 31 Dec 2009 and a premium of up to £40 million is paid.

undertaking successfully sues Speyford (or the Name notwithstanding the Transfer), Lloyd's will honour its obligations under such undertakings as if the Transfer had not taken place; and pay the amount of any final and non-appealable judgement (against Speyford or the Name notwithstanding the Transfer) to the Policyholder (after taking credit for any amount of the claim paid by Speyford). This will be the case provided it can be demonstrated that the relevant Name did in fact have the benefit of such an undertaking. Lloyd's undertakings in respect of Assisted Names are also shown on Figure 3-15.

3.5.13 The arrangement is intended to leave Lloyd's protection for Policyholders and Names no worse than at present.

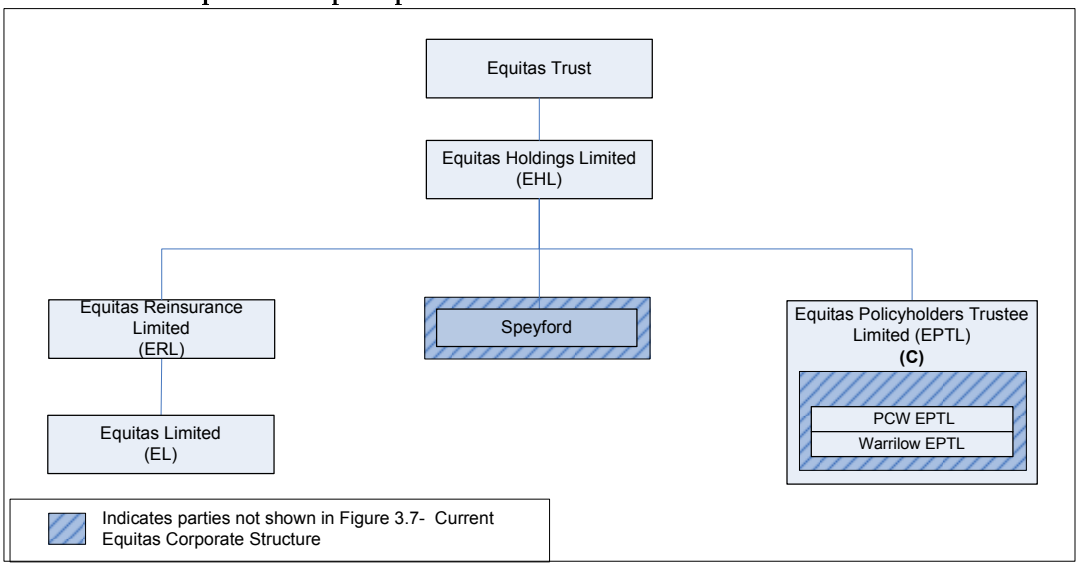
3.5.14 In the case of an Equitas Insolvency, the Assisted Names Undertakings would operate in favour of Policyholders despite the Policy having transferred to Speyford under the court order. The Policyholder would still have to show his contract had been covered by an Assisted Name.

Figure 3-15
Structure in the Event of the Transfer – Policyholders of PCW, Warrilow and Assisted Names



3.5.15 Equitas Group corporate structure, including Speyford and the new trust arrangements, is shown in Figure 3-16 below.

Figure 3-16
Equitas Group Corporate Structure in the Event of the Transfer



Regulation

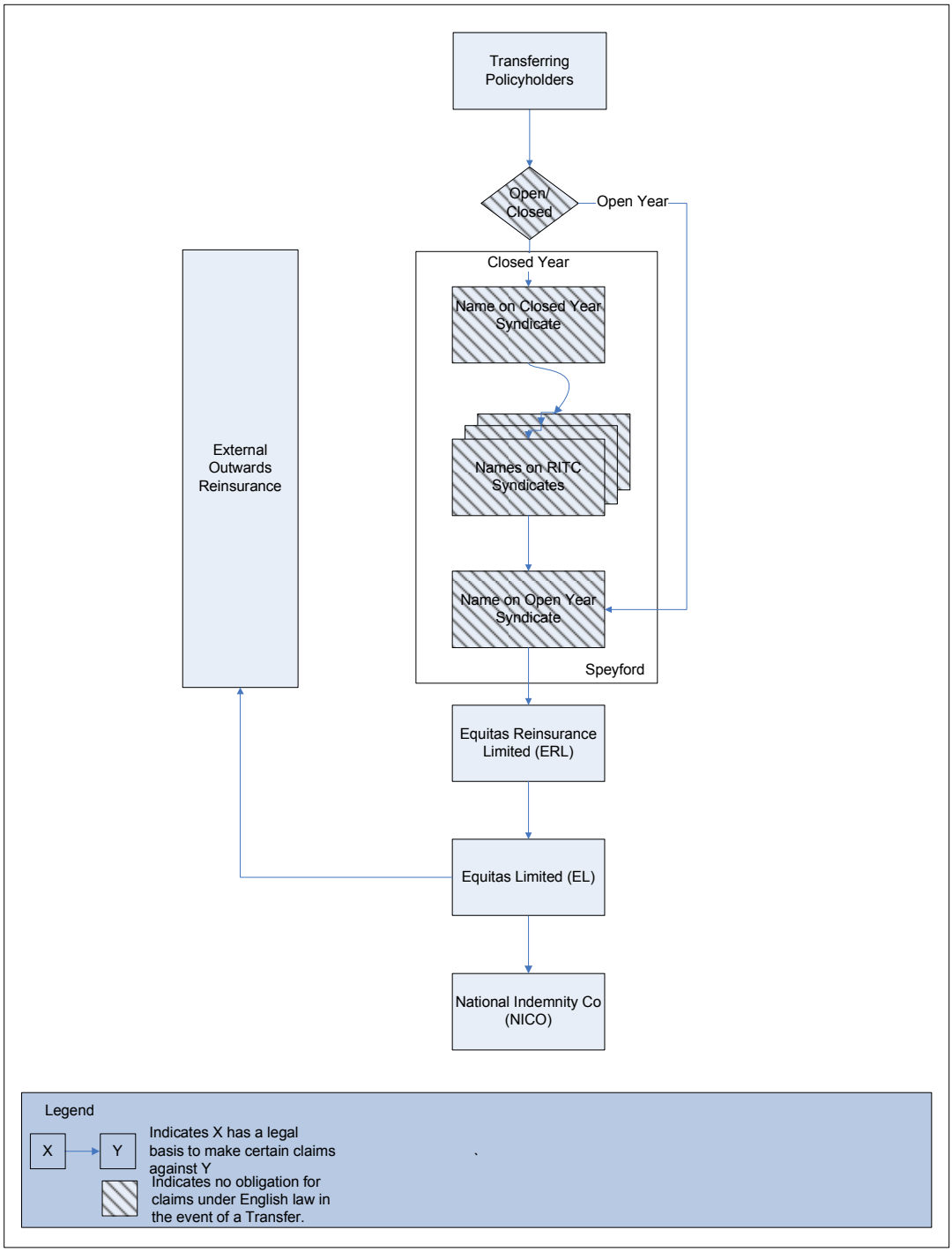
3.5.16 The situation with respect to regulation is as follows:

1. RMSL continues to be regulated by the FSA as an insurance intermediary for claims handling and related work;
2. ERL, EL, Lioncover and Centrewrite continue to be regulated FSA (re)insurers; Speyford will be a FSA regulated insurer/reinsurer;
3. Names who underwrote 1992 and Prior Business, in their capacity as such, are theoretically subject to regulation by the FSA as former members of Lloyd's, but as a matter of English law they will no longer have a role in the event of the Transfer;
4. NICO continues to be regulated in the USA; and
5. The Trust Funds are regulated in their home jurisdictions (USA, Canada, Australia and South Africa); and

Other Reinsurance

3.5.17 It is intended that the External Outwards Reinsurance provided by non-Lloyd's reinsurers, ERL, EL and NICO remains in place; thus, the court order obtained on the sanction of the Transfer would include provision to ensure that the reinsurance of the liabilities, to the extent not already assigned to Equitas as in the case of External Outwards Reinsurance, transfers with the business. This is illustrated in Figure 3-17.

Figure 3-17
Structure in the Event of the Transfer – External Outwards Reinsurance



English and Overseas Law

3.5.18 In my analysis I assume that in the event of the Transfer the terms take effect under English Law.

3.5.19 EL informs me that it is investigating whether it is practicable to seek recognition of the Transfer in other jurisdictions.

3.5.20 I have not analysed the effect under the relevant foreign law according to whether EL does or does not obtain recognition of the Transfer under that law. However I have considered the effect under foreign law of the way the Trust Funds and Credit for Reinsurance would operate in the light of the English Court order under the law relevant to them.

Financial Overview

3.5.21 Table 3-18 shows the 31 March 2008 financial position given the current structure and a pro forma financial position in the event of the Transfer at 31 December 2008.

Table 3-18
Equitas – Financial Highlights

Item	Description	31-Mar-08	31-Dec-08	31-Dec-08 Pro Forma In the Event of the Transfer
(1)	Equitas Capital	£124m	£123m	£65m
(2)	Speyford Capital		n/a	£16m
(3)	Equitas Best Estimate of Liabilities	$7.825bn	$7.824bn	$7.824bn
(4)	NICO Reinsurance excess of (3)	$5.643bn	$5.285bn	$6.585bn
(5)	EATF	$3.1bn	$2.56bn	$2.56bn
(6)	Canadian Trust Fund	Can$35m	Can$34m	Can$34m
(7)	Australian LOC	Aus$155m	Aus$150m	Aus$150m
(8)	JATF (Reinsurance)	$112m	$112m	$112m
(9)	JATF (Surplus Lines)	$214m	$112m	$112m

Source: Equitas
Notes:

(1) EL, ERL, and EHL combined
(1) Includes £18m due to be received by EL from Lloyd's by 31 December 2009.
(1) Reduced by expected Part VII costs through date of Court hearing.
(1) £65m = £123m minus £40 premium for additional NICO cover minus £16m to Speyford minus £2m for Part VII implementations costs that would not be incurred if the Transfer were not approved.
(2) Speyford business plan;
(3) Net of External Outwards Reinsurance , gross of discount, excludes estimated claims handling run-off costs that are covered by NICO. RMSL estimates that the future claims handling and run-off costs are $0.9 bn.
(4) NICO made payments of $359m between 31-Mar-08 and 31-Dec-08, and there was an increase in Equitas Best Estimate of Ultimate Liabilities of $358m, so the unpaid liabilities decreased by $1m. The NICO Reinsurance excess of Equitas Best Estimate of Liabilities at 31-Dec-08 is $5.643bn – $358m = $5.285bn.
(4) In the event of the Transfer includes the $1.3bn of additional cover from NICO.
(5) Does not include uncollected reinsurance recoverable amounts that will be paid to EATF. The EATF figure includes amounts in respect of the Illinois Trust Fund.
Trust fund assets (5) to (7) form a part of the NICO limit.

3.6 RELIANCES

3.6.1 The basis for the material in this section includes the following:

3.6.2 In this section I am relying on Clifford Chance, Equitas and Lloyd's as follows:

3.6.3 Advice from Clifford Chance with respect to:

1. The operation of Lioncover and Centrewrite;
2. The legal structure of the Equitas Group;
3. Operation of the US Trust Funds;
4. Operation of other Overseas Trust Funds; and
5. Treatment of direct vs. reinsurance Policyholders under implementation of the EU Winding-Up Directive in the event of the Transfer.

3.6.4 Input from Lloyd's:

6. Extent and nature of Assisted Names Undertakings;
7. Confirmation that there are no obligations that exist now that will not continue in the event of the Transfer; and
8. Operation of Lloyd's bonds and undertakings.

3.6.5 Input from Equitas:

9. Tables and other data as indicated throughout this section

3.6.6 I was assisted by Sidley in my review of this material.

4 ANALYSIS - ISSUES OTHER THAN NICO COVER AND SECURITY FROM NAMES

4.1 INTRODUCTION

4.1.1 The purpose of this section is to analyse Policyholder issues (3) – (13) and each of the affected parties (14) - (18) identified in Table 2-3 and Table 2-4 and summarized in the table below.

Section	Policyholder Issue/Affected Party
4.2	All Policyholders - Claims Handling and Run-off Governance
4.3	All Policyholders – Regulation
4.4	All Policyholders - Speyford - Solvent Scheme of Arrangement
4.5	Reinsurance Policyholders - Mutuality and Set-Off
4.6	Reinsurance Policyholders - Credit for Reinsurance
4.7	Reinsurance Policyholders Priority of Payments - Direct vs. Reinsurance
4.8	Policyholders of PCW and Warrilow Syndicates
4.9	Policyholders of Names with Other Lloyd's Guarantees
4.10	Trust Funds
4.11	Non-Transferring Policyholders
4.12	Names as Policyholders
4.13	Names as parties
4.14	External Outwards Reinsurance
4.15	Insurers who might be Jointly Liable with Names for UK Mesothelioma Claims
4.16	FSCS
4.17	Lloyd's

4.2 ALL POLICYHOLDERS - CLAIMS HANDLING AND RUN-OFF GOVERNANCE

4.2.1 NICO has contracted to fund the claims and run-off services for EL under the NICO Retrocession Agreement. RMSL already carries out this function on behalf of NICO and EL.

4.2.2 The NICO Retrocession Agreement includes terms to assure proper handling of the run-off, including the following:

1. Standards for RMSL performance, provisions for oversight of RMSL by EL and requirements for reporting financial and other data by RMSL to EL[30];
2. RMSL may not delegate all or substantially all of its duties, obligations and responsibilities to any person other than a person with a Part IV Permission or who is otherwise approved for such purpose by the FSA [31];
3. Extra contractual costs, punitive damages and/or other expenses arising from bad faith claims handling, if arising from conduct constituting gross negligence as interpreted by New York law, are not included within the limit of the cover. These costs would be NICO costs in excess of the NICO Policy limit with respect to EL claims[32];
4. The contract defines two triggers after which provisions called the 'Hard Governance Rights' can be implemented. The triggers are:
   a. "Erosion Trigger Event" if liabilities are within $1bn of remaining NICO reinsurance obligations[33];
   b. "Default Trigger Event" if NICO or RMSL is, for example, in material breach of its obligations, is subject to enforcement action by its regulator(s), or is subject to change of control[34];
5. If the 'Hard Governance Rights' applies then:
   a. Certain RMSL powers in managing the run-off can be exercised only with prior consent of EL[35];
   b. RMSL will establish a Claims and Commutation Committee with EL representation to oversee other aspects of the run-off and pay a portion of the costs of that committee[36]; and
   c. EL has the option to revoke NICO's right to handle the run-off of the liabilities in the event of a material default[37].

[30] NICO/Retrocession Agreement sections 13-19
[31] Ibid section 13.7
[32] Ibid section 6.3
[33] Ibid section 22.1
[34] Ibid section 21.1
[35] Ibid section 24.2
[36] Ibid section 24.3

4.2.3 In addition to the contract terms, oversight requires proper management and sufficient resources.

4.2.4 The Boards of ERL and EL are responsible for overseeing NICO's run-off responsibilities. The Board members are subject to the same FSA requirements regarding constituting 'fit and proper' people for the positions.

4.2.5 EL, ERL and EHL have combined capital of £123m ($177m[38]) in the current structure; and Speyford, EL, ERL and EHL will have capital of £81m ($116m) in the event of the Transfer.

4.2.6 Either level of assets appears sufficient to monitor RMSL and NICO.

4.2.7 The claims handling and run-off management is not changed in any material aspect in the event of the Transfer, and thus, I believe Policyholders are not disadvantaged by claims handling and run-off management in the event of the Transfer.

[37] Ibid section 21.2(b)(ii); 25.5

[38] £1 = $1.43 31 December 08 exchange rate.

4.3 ALL POLICYHOLDERS-REGULATION

4.3.1 The regulation of Names in the current structure is described in section 3.4.

4.3.2 In the event of the Transfer, Names are subject to regulation by the FSA as they will still be former members of Lloyd's, but as a practical matter they will no longer have a role in the structure in the event of the Transfer. Therefore (unless they are Continuing Names), these Names will no longer effect or carry out contracts of insurance at Lloyd's, and so they will not need to be regulated.

4.3.3 In the event of the Transfer, Lioncover will no longer have a role, therefore Lioncover's status is not relevant to Policyholders or other affected parties.

4.3.4 I have carried out my analysis on the assumption that Speyford is an FSA regulated insurer.

4.3.5 In either case, EL, ERL, and Centrewrite continue to be regulated by the FSA in the UK.

4.3.6 NICO and the US Trust Funds continue to be regulated in the USA.

4.3.7 Other Overseas Trust Funds continue to be regulated in their respective jurisdictions.

4.3.8 The ability of regulators to change the rules regarding Overseas Trust Funds is also unaffected by this Transfer.

4.3.9 Policyholders' protection by means of regulation is largely unchanged in the event of the Transfer, and thus, I believe Policyholders are not disadvantaged by any regulation changes which come about in the event of the Transfer.

4.4 ALL POLICYHOLDERS-SPEYFORD - SOLVENT SCHEME OF ARRANGEMENT

4.4.1 I am aware that there has been some discussion in the market about the relationship between the Transfer and the possibility of a future solvent Scheme of Arrangement. Therefore, I note that:

1. In event of the Transfer a Scheme of Arrangement is a legal possibility, but any Scheme would require its own separate procedure involving Policyholder approval[39] and court sanction;
2. Absent a Transfer, a Scheme of Arrangement is not possible for the Names under current law, since legislation only permits Schemes of Arrangement for corporate entities, not individuals (i.e. Names);
3. Depending on the terms of the reinsurance contract, a Scheme of Arrangement may not be binding in respect of debtors, including outward reinsurance contracts, and the outward reinsurers may not accept that they are bound to pay claims estimated through a Scheme of Arrangement;
4. Thus, as Speyford's ability to pay claims depends on receiving that money from its reinsurers, ERL, EL and NICO, a Scheme of Arrangement by Speyford would not be practical without the support of those reinsurers;
5. Further, if a Scheme of Arrangement were being promoted it would likely need to be recognised in the USA by obtaining a Chapter 15 order under the US Bankruptcy code; and
6. EL inform me they have no current intention of supporting a Scheme of Arrangement proposed by Speyford.

4.4.2 In view of the above I have not considered this point any further.

[39] A simple majority in number and 75% by value of creditors voting in person or by proxy and Court Sanction is required before a scheme can be effective.

4.5 REINSURANCE POLICYHOLDERS - MUTUALITY AND SET-OFF

4.5.1 Prior to R&R, a Managing Agent acting on behalf of a Syndicate of Names would often have bought reinsurance from entities who were also reinsured by the Syndicate.

4.5.2 Such arrangements created a relationship of 'mutuality' because the same party was both a reinsured[40] Policyholder and also a reinsurer – a creditor and a debtor relationship exists at the same time. These mutual dealings could have been with companies and other Syndicates.

4.5.3 In the event that a Name, due to bankruptcy, did not meet the obligation to pay the reinsured Policyholder, the ability to offset amounts due in both directions is available. This would result in either a zero balance or a net sum due to one or other of the bankrupt Name or the reinsured Policyholder depending on how the amounts flow. Insolvency Set-Off provisions are contained in section 323 of the Insolvency Act 1986.[41]

4.5.4 Similarly, if the reinsured Policyholder failed to meet its obligations as a reinsurer to the Name, due to the Name's bankruptcy/insolvency, the obligations of the Name to the reinsured Policyholder would be offset.

4.5.5 Under the Equitas Reinsurance Contract[42] and the Equitas Retrocession Agreement, amounts due to the Syndicate/Name under reinsurance contracts (other than RITC contracts) were assigned, on behalf of the Names to ERL and then in turn to EL. This may have affected mutuality.

4.5.6 In some very limited circumstances this assignment may not have occurred in law[43].

Set-Off if Equitas Reinsurance Contract disturbed mutuality

4.5.7 Thus, the current position with respect to mutuality may not be the same as the position when the reinsurance contract was agreed.

4.5.8 For purposes of assessing the effect in the event of the Transfer, I need to consider only the position on mutuality at present.

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[40] In this section I also refer to reinsurance Policyholder as 'reinsured' Policyholders to distinguish the possible role of the entity as reinsurer of Names from being reinsured by Names.
[41] There are also special insolvency provisions which apply to persons carrying on insurance in the Lloyd's market, and these include provisions requiring, in applicable cases, insolvency Set-Off to be applied at Syndicate level, not at the level of individual Names. Outside insolvency, availability of Set-Off depends on whether it is permitted by contract or is available applying equitable principles.
[42] Clause 6
[43] Source: Equitas

4.5.9 To the extent there is no current mutuality as a result of R&R and the Equitas Reinsurance Contract, regardless of the position of mutuality when the contracts were agreed, the Transfer will have no effect on mutuality going forward.

Set-Off if Equitas Reinsurance Contract Did Not Disturb Mutuality

4.5.10 To the extent that there has not been an assignment, then, mutuality for insolvency Set-Off would have been preserved in R&R. As a result, in the current structure, if a Name were to become bankrupt the amount due from the reinsurer/reinsured Policyholder would be offset in full against its claim as a reinsurance Policyholder against the Name. In the event of the Transfer to Speyford - in English law – the effect would be to transfer not only the Name's obligations to the reinsured Policyholder, but also any reinsurance claim arising under reinsurance bought by the Name from the reinsurance Policyholder as reinsurer of the Name. In the event of the Transfer the Set-Off position will not be altered in relation to all parties in English law and the Court will be asked explicitly to preserve this position in the order giving effect to the Transfer.

Operation of EPTL

4.5.11 The operation of EPTL does not alter the underlying obligations between the Names (and Speyford in the event of the Transfer) and the reinsured Policyholder. Therefore, Set-Off is not changed in the event of the Transfer.

Further Protections for Policyholders

4.5.12 Notwithstanding these points, the scheme (given effect by the sanction order made by the High Court) will provide that any Set-Off rights that Reinsurers may have had prior to the Transfer will remain unaffected by it.

4.5.13 The operation of Set-Off in the event of the Transfer will not disadvantage any Policyholder compared to the operation of Set-Off in the current structure as in the event of the Transfer the current position will be preserved.

4.6 REINSURANCE POLICYHOLDERS-CREDIT FOR REINSURANCE

4.6.1 Currently, US insurers and reinsurers (US Cedents) that are Lloyd's Policyholders can record the full value of their estimated reinsurance recoveries for solvency reporting purposes.

4.6.2 Credit for Reinsurance is a significant issue for reinsurance Policyholders. I have not researched the credit taken by these Policyholders, but it is useful to note that the Equitas estimate of liabilities for its reinsurance Policyholders is $2.8bn in the USA, $80m in Australia and $20m in Canada.[44]

4.6.3 Credit for Reinsurance is based on the nature of the reinsuring entity and the existence of Trust Fund arrangements.

4.6.4 Sanction of the Transfer, by the Court (in England) creates no requirement that any US court or regulatory body recognise the Transfer. As such there is no legally recognised change in reinsuring entity. Moreover, the existing Trust Funds are arranged so that there is no reduction in Policyholder protection in the event of the Transfer. As such, sanction of the Transfer in England does not require a change in the treatment of Credit for Reinsurance in the USA.

4.6.5 Thus, I am advised by legal counsel that subsequent to the Transfer, but prior to any recognition of the Transfer by a US court of competent jurisdiction, such US Cedents should continue to be allowed to take accounting credit for their reinsurance recoverables to the extent that Names remain liable on such Policies as a matter of US law.

4.6.6 It is also expected that reinsurance Policyholders in Canada, Australia and South Africa will be able to continue to take credit for their reinsurance with Lloyd's in the event of the Transfer.

4.6.7 Therefore, Policyholders should not be disadvantaged in relation to Credit for Reinsurance for regulatory reporting purposes, in the event of the Transfer.

[44] Values taken from Table 6-2

4.7 Reinsurance Policyholders Priority of Payments - Direct vs. Reinsurance

4.7.1 Under the current structure, if assets are not sufficient to pay all Policyholder claims in full, then Equitas Group assets, including the NICO Retrocession Agreement cover, would be used to pay direct and reinsurance Policyholders at the same percentage rate (known as a pari-passu basis).

4.7.2 In the event of the Transfer, Speyford (should it become insolvent) would be subject to the provision of the Insurers (Reorganisation and Winding-Up) Regulations 2004 which gives priority to direct Policyholders.

4.7.3 These regulations implement the EU Winding-Up Directive in England. They apply to insurance entities who wrote direct business and reinsurance business. Under the regulations, direct Policyholders have to be paid in full before any payments are made to reinsurers in the event of an insolvency of Speyford.

4.7.4 As ERL and EL are reinsurance companies these regulations do not apply to them.

4.7.5 However, under the Equitas Reinsurance Contract the reinsurance recovery from Equitas and NICO would be paid through EPTL and not Speyford.

4.7.6 Legal counsel advises me that the payments through EPTL will not be subject to the Insurers (Reorganisation and Winding-Up) Regulations 2004 provisions that give priority to direct Policyholders but will be paid on a pari-passu basis.

4.7.7 Thus the Insurers (Reorganisation and Winding-up) Regulations 2004 would affect only Speyford which has limited assets, (£16m initially).

4.7.8 As nearly all the assets will be paid through EPTL rather than Speyford, the impact of the Insurers (Reorganisation and Winding-Up) Regulations 2004 on reinsurance Policyholders is small. The extent of that impact is tested in the modelling described in sections 5 to 7. I conclude that reinsurance Policyholders are not disadvantaged in the event of the Transfer.

4.8 POLICYHOLDERS OF PCW AND WARRILOW SYNDICATES

4.8.1 New arrangements will be established so that relevant Policyholders and PCW Names are not disadvantaged in the event of the Transfer.

4.8.2 The Scheme Document describes the structure of:

1. PCW Reinsurance Contracts (clause 10.1 and 10.3);
2. Lioncover Reinsurance Contracts (clause 10.2);
3. Warrilow Reinsurance Contracts (clause 11.1); and
4. Centrewrite Reinsurance Contracts (clause 11.2).

4.8.3 The Scheme effects certain changes to these contracts so as to result in Speyford taking over the rights and liabilities of the PCW Names and Warrilow Names in respect of the 1992 and Prior Business of those Names.

4.8.4 Centrewrite will continue to reinsure the business of the Warrilow Names, now held by Speyford and the benefit of the Centrewrite reinsurance transferred to Speyford will be held in trust by EPTL for the benefit of the former Policyholders of Warrilow Names. The Lloyd's bond providing support to Centrewrite for its obligations under the Centrewrite reinsurance will remain in place.

4.8.5 Lioncover will be removed from the structure to cut down on administration time and costs and the business of the PCW Names will transfer to Speyford and be reinsured directly by ERL with the rights of Speyford being held on trust by EPTL for the benefit of Policyholders of the PCW Names.

4.8.6 In order to replace the effect of the Lloyd's Lioncover bond supporting the obligations of Lioncover to the PCW Names, Lloyd's will execute a substitute undertaking, to be held on trust by EPTL, agreeing to pay claims of the Policyholders of the PCW Names in the event Speyford fails to meet its obligations to such Policyholders after the Transfer.

4.8.7 I am advised by legal counsel that the mechanisms in the Scheme document, the Warrilow Deed of Assignment, the Warrilow Declaration of Trust, and the Substitute Lioncover Bond and Deed of Trust will provide equivalent protection to Policyholders and PCW Names.

4.8.8 The new arrangement operates directly for the benefit of Policyholders, rather than for Names in response to claims by Policyholders against Names.

4.8.9 Therefore, Policyholders of PCW and Warrilow Names will not be disadvantaged in the event of the Transfer.

4.9 POLICYHOLDERS OF NAMES WITH OTHER LLOYD'S GUARANTEES

4.9.1 Over the years, Lloyd's entered into a number of agreements with Names that include varying degrees of protection for Names against Policyholder claims in the event of an Equitas Insolvency. These are characterised as follow[45]:

1. Approximately 1,300 Names who signed Hardship Agreements of whom approximately 550 have now terminated those agreements;
2. Some 40 agreements under the terms of the American International Mediation Services (AIMS) Agreements; and
3. A number, believed by Lloyd's to be less than 40, of informal agreements with Names prior to R&R.

4.9.2 Lloyd's proposes to provide an undertaking assuring the same protection to Policyholders in the event of the Transfer that the Policyholders would have had under the current structure.

4.9.3 Therefore, Policyholders of Assisted Names will not be disadvantaged in the event of the Transfer.

[45] Source: Lloyd's

4.10 TRUST FUNDS

4.10.1 I am advised by legal counsel that in the event of the Transfer, but prior to any recognition of the Transfer by a US court of competent jurisdiction, Policyholders should continue to be able to benefit from the protection afforded by Trust Funds to the extent that underwriters remain liable on their Policies as a matter of US law. To this end Policyholders will remain able to access the EATF, LATFs and JATFs.

4.10.2 As regards Canada, Australia and South Africa the position subsequent to the Transfer but prior to any recognition of the Transfer by a court of competent jurisdiction in those jurisdictions will be similar to that in the USA.

4.10.3 Therefore, Policyholders in jurisdictions with Trust Funds should not be disadvantaged in the event of the Transfer.

4.11 NON-TRANSFERRING POLICYHOLDERS

4.11.1 Some of the Names continued as Lloyd's Names in 1993 and subsequent years (Continuing Names). As such, with respect to Policies written in 1993 and subsequent years, Policyholders of these Names represent 'Non-Transferring' Policyholders.

4.11.2 There is no loss of protection to Non-Transferring Policyholders as there are no Equitas related assets at Lloyd's provided by Continuing Names.

4.11.3 Continuing Names will be more secure after the Transfer as they will no longer have the risk of claims arising from 1992 and Prior Business. Accordingly, they should be more able to meet the costs of Non-Transferring Policies.

4.11.4 Therefore, Non-Transferring Policyholders will not be disadvantaged in the event of the Transfer.

4.12 NAMES AS POLICYHOLDERS

4.12.1 Most Names are both insurers and Policyholders with respect to RITC and sometimes with respect to other Inter-Syndicate Reinsurance (ISR) contracts.

4.12.2 In such arrangements, the Name as Policyholder is ceding liability for exposures arising from the 1992 and Prior Business. When that business is transferred from the Name to Speyford, the Name will no longer have liability under English law and, therefore, no need of the relevant Policies.

4.12.3 Therefore, the Names interests as Policyholder are protected under English law in the event of the Transfer. Names as Policyholders are not disadvantaged under English law in the event of the Transfer

4.13 NAMES AS PARTIES

Under English Law

4.13.1 From the perspective of Names as parties to the Transfer the advantage of the Transfer is the elimination under English law of future claims by Policyholders.

4.13.2 The disadvantage of the Transfer from the perspective of the majority of the Open Year Accepting Names under the Equitas Reinsurance Contract is that the £40m premium paid to NICO for the additional reinsurance, and the costs of doing the Transfer, reduce the potential for future return premiums to those Names. This disadvantage does not apply to Closed Year Names who did not pay a premium to ERL or to Open Year Accepting Names who would not be entitled to a return premium payment (because, for example, their Equitas premium was nil or negative) or to Open Year Non-Accepting Names.

4.13.3 Whether their share of £40m for $1.3bn of NICO coverage and release from all future claims under English law is beneficial to particular Accepting Names depends on their personal circumstances.

4.13.4 However, I observe that the terms of the reinsurance coverage were approved by the Equitas Trustees on behalf of the Names reinsured by ERL and EL.

4.13.5 Moreover, Equitas informs me that Names were supportive of both phases of the NICO transaction when it was proposed to them in December 2006.

Overseas Position

4.13.6 If the Transfer does not achieve recognition in overseas jurisdictions then Names can still be sued in those overseas jurisdictions. That, of itself, does not create a new risk for the Names. Moreover, the risk of an Equitas Insolvency has been reduced by the increased coverage under the NICO Retrocession Agreement.

4.13.7 In the event of claims against the Name, the Name may no longer be able to obtain protection, in whole or in part, from RITC or other Inter-Syndicate Reinsurance that the Name might have purchased. Under English law those RITC reinsurance arrangements are transferred to Speyford and collapse. In the event of an Equitas Insolvency, Speyford (assuming it has the funds) would be liable to pay the claim and not the RITC Name. Names are relieved of the obligation to make payments under any RITC arrangements that the Name participated in. The balance (gain or loss) will depend on individual circumstances.

4.13.8 Therefore, Names, as parties, overall, are not disadvantaged in the event of the Transfer.

4.14 External Outwards Reinsurance

4.14.1 The operation of the Scheme Document assures that the External Outwards Reinsurance currently applicable to the 1992 and Prior Business remains in force. in the event of the Transfer covering the liabilities transferred to Speyford.

4.14.2 From the perspective of the reinsurers providing the External Outwards Reinsurance I note the following:

4.14.3 Claims under the External Outwards Reinsurance will be the same regardless of whether the Transfer is approved, so there is no financial disadvantage to reinsurers.

4.14.4 Currently, operational responsibility for collections is with RMSL under the NICO Retrocession Agreement. In the normal course operational responsibility for reinsurance collection will continue with RMSL in the event of the Transfer.

4.14.5 The Transfer reduces the risk of insolvency. In particular it eliminates the risk of an Equitas Insolvency involving Names, which is important because such an insolvency is unprecedented and might create difficulties for reinsurers.

4.14.6 Therefore, the External Outwards Reinsurers are not disadvantaged in the event of the Transfer.

4.15 Insurers who might be Jointly Liable with Names for UK Mesothelioma Claims

4.15.1 Mesothelioma Claims arise as a result of exposure to Asbestos. Claimants who suffer from mesothelioma make claims against their employer(s) which had exposed them to Asbestos.

4.15.2 Where an employer is found to have materially contributed to the risk of the employee contracting the disease, the employer will be liable (and where there is more than one liable employer, each will be Jointly and Severally Liable) for the whole cost of the injury caused to the employee.

4.15.3 In practice the cost of the claim is shared on a 'time on risk' basis between insurers, with the FSCS and / or the employer stepping in to pay a share if either there was no insurance for a period or an insurer is insolvent.

4.15.4 As the result of these arrangements, to the extent there is at least one insurer or employer able to meet their financial obligations, the claimant would nearly always be paid in full (even without regard to the FSCS).

4.15.5 However, if Equitas were unable to pay claims in full, the effect would either be to reduce payments to individual claimants, or to shift costs to a combination of other solvent insurers, the FSCS and employers or both; depending upon the circumstances of each claim.

4.15.6 Thus, as well as potentially impacting individual claimants, insolvency can affect the costs of other insurers, the FSCS and employers.

4.15.7 This legal situation exists in the current structure or in the event of the Transfer.

4.15.8 In section 7.8 I evaluate the financial effect of the Transfer on these insurers. I conclude that these insurers are not materially disadvantaged by the Transfer.

4.15.9 Based on that analysis, I conclude that other insurers are not disadvantaged in the event of the Transfer.

4.16 FSCS

4.16.1 The FSCS will compensate eligible claimants if their insurer is in default[46].

4.16.2 The FSCS pays 100% of eligible claims for compulsory coverages (for example, third party liability motor insurance and employers liability insurance since 1972). For non compulsory insurance FSCS pays the first £2,000 in full, and 90% of the balance.

4.16.3 FSCS does not cover Lloyd's Policies prior to 2004, (and thus FSCS does not currently cover 1992 and Prior Business).

4.16.4 I will discuss the effect, if any, of the Transfer on the FSCS in a Supplemental Report.

[46] FSCS will compensate in the event of a default, if insurer is unable, or is likely to be unable to pay claims against it.

4.17 LLOYD'S

4.17.1 The terms of the Transfer require certain changes in Lloyd's undertakings and bonds so as to preserve existing protections for certain Policyholders of the 1992 and Prior Business in the event of the Transfer to Speyford.

4.17.2 The changes may simplify the manner in which Policyholders can access those benefits in the event of an Equitas Insolvency.

4.17.3 A successful Transfer is advantageous to Lloyd's as described in paragraphs 3.3.29-3.3.31.

4.17.4 Moreover, I observe that Lloyd's is a party to those changes.

4.17.5 I see no reason to conclude that Lloyd's is disadvantaged in the event of the Transfer.

4.18 CONCLUSION

4.18.1 No group of Policyholders or other identified parties is materially disadvantaged by issues described above (subject to the analysis in my Supplemental Report).

4.19 RELIANCES

4.19.1 In this section I relied on advice from Clifford Chance with respect to the Policyholders' situation in the event of the Transfer in the following areas:

1. Credit for Reinsurance for the USA;
2. US Trust Funds;
3. The availability of the Scheme of Arrangement process before and after the Transfer;
4. Right of Set-Off with or without the Transfer;
5. Reinsurance Policyholders and priority of payment;
6. The protection provided to Policyholders insured by Names of PCW and Warrilow Syndicates, and Policyholders of Names having other Lloyd's guarantees before and after the Transfer; and
7. The extent to which Names are regulated by the FSA.

4.19.2 Sidley assisted me in interpreting the information from Clifford Chance.

5 ANALYSIS - INSOLVENCY OF EQUITAS & SECURITY ASSOCIATED WITH NAMES

5.1 INTRODUCTION

5.1.1 In this section I analyse the security available to Policyholders in the current structure, in the event of an Equitas Insolvency, in relation to claims against Names.

5.1.2 Policyholders can currently seek to recover the shortfall from Names. In the event of the Transfer these Policyholders will no longer be able to seek that recovery since recovery can only be made against Speyford under English law.

5.1.3 The analysis is based on comparing the Policyholder position if there is no Transfer, to the position of the Policyholders in the event of the Transfer. To do so, I consider the following:

1. Insolvency Assumptions;
2. Policyholder recoveries from Open Year Names (when they are also the Original Year Names);
3. Policyholder Recoveries from Closed Year Names; and
4. Related issues.

5.2 INSOLVENCY ASSUMPTIONS – IN THE CURRENT STRUCTURE

5.2.1 To assess the effect of the Transfer, a view of the impact of an Equitas Insolvency on Policyholders and other stakeholders is required. Given the number of potential Names and their nature as individuals rather than corporate entities, there would be unprecedented issues associated with an Equitas Insolvency.

5.2.2 Nonetheless, this section identifies the events I consider likely in the unlikely event of an Equitas Insolvency in the current structure. This analysis is based on the existing contracts, relevant current law, experience of insurance insolvencies, experience with R&R and commercial judgement.

5.2.3 On this basis, the initial events are likely to be as follows:

1. An analysis of Equitas liabilities indicates that liabilities exceed the remaining Equitas assets, including the cover under the NICO Retrocession Agreement;
2. An Administrator is appointed to manage the Equitas Group and its assets in the interest of creditors. EPTL is the main creditor;
3. NYID takes US Trust Funds (EATF, JATFs and LATF) into conservatorship. Other countries with trust arrangements take control of those trusts;
4. The Administrator seeks to secure and collect all of the Equitas assets;
5. RMSL continues to determine appropriate values for claims, until the NICO reinsurance cover is exhausted, but claim payments are paid (through EL and ERL) to EPTL rather than direct to Policyholders; and
6. Claims payments to Policyholders are held in abeyance until such time as a suitable distribution methodology is determined.

5.2.4 Policyholders, claimants and other interested parties would participate. In particular;

7. The FSA's role might include the following:
   a. Continued regulation of EL and ERL notwithstanding that they are subject to insolvency proceedings;
   b. As Names (who ceased underwriting on or after 24 December 1996) are still carrying out contracts of insurance as a regulatory matter, the FSA has authority to impose requirements as it deems appropriate; and
   c. If the stability of the insurance market operating through Lloyd's appeared to be at risk, the FSA or Lloyd's might trigger a LMRO[47] (which

[47] An LMRO would be made by the Court pursuant to the Insurers (Reorganisation and Winding Up) Regulations 2005 (the regulations promulgated to implement the EU Winding Up Directive in relation to the Lloyd's market). The purpose of the LMRO would be to preserve or restore the financial situation of, or market confidence in, the Lloyd's market in order to facilitate the

might lead to a moratorium on actions and proceedings against various Lloyd's participants, including the Names reinsured by Equitas).

8. 'Action groups' supporting the interests of particular subsets of Names, Policyholders and other possible claimants might, as in the past, be established.

5.2.5 Over the next several years:

9. Litigation is likely to commence against Names with claimants, Policyholders, and Names, individually or through action groups seeking to protect their particular interests. There would (subject to any LMRO) possibly be extensive litigation involving these parties and potentially other market participants such as Lloyd's over a variety of matters (subject to any stay on legal proceeding that may exist);

10. Any Administrator(s) appointed would act to protect creditors interests;

11. The regulators, subject to the limits of regulation and law, would attempt to achieve fair treatment across the market and protect the legitimate interests of Policyholders, Names and other stakeholders;

12. Investment returns earned on funds would be held by EPTL, Equitas and Speyford during the delay period. This would ultimately be used to satisfy claim amounts, but not to pay interest to Policyholders, except in the unusual situation in which the funds available exceeded 100% of required payments;

13. Claims handling costs would continue to be covered by NICO until NICO's limit has been paid in full. It is nearly certain that this NICO obligation to pay claims handling costs will last for many years after the Equitas Insolvency is identified;

14. When the NICO limit is exhausted by payments, the cost of claims handling would be taken on by EPTL, which would reduce the EPTL funds available to pay claims; and

15. There would be an increase in the costs of managing claims, making distributions to creditors, and Policyholder disputes that might arise from insolvency. These costs would reduce the amounts available from Equitas to satisfy claims.

5.2.6 When these events have developed sufficiently, and this would probably take years, the following events are likely:

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carrying on of business at Lloyd's and to assist in achieving an outcome that is in the interests of insurance creditors of Names. An insolvency officeholder would be appointed by the Court to devise and implement a market reorganisation plan for these purposes. Upon the making of an LMRO, a moratorium would be imposed on proceedings and legal processes in respect of affected Lloyd's market participants.

16. The amount of the deficit is estimated sufficiently well to enable EPTL to make interim payments to Policyholders. Decisions on the interim payments would be based on the funds available to EPTL through the NICO/EL/ERL reinsurance chain and on negotiations with overseas regulators with respect to their country's Trust Funds. These payments by EPTL would be made partly using funds from the USA and other country's Trust Funds and partly using reinsurance funds received from NICO/EL/ERL reinsurance claims;

17. The payments would be a proportion of the agreed claim amounts. There would likely be five 'pots' from where payments are made. One for each of the eligible creditor groups—USA, Australia, Canada, South Africa and 'all other'. It is likely that no creditor would be paid at a rate less than the percentage applicable to 'all other'. Initially there might be conservative (low) partial payment ratios and then higher ratios as the ultimate cost becomes better known. It may be that ultimately different payment ratios are paid out to the various groups of creditors; and

18. If a 'mapping' exercise is considered a legitimate claims handling expense, EPTL might consider whether it would be possible to arrange for the preparation of a 'mapping' in respect of claims relating to each Original Year Name, to inform the Names of the amounts that have been paid on their behalf. This would be difficult and time-consuming, and might not be sufficiently accurate to satisfy disputing interests.

5.2.7 After enough time, the insolvency process would become clearer as the following issues would be resolved:

1. Any ongoing litigation between Policyholders and Names on specific claims as well as on any general issues would be settled;

2. Claims would be paid over time by Names considered responsible under agreed procedures; or

3. A compromise agreement would be concluded producing a final settlement arrangement.

5.3 INSOLVENCY ASSUMPTIONS – IN THE EVENT OF THE TRANSFER

5.3.1 The events relating to an Equitas Insolvency in the event of the Transfer are similar except that:

Items in Section 5.2

1. Item 7 in section 5.2 - FSA regulation would relate to Speyford as well as Equitas. There would be no need to regulate Names who are no longer insurers. There would be less risk to the insurance market operating through Lloyd's, although the relationship between Equitas and the JATFs would continue in the event of the Transfer;
2. Item 8 and 9 in section 5.2 - There should be no Names Action Groups, at least with respect to UK Names, and overall less litigation. As a matter of English law Policyholders would be unable to seek recovery from Names for contributions towards claims within the EEA;
3. Item 11 in section 5.2 - Achieving market wide consistency would be simpler;
4. Item 13 in section 5.2 - Additional costs would be lower; and
5. Item 18 in section 5.2 - Mapping of claims to Names would be unnecessary.

Other Items

6. An insolvent Scheme of Arrangement or similar 'compromise arrangement' would be easier to implement.

5.4 POLICYHOLDER RECOVERIES FROM OPEN YEAR SYNDICATES

5.4.1 It is necessary to analyse the amount of money that might be recovered by Policyholders, under the current structure or in the event of the Transfer should an Equitas Insolvency occur.

5.4.2 In this section 5.4 I consider Policyholders whose Policies were wholly or partially underwritten by an Open Year Syndicate[48].

5.4.3 The proportion of Policies underwritten by Open Year Syndicates represents less than 9%[49] of ERL's current liabilities, but it is useful to consider these first for three reasons:

1. The Policyholders on Open Year Syndicates are a sub-group of Policyholders, and as part of my overall analysis I need to consider whether they are disadvantaged in the event of the Transfer;
2. These Policies are the simplest to analyse and easiest to understand because there is no reason for the Policyholder to pursue a claim against any Name other than the Original Year Name; and
3. Finally, understanding the position of these Policies is helpful in understanding the position of the Policies partially or wholly underwritten by Closed Year Syndicates. I discuss the position of Policies with respect to Closed Year Syndicates in section 5.5.

5.4.4 Each Name is responsible only for his/her several share of the Syndicate's obligations for each Open Year of Account (for which the Name participated).

5.4.5 As well as establishing a Name's liability to a Policyholder there are other issues that may affect a Policyholder's ability to collect from a Name as follows:

1. Effect of Death – Treatment in estates;
2. Effect of Death – Mortality and survivorship rates;
3. Bankruptcy of Names and sufficiency of assets;
4. Location;
5. Delay;
6. Fragmentation – whether individual claims are large enough to permit economical collection from the Name;
7. Disputed payments – costs; and
8. Settlement of disputed recoveries.

[48] Each Policy will normally be with a number of different Syndicates. Therefore a Policy may be in part with Open Year Syndicates and in part with Closed Year Syndicates.
[49] Approximate`ly 91% of claims are for Closed Year Syndicates (paragraph 3.2.23). Thus 9% are for Open Year Syndicates.

5.4.6 Each of these issues is described in greater detail in the remainder of this section.

Effect of Death – Treatment in Estates

5.4.7 A Policyholder has limited ability to make a successful claim against the estate's executors or beneficiaries where a Name's estate is closed at the time of an Equitas Insolvency. Paragraphs 5.4.8 – 5.4.12 and 6.4.14 below sets out legal advice regarding claims against estates in England. Paragraphs 5.4.13 and 5.4.14 below outlines legal advice regarding claims against estates in the USA.

5.4.8 In England, any claim brought against an executor would have to be brought before the expiry of six years from the final distribution out of the estate. Even where a claim is brought within the six year period a claim would fail where the executor obtained a Re Yorke order[50] or was otherwise protected from liability under Section 61 of the Trustee Act 1925.

5.4.9 Under English law, a Policyholder may bring a 'personal' claim or 'proprietary' claim (under equity) against the beneficiary (provided there is no available claim against the executor).

5.4.10 A personal claim, which is a claim against the beneficiary based on the law of restitution which requires a person who has been unjustly enriched to refund what has been received (regardless of whether the beneficiary has disposed of his beneficial interest in good faith before an action is brought against him), must be brought before the expiry of six years from the death of the deceased.

5.4.11 A proprietary claim, which is based on the right to follow, trace and claim the money or property that has been wrongfully distributed, is not subject to a statutory limitation period but may be defeated, amongst other defences, by the Policyholder failing to act with reasonable diligence in commencing proceedings (the "doctrine of laches") or by his conduct where it indicates an intention to seek no redress against the beneficiary ("doctrine of acquiescence"). As a proprietary claim is based on following or tracing an asset, such a claim will be extinguished where the relevant asset or money has been dissipated.

5.4.12 Both personal and proprietary claims are liable to fail where one of the relevant equitable defences applies. In this respect, two defences are noteworthy. First, a personal claim is likely to be defeated where a beneficiary can prove that he has "changed his position" on the basis of the payment received to the extent that it would be inequitable to require him to return that payment. Second, where the legal title to an asset bequeathed to the beneficiary has passed to a purchaser for value without notice of the Policyholder's equitable interest there will be no

[50] Following the case of Re Yorke (deceased) [1997 4 All ER 907] it has become common practice for executors of estates of deceased Lloyd's Names to seek the authority of the Court to distribute assets. Such orders have been readily granted on the basis that the deceased's liabilities in respect of 1992 and earlier Year of Account were reinsured into Equitas and there was no reason to doubt the adequacy of the resources available to Equitas to meet claims.

claim against the bona fide purchaser. This defence will defeat a proprietary claim.

5.4.13 With respect to the USA, less than ten percent of Names on Open Years at the time of R&R have provided Equitas with US addresses, and based on the historical experience of recruitment of Names, the percentage of all Names who are US residents is likely to be lower[51]. Therefore, US law on personal estate closure upon death does not have a significant effect on my conclusions with respect to benefits available to Policyholders. Moreover, under New York, Florida, and California law, personal estates close more quickly and no less completely upon death than in the UK. I use these states to evaluate this issue because over one-third of the last known addresses of the Open Year US Names are in these three states and because the estate law of these states is reasonably representative of those in other states with respect to closure of estates.

5.4.14 In England and in the USA for at least the states studied, the amount of a claim against an executor or a beneficiary where the estate is closed is limited to the amount of the estate/bequest respectively.

Summary

5.4.15 In England a Policyholder has six years to bring a claim against an executor from the final distribution of the estate, and six years to bring a personal claim against a beneficiary from the death of the deceased. There is no time limit for bringing a proprietary claim against a beneficiary. There is a high likelihood that Policyholders would be unsuccessful in bringing such claims against an executor because the executor is likely to have the benefit of a Re Yorke order or section 61 of the Trustee Act 1925, and in relation to claims against beneficiaries the beneficiaries may be able to rely on equitable defences to defeat any claim made.

5.4.16 To summarise, it can be assumed that in a majority of cases the prudent executor will not distribute an estate until he has obtained a Re Yorke order. It is likely that this order may be obtained fairly quickly after the deceased's death provided all that is holding up the distribution is the executors' concerns of personal liability to the creditors of the deceased Names. Once a Re Yorke order has been obtained the limitation period relevant to bringing claims against executors becomes irrelevant as the Re Yorke order provides a defence to any such claim. Whilst the time-limit for bringing personal claims against beneficiaries is six years from the date of death of the deceased it is possible that any claims could be defeated within the six year period due to one of the equitable defences applying. Further, whilst proprietary claims against beneficiaries are not subject to any limitation period, it is probably fair to say as more and more time elapses (and as assets and cash change hands) the greater the likelihood of failure as one or more of the equitable defences are likely to apply.

[51] Source: Equitas

Effect of Death – Mortality and Survivorship Rates

5.4.17 The ages of Open Year Names are shown in Table 5-1 below.

Table 5-1
Age Distribution of Open Year Names at December 1992

Age at Dec 92	Number	%
19 – 30	598	1.8%
31 – 40	3,455	10.2%
41 – 50	7,856	23.1%
51 – 60	9,114	26.8%
61 – 70	7,598	22.3%
71 – 80	3,176	9.3%
81 – 90	556	1.6%
Over 90	27	0.1%
Total Alive on 31/12/1992:	32,380	95.1%
Total Deceased by 31/12/1992:	1,656	4.9%
Total Number of Open Year Names:	34,036	100%

Note: Average age in 1992 was 55.
Source: Equitas, based on anonymised information collected by Lloyd's on Open Year Names as part of R&R

5.4.18 Equitas developed and I have reviewed a Mortality table, reflecting the observed life expectancy of Names.[52]

5.4.19 Based on that Mortality table, the estimated Survival Rate of Names at 2011 and 2017 is illustrated below:

Table 5-2
Survival Probabilities

Group of Names	% Living at 2011	% Living at 2017
Year of Account 1960 & earlier	7.5%	3.9%
All Names	36.4%	28.3%
Open Year Names	71.5%	61.7%

5.4.20 Table 5-2 shows survival probability at 2017 because the end of 2017 is, according to the modelling exercise described in section 6, the average date of an Equitas Insolvency, weighted by the size of the insolvency (and assuming insolvency occurs).

[52] I discuss the Mortality Model and my review of it in Appendix X.

5.4.21 The table shows survival probability in 2011. That would be six years prior to the average date of an Equitas Insolvency and more than six years prior to the dates at which Policyholders would bring claims seeking recovery for a shortfall. Some claims are limited to six years from date of death and some claims are limited to six years after final distribution of the estate assets.

5.4.22 The Mortality Model assumes that the death of a Name after an Equitas Insolvency will not impede recovery by a Policyholder. In part this is appropriate, because it may be difficult for an executor of a Name to close an estate without providing for future claims. This may overstate a Policyholder's ability to secure recoveries from a deceased Name as it will take years before claims arise and are settled and this is likely to make some recoveries difficult or impossible.

Bankruptcy of Names and Sufficiency of Assets

5.4.23 Under English law, if a Name has been discharged from bankruptcy prior to an Equitas Insolvency, then no claims by Policyholders relating to the Name's obligations undertaken prior to bankruptcy are possible against the Name but claims will continue to be possible against his bankruptcy estate. The bankruptcy estate would include the Name's reinsurance recoveries generated by an insurance claim against another Name or otherwise, or any other asset. Other assets available towards settlement of the claim may take the form of security in force (for example premium trust funds). Given the relatively small number of US resident Names, I have not investigated the situation with respect to bankruptcy in the USA.

5.4.24 During R&R, bankruptcy and adjustment for 'hardship cases', affected premium payments for 3%[53] of Names. If there were no 'hardship' programs for Names in the event of an Equitas Insolvency some Names in similar situations would become bankrupt.

Location

5.4.25 In order to bring a claim against an Original Year Name under English law, the Name needs to be located. In the USA, a claim against an Original Year Name can be brought via service on the agent for service of process designated in the insurance Policy, but in order to collect on the judgement it would be necessary to locate the Name and to institute proceedings in the jurisdiction in which assets of the Name can be found.

5.4.26 This will not be universally possible.

5.4.27 For example, when the 2007 Equitas return premium was paid, only about 81%[54] of the Open Year Names could be located.

[53] Source: Lloyd's

[54] Source: Equitas

5.4.28 Where a Name is located, investigation will be required to determine the Name's assets and where those assets are located. Where those assets are located overseas, the Policyholder will need to incur additional time and expense in pursuing those assets.

Delay

5.4.29 Delay in payments to Policyholders during the initial years after an Equitas Insolvency is declared would be inevitable.

5.4.30 Some delay will be caused by the time needed to assess liabilities sufficiently and to assess the likely recovery of assets, in order to determine how the insolvency process is to be conducted. These would need to be understood before an interim payment could be made through EPTL. There would be an even longer delay before a final payment ratio, or an overall settlement (per paragraph 5.2.7(3)) could be determined.

5.4.31 Some delay would be caused by litigation, and there may be more issues to litigate in the current structure compared with the position in the event of the Transfer. For example, it is not clear when Names would be obliged to meet their share of any shortfall in payments due to Policyholders relative to the payment of EPTL interim or final dividends. Subject to any LMRO in force at the time, Policyholders might demand immediate 100% payment from Names. Names might respond that they have no obligation to make any payments until the Name's obligation to the Policyholder is determined (and interim dividends start to flow). After which, Names might argue that no payments should be forthcoming from them until the final dividend distribution from EPTL is known. The result could be a stand off until the Names' final obligations to Policyholders are determined and final distributions are paid.

5.4.32 Even when the general issues have been litigated and the Names' obligations are determined, without the Transfer, delay will result from the need, in some cases, to obtain a judgement for a certain amount against each individual Name as a precursor to enforcement proceedings.

5.4.33 Based on experience in major insolvencies, any payments will not take place for years, and the final payments might not be made for well over 15 years.

5.4.34 I expect an Insolvency associated with Names would result in more delay than an Insolvency not involving Names. I expect this because an insolvency involving Names would have many parties to the potential litigation and a number of significant and unprecedented issues. As a matter of English law, issues related to Names become moot in the event of the Transfer. Even issues related to overseas recognition become financially less significant as fewer than 10% of Original Year Names reside outside the UK. Therefore I believe an insolvency in the event of the Transfer will involve less delay and less cost.

5.4.35 Moreover, the likelihood of an Equitas Insolvency and thus, any delay, reduces in the event of the Transfer, given the additional NICO reinsurance cover.

Fragmentation, Policyholder Expenses, and Settlement Costs

Fragmentation

5.4.36 The liability for each Policyholder's claims is divided among many Names, on a several basis and would be spread over many Years of Account. The amount due from each Name may be small, even for large claims. The amounts due will be spread over long periods of time.

5.4.37 The Table 5-3 below shows the percentage of claims expected to be paid in each time increment, given that an insolvency occurs. The total shortfall amount is $2.4bn. $2.4bn is the average shortfall amount in the event of an Equitas Insolvency.[55]

Table 5-3
Effect of Fragmentation Over Time

Years	Payout Pattern from Date of Insolvency	Shortfall ($M)	Average Liability per Name ($)
1 - 5	26.0%	632	18,578
6 - 10	20.0%	486	14,290
11 - 15	16.0%	389	11,432
16 - 20	12.0%	292	8,574
21 - 25	9.0%	219	6,431
26 - 30	7.0%	170	5,002
31 - 35	5.5%	134	3,930
36 - 40	4.0%	97	2,858
41 - 45	0.5%	12	357
Total	100%	2,431	71,452

5.4.38 I show the amounts in five year increments for two reasons. Firstly, the initial payments may be delayed 5 – 10 years after the initial bankruptcy. Secondly, the liabilities per Name on an annual basis are so small that annual collections may not be feasible. Periodic collections, perhaps every five years might be more feasible. Statutes of limitation may restrict the length of the period between collections.

5.4.39 The average amount per Name represents the average amount due from each Name, to perhaps several hundred Policyholders.

5.4.40 The extent to which claims are divided among the Names may make it uneconomical to collect some claims. Table 5-4 summarizes, on average, the

[55] Base liability assumptions

number of Names and the percentage of claims that fall below certain thresholds, assuming base liability assumptions.

Table 5-4
Number of Names With Claims Liabilities Under Various Thresholds

		5 Years		10 Years		All Years	
Threshold (£)	Threshold ($)	Number of Names	% Claim Amounts	Number of Names	% Claims Amounts	Number of Names	% Claims Amounts
5,000	8,500	18,396	8%	14,014	4%	9,041	1%
10,000	17,000	24,067	19%	19,393	10%	13,419	3%
15,000	25,500	27,124	30%	22,732	16%	16,426	6%
20,000	34,000	28,979	38%	25,033	22%	18,713	9%
25,000	42,500	30,194	45%	26,702	28%	20,541	12%
30,000	**51,000**	31,033	52%	**27,953**	**33%**	22,047	15%
250,000	425,000	34,013	98%	33,907	93%	33,217	77%

Note: I have assumed (£1= $1.70) based on the 1972-2009 average exchange rate. The result is not very sensitive to the exchange rate. Sensitivity test discussed with Table 5-6.

5.4.41 This table shows, for example, that 27,953 Names would be responsible for less than £30,000 ($51,000) of claims in the first ten years, on average. This represents 33% of the total shortfall amount.

Policyholder Expenses

5.4.42 In the years immediately preceding and then following an Equitas Insolvency, Policyholders will have internal costs and management time spent in dealing with their exposure to loss from the insolvency.

5.4.43 In at least the initial years after an Equitas Insolvency, it is likely that litigation may be necessary to obtain payments from Names once the exercise of locating them has been accomplished and their share of a quantified claim has been established.

Settlements of disputed recoveries

5.4.44 Finally, it is inevitable given the nature of the process that some claims will be settled for less than the full value of the claim.

5.4.45 For large claims to Names it will be difficult to recover the full amount, and many of these claims would likely result in settlement. Table 5-4 shows that 77% of the claims are below £250,000. This means that 23% of these are above £250,000 and would likely settle for less than the full amount.

5.4.46 On the other hand, for very small claims, the relative Policyholder cost associated with pursuing the Names for these claims will give the Policyholders an incentive to settle shortly after an Equitas Insolvency, likely at a level far below the full amount of the amount originally claimed.

Analysis

5.4.47 The effect of Fragmentation, Policyholder costs, and settlements are interrelated. Therefore, I have analysed these effects together. In this analysis, I considered these effects from two perspectives. Firstly, I considered the Recovery Rates if all Policyholders coordinated their effort to pursue recoveries from Names. Secondly, I considered the Recovery Rates if an individual large Policyholder pursued its recovery from Names separately. The analysis showed that large Policyholders will likely recover greater amounts if they coordinated with all other Policyholders. This analysis is described in further detail in Appendix XI.

5.4.48 The effects of Fragmentation and settlement would likely be different for small claims against Names than for large claims against Names. For large claims against Names, I assumed that the Policyholders would likely settle these for some fraction of the full amount, shortly after an Equitas Insolvency.

5.4.49 For small claims against Names, some of these will be too small to be economical to pursue. I assumed that there is no recovery in respect of these claims.

5.4.50 Of the remaining claims, as time progresses it will become less economical to pursue these claims, due to the cost relative to the amount recoverable in each time interval. For this reason, Policyholders would likely settle these claims for less than the total amount due. I assumed that these claims would settle half-way between the amount likely to be recovered in the first 10 years and the amount likely recovered (less expenses) if the Policyholders pursued the Names through the entire 45 year span.

5.4.51 In order to test the effects of all of these factors, I have selected the following assumptions[56]:

1. Policyholder Expense – This is the cost to the Policyholder associated with pursuing each Name. I assumed that there would be at least £10,000 in expenses to pursue each Name for claims due over a ten year period, or £1,000 per year. This selection results in a total of about £61m, which is not large compared to the £100m cost[57] of just the reserving and allocation work as part of R&R.

2. Minimum Claim Level Pursued – This is the minimum recovery amount from a Name which would be considered worthwhile to pursue. I assumed that this would be £20,000, after Policyholder expenses. This selection is supported by the fact that banks often do not petition for bankruptcy for debts less than £20,000 because it is uneconomical to do so; [58] [59]

[56] The assumptions are stated in GBP to reflect the fact that the claims and expenses will be paid in GBP.
[57] Source: Equitas
[58] Source: PWC

3. Time Delay After Insolvency – I assumed that there would be a ten year delay from the time of insolvency before the first payments are made to Policyholders;
4. Large Claim Threshold – This is the level where I consider a claim large enough that it would be treated differently from others, and likely would result in settlement. I assumed that this would be £250,000; and
5. Settlement Cost to Large Claims – This is the percentage that would be unrecoverable from large claims, due to settlement negotiations. I assumed this to be 25%.

5.4.52 The details behind the modelling, along with sensitivity testing and further support of the assumptions noted above, are set out in Appendix XI.

5.4.53 The results of the modelling are summarised in the table below.

Table 5-5
Results of Fragmentation, Policyholder Expense and Settlement Analysis

Collection Issue	Amounts (£m)	Percentage of Total
Uncollected Portion of Large Claims – Settlement Cost	84	6%
Uncollected Portion of Small Claims – Settlement / Fragmentation Cost	631	44%
Fixed Policyholder Expenses	61	4%
Total Uncollected Due to Settlement, Fragmentation & Policyholder Expenses	776	54%

Variable Policyholder Expenses

5.4.54 In addition to fixed Policyholder expenses associated with pursuing each Name, described in the previous paragraphs, there will also likely be an additional expense which varies by the amount of the claim being made.

5.4.55 Part of this expense will relate to litigation fees and costs that might be transferred to Names, as part of an award. In practice, however, it is generally accepted that for litigation in English courts, only about 70% of costs are recovered even in successful cases[60]. In the event that litigation fees and costs must be expended in US litigation, in order to obtain final judgement against individual Names, it is very unlikely that more than a nominal amount of those fees and costs could be recovered[61].

5.4.56 Part of the cost is internal to the Policyholder, and thus not recoverable from Names.

[59] A threshold higher than £20,000 may be appropriate for this purpose as there would be thousands of Policyholders sharing the £20,000 rather than one individual bank.
[60] Source: Clifford Chance
[61] Source: Clifford Chance/Baach Robinson

5.4.57 Lloyd's estimates that it incurred approximately 15 pence of uncollected cost for every £1 of R&R premium recovered from Names who did not pay voluntarily. This 15 pence cost does not include the costs of defending actions brought against it by litigating Names. If these costs were included, the uncollected costs figure would rise to at least 30 pence for every £1 of R&R premium recovered.[62]

5.4.58 I have assumed that there will be Policyholder expenses equal to 10% of the total recovery amount, in addition to the fixed Policyholder expenses discussed in the previous paragraphs.

Summary of Situation with Respect to Open Year Names

5.4.59 Table 5-6 below provides a numeric view of the possible probability levels of recovery that Policyholders might expect in respect of Open Year Names. The first column shows the results for all Policyholders, while the second column shows the results for long duration direct Policyholders.

5.4.60 I intend that the table below provides guidance only in assessing the range of possible Recovery Rates from Names rather than precise figures.

Table 5-6
Recoverability Analysis – Open Year Names

Item	Collection Issue	Open Year Names Recovery %	Open Year Names Recovery % - Long DIR
(1)	Death of Names	67%	55%
(2)	Delay	98%	98%
(3)	Bankruptcy/past and future	98%	98%
(4)	Locating Names	95%	95%
(5)	Fragmentation, Settlement, & Policyholder Expense	46%	34%
(6)	Variable Policyholder Expense	90%	90%
(7)	**Combined Effect (Product of 1-6)**	**25%**	**15%**

Note: I have assumed (£1= $1.70) based on the 1972-2009 average exchange rate. The result is not very sensitive to the exchange rate. Based on current exchange rate of £1=$1.40 the Open Year Recovery Rate would be 27% instead of 25%.

5.4.61 The assumptions in this table are based on the following:

1. The Survival Rates are set out in Table 5-2. A 67% recovery is likely from Open Year Names when the death of Names is taken into account. This is the average of 61.7% and 71.5% based on the assumption that Recovery from Names will be increasingly difficult after the death of the Name.

   It is expected that long duration direct Policyholders will recover less due to the fact that these Policyholders will be impacted by insolvencies in later

[62] Source: Lloyd's

years to a greater extent, when fewer Names will be alive. This Survival Rate is 55%.

2. I make the assumption that the delay in payments to Policyholders is three years longer in the current structure than in the event of the Transfer. The Equitas payment patterns indicate that a three year delay affects approximately 17% of future payments to after the average insolvency date. Assuming the cost of delay to the Policyholder is 8% per year (the Policyholder time value of money, 4% more than a 'risk free' rate), the average cost of the delay is 2%[63]. Therefore the effective recovery from an Open Year Name taking account of delay factors is 98%.
3. If Names were required to make payments only after the Names' final obligation to the Policyholder is determined and an EPTL dividend is calculated, then the delay would be much longer.
4. The factor of 98% for bankruptcies follows from an assumed 2% bankruptcy rate. The 2% bankruptcy rate is based on half the 3% proportion of R&R Hardship Agreements plus a small number of actual R&R bankruptcies[64].
5. Equitas was unable to locate over 21%[65] of Open Year Names for the purpose of making a return premium payment in 2007. Simply because of the passage of time, Names will be less readily located by the time an Equitas Insolvency might be apparent. However, despite this increasing difficulty, the example assumes only 5% of Names will not be located because in the event of an Equitas Insolvency, Policyholders would likely expend more effort in locating Names and more effort still to locate their assets. Taking the issue of locating Names into account there is a 95% probability that recoveries from Open Year Names will be made in this situation.
6. The effects of Fragmentation, Policyholder expenses, and settlement costs are shown in Table 5-5, and are equal to 54%. Thus, the Recovery Rate is assumed to be 46% for Open Year Names. For long duration direct Policyholders, I have assumed that the Recovery Rate will be 75% [66]of the Recovery Rate for all Policyholders, or 34%. This is supported in Appendix XI.
7. I have assumed that there will be Policyholder expenses equal to 10% of the total recovery amount, in addition to the fixed Policyholder expenses

[63] A detailed calculation approximately equal to 8% interest for 1.5 years on 17% of the amount to be recovered.

[64] Source: Lloyd's

[65] Source: Equitas

[66] Long duration Policyholders will be primarily individual UK Mesothelioma Claimants. The claim size will be smaller on average and there will be fewer Policyholders to share the cost of seeking recoveries from the Names. This will be partly offset by the likelihood that there will be fewer Names per claim, as UK EL is a speciality line of business.

discussed above. Therefore, the effective recovery from an Open Year Name taking into account variable Policyholder expenses is 90%.

8. The combined effect is the product of the percentages in rows (1) to (6). This calculation assumes these effects are fully independent or have been selected to recognise the relationships between the factors. Based on these values a Policyholder recovery would be $25 for each $100 of claim amount due from Names.

Summary for Open Year Policies

5.4.62 The values in Table 5-6 are necessarily subjective, but illustrate that Policyholders should not expect a Recovery Rate higher than approximately 25% on Open Year Policies.

5.5 POLICYHOLDER RECOVERIES FROM CLOSED YEAR SYNDICATES

5.5.1 I now consider the case of Policyholders of Closed Year Policies.

5.5.2 The portion of liabilities underwritten by Names on these Closed Year Syndicates represents over 91% of the Equitas liabilities[67]. These are a sub-group of Policyholders, and I need to consider whether they are disadvantaged in the event of the Transfer.

5.5.3 These Policies are affected by all the issues discussed in section 5.4 above and, in addition, by several other issues.

Original Year Names

5.5.4 The first issue is determining which Name is responsible.

5.5.5 A Name who underwrote the Policy at the inception of the Policy is referred to as the Original Year Name.

5.5.6 Under English law, a Policyholder only has a claim against Original Year Names.

5.5.7 Under US law, it is unlikely that a Policyholder has a direct claim against anyone other than the Original Year Name. State law governs this issue. US jurisdictions accept the general rule that Policyholders have no direct right of recovery from their insurers' reinsurers.

5.5.8 There are exceptions to this rule, varying from state to state, which would not appear to be applicable to RITC. RITC is not a feature of US insurance practice, therefore the nature of the RITC relationship has not been tested in US law. In the years following R&R, a related issue with respect to Policyholders' right to sue Equitas directly was addressed by numerous trial courts in the USA. Courts in most states that considered the issue, found that there was no direct right of action against Equitas, and no final judgement against Equitas was ever entered.[68] Because the US legal system is a federal system, it is not possible to say unequivocally that every state will necessarily conclude that there can be no direct right to claim against RITC Names. However, based on the decisions arising out of the Equitas experience, I am advised that the great majority of states are likely to conclude that a Policyholder has no direct right of action against Names providing RITC to the Policyholder's original insuring Names.

5.5.9 If the Original Year Name is alive, or if he is deceased and the estate is or can be opened and has assets, then the Policyholder would be in the same position as an Open Year Policy in respect of that particular Name.

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[67] See paragraph 3.2.23

[68] This is not to say that Policyholders have not claimed to have a right of direct action against Equitas or that all such claims are dismissed immediately in all courts. However, I am advised that some such claims have been dismissed, while no such claims have resulted in a decision holding that a Policyholder has a right of direct action against Equitas.

5.5.10 Table 5-2 showed that for all Original Year Names (both Open Year Names and Closed Year Names) the expected percentage of surviving Names at the average date of default is 28% (and it showed that it is 36% six years prior to the expected default date)[69].

Original Year Names - Long Duration Direct Policyholders

5.5.11 As I discussed in section 5.4 with respect to Open Year Names, the Recovery Rates will be lower for long duration direct Policyholders. This is due to the nature of these claims, as it relates to the Mortality of Names and the Fragmentation, Settlement, and Policyholder expenses.

Effect of Death - RITC Policies

5.5.12 If the Original Year Name is deceased and the estate is closed[70], the next issue is the extent to which the Policyholder might seek recoveries from the Names who underwrote the RITC Policies that reinsured the Original Year Names.

5.5.13 Under English law, if the Original Year Name is deceased and the estate is closed, there are legal procedures by which the Policyholder can have the estate re-opened to pursue any reinsurance, particularly RITC, which might have been available to the deceased Name. But before the Policyholder can attempt these procedures, the Policyholder would first need to prove his claim against the Original Year Name[71].

5.5.14 In that case, under English law, the executor or Administrator (which may be the Policyholder if appointed by court order) would need to bring claims against the Names who are Severally Liable as members of the Syndicate that provided the RITC. Many, but not all, of those Names will be Original Year Names on the same Policy, although the nature of the claim on the reinsurance contract would be different from the direct claim. There are legal uncertainties and limitations regarding the extent to which Policyholders can expect to make recoveries in this way. This approach has never been tested in court.

5.5.15 Nonetheless, I have assessed the implication if Policyholders were given the right to fully access the RITC Chain for two reasons. First, that RITC protection

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[69] These survival percentages consider both Names who underwrote Open Year Policies and Closed Year Policies. Considering them together is necessary as some Names who underwrote Closed Year Policies also underwrote Open Year Policies. This is conservative, as Names who underwrote Open Year Policies would on average be, slightly younger than Names who underwrote Closed Year Policies.

[70] In section 5.4, I showed that if this had been an Open Year Policy the Policyholder would have little chance of recovery from the estate but may also have a limited ability to make a claim against the estate's, executors or beneficiaries. The issue being addressed here is the extent, if any, to which the existence of RITC increases the potential recoveries by Policyholders.

[71] I have not explored the issue with respect to US law because, according to Lloyd's, the number of US Names is relatively low, well below 10% on Open Year Syndicates and even lower on Closed Year Syndicates.

is not necessarily unavailable in all situations and, second, it would be appropriate to explore all options.

5.5.16 If a Policyholder could access the entire RITC Chain, the Policyholder could make a claim against any surviving Name who underwrote an RITC contract that covered the Policyholder's contract.

5.5.17 Mathematically, the interest is in the probability of finding a survivor among a group of people. This is called the 'Joint Survival Rate'. Based on the Mortality Model, Equitas estimated that the Joint Survival Rate is 8.9% higher than the Survival Rate for Open Year Names or 73% (8.9% is 1.089 as a factor and 1.089 * .67 = .73). For the reasons discussed below and further described in Table 5-7 Item (1), I use a lower value, 67 %.

RITC - Other Effects

5.5.18 If a Name cannot be located in order that a judgement can be enforced against him / her, then the related RITC is inaccessible.

5.5.19 As a matter of English law, if an RITC Name has had their bankruptcy discharged prior to an Equitas Insolvency, then no claim by a Closed Year Name pursuant to an RITC contract against such RITC Name can be made. However, it will continue to be possible to make claims against the RITC Names' bankruptcy estate or any security in force in relation to such claims (for example premium trust funds).

5.5.20 Given the relatively small number of US resident Names, I have not investigated the situation with respect to bankruptcy in the USA.

5.5.21 There will be costs associated with obtaining a recovery from RITC including the following:

1. The added costs of additional actions for RITC recoveries against Original Year Names who also underwrote RITC with respect to the same Policy in later years;
2. The cost of locating and bringing an initial action against the Names who are RITC Names who were not also Original Year Names with respect to this Policy; and
3. The claim amounts for each RITC Name are likely to be smaller than claim amounts from Original Year Names. As a result, the Fragmentation effect will be more unfavourable and the Recovery Rate lower.

5.5.22 There is no existing legal mechanism to consolidate all of these claims.

Summary for Closed Year Names

5.5.23 However, if consolidation were possible, then the recoverability, recognising some additional costs in managing the 'combination' is shown in Table 5-7 below.

5.5.24 As with Table 5-6, I intend that Table 5-7 provides guidance only in assessing the range of possible Recovery Rates from Names, rather than precise figures.

Table 5-7
Recoverability Analysis – Closed Year Names

Item	Collection Issue	Recovery %		
		A	B	C
		Original Year Names Only	RITC Chain	Original Year Names – Long Direct
(1)	Death of Names	32%	67%	25%
(2)	Delay	98%	98%	98%
(3)	Bankruptcy/Past and Future	98%	97%	98%
(4)	Locating Names	95%	95%	95%
(5)	Fragmentation, Settlement & Policyholder Expense	46%	46%	34%
(6)	Variable Policyholder Expense	90%	85%	90%
(7)	**Combined Effect (Product of 1-7)**	12%	23%	7%

5.5.25 The assumptions in Table 5-7 are set out in Table 5-8 below.

Table 5-8
Notes in Respect of Table 5-7

Item	Original Year Names Only	RITC Chain	Original Year Names – Long Direct Policyholders
(1)	The 32% is calculated by taking the average of 28.3% and 36.4% from Table 5-2. Achieving that recovery from Names will be increasingly difficult after the death of the Name.	Same as value in Table 5-6. As there will be full access to the RITC Chain this indicates 73% probability is possible rather than 67%, but there will be instances where recoveries are not made. Further, while more Names might be reached, the costs will be higher than assumed in items (5) and (6).	It is expected that long duration direct Policyholders will be impacted by insolvencies in later years to a greater extent than the average Policyholder. Therefore, the average Survival Rate for Names will be less for Names on long direct Policies than for Names on all Policies. The Survival Rate for long direct Names is 25% as set out in Appendix XI.
(2)	Taken from Table 5-6.	Taken from Table 5-6. The delay might be longer because of time required to deal with RITC issues.	Taken from Table 5-6.
(3)	Taken from Table 5-6.	Slightly lower than Table 5-6 to reflect possible bankruptcies along the RITC chain.	Taken from Table 5-6.
(4)	Taken from Table 5-6. The probability could be lower to reflect additional difficulties in locating Names from older years.	Taken from Table 5-6. The probability could be lower to reflect additional difficulties in locating Names from older years.	Taken from Table 5-6.
(5)	Taken from Table 5-6.	Taken from Table 5-6.	Taken from Table 5-6. The probability is lower than Table 5-6 because of issues connected with Fragmentation and the RITC Chain combined.

Item	Original Year Names Only	RITC Chain	Original Year Names – Long Direct Policyholders
(6)	**Taken from Table 5-6.**	**Policyholder costs higher if pursuing claims through RITC than otherwise, so Recovery Rate is lower.**	**Taken from Table 5-6.**
(7)	**The Combined Effect is the product of the percentages in rows (1) to (6). This calculation assumes these effects are fully independent or have been selected to recognise the relationships (e.g., higher settlement loss is related to lower Policyholder expenses).**		

5.5.26 Values in Table 5-7 illustrate that Policyholders should not expect a Recovery Rate higher than 12% on Original Year Policies and 23% on the RITC Chain.

5.5.27 Giving 50% weight to each possible Recovery Rate, realistically the percentage of claim amounts recovered is no higher than 18% (the average of 12% and 23%).

5.5.28 I use 25%, equal to the Recovery Rate associated with Open Year Names, for discussion in section 7. However, I test the Transfer over a range of Recovery Rates from 0% to 75%.

5.6 RELATED ISSUES

5.6.1 To achieve the Recovery Rates from Names illustrated in Table 5-6 and Table 5-7, the liability must be managed effectively. In particular:

1. The liability would need to be measured at the Name and RITC level (Measurement);
2. Funds must be set aside for future payments at or close to the Equitas Insolvency date. (The Mortality calculation assumes that after Insolvency the death of a Name will not impede recovery by a Policyholder) (pre-funding); and
3. A mechanism is needed to manage the claims that will arise and need to be settled over many years (claim management).

5.6.2 It is possible, but not certain, that some of this could be accomplished through regulatory means.

Measurement

5.6.3 Determining the full chain of liabilities through the RITC Chain will be difficult and may not be possible with sufficient accuracy, for the reasons discussed immediately below.

5.6.4 On the one hand, some information is available or can be constructed with less difficulty:

4. The gross amounts paid or outstanding by Syndicate Year are already determined as part of the claims management process;
5. Reserves for unreported claims are determined for all years and all Syndicates combined, but could be allocated by Syndicate and year;
6. Syndicate Year liabilities can be allocated to Original Year Names, gross of Inter-Syndicate Reinsurance.

5.6.5 However, some information is not now readily available and/or is not straightforward to apply, for example:

1. Full details of Inter-Syndicate Reinsurance (ISR); and
2. Allocation of claims to RITC Syndicates and then to Names.

5.6.6 The exercise to determine the liability estimates through the Lloyd's RITC Chain and maintain that over time would be expensive. For example, as a comparator the initial R&R reserving and allocation exercise cost in excess of £100m[72] and took several years to complete.

5.6.7 In some ways the process to determine the RITC liability will be simpler because part of the 'machinery' is in place in RMSL.

[72] Source: Equitas

5.6.8 In other ways the process would be more complex because:

1. The reinsurance detail required is more extensive in that it would require a complete mapping of Inter-Syndicate Reinsurance;

7. Information is required at each level of the RITC Chain, not just the Original Year and Open Year; and

8. 'Accounting accuracy' will be required to 'bill' Names as compared to use of actuarial approximations considered sufficiently accurate for purposes of a settlement agreement such as was the case with the R&R analysis.

5.6.9 It is not clear which party, if any, could be ordered to finance this work. EPTL, perhaps the obvious candidate, is required to use its assets in accordance with its Trust Deed, which does not appear to contemplate expenditure for this purpose, and it is not subject to regulation by the FSA.

Pre-Funding

5.6.10 The potential for recovery by Policyholders against Names will be affected by the extent to which the liability of Names at the date of the Equitas Insolvency is pre-funded by Names.

5.6.11 If the liability is not pre-funded, then recovery by Policyholders, as claims emerge over the subsequent years, would be subject to the risk of non-payment due to death of the Name or change in financial condition of the Name subsequent to the date of bankruptcy. My analysis assumes that a pre-funding mechanism is implemented.

5.6.12 If a pre-funding mechanism is not implemented, the recovery from Names will be lower than I estimate.

5.6.13 The difference between the Survival Rate at the date of the Equitas Insolvency and the Survival Rate at date of payment in insolvency is significant. The average Survival Rate at date of payment for Open Year Names and Original Year Names would be 45% and 18%, respectively. These values can be compared to the Survival Rate at the date of insolvency, 67% and 32%, respectively (Tables Table 5-6 and Table 5-7, line 1). The corresponding Recovery Rates from Names would be 17% and 7% based on survival to date of payment compared to 25% and 12% (Table 5-6 and Table 5-7, line 7), respectively, based on survival to date of insolvency.

Claim Management

5.6.14 There is no existing mechanism for consolidating claims handling across Policyholders, Names, Years of Account, RITC Chain, and so on.

Impact on Recovery Rates from Names

5.6.15 The illustrative Recovery Rates in Table 5-6 and Table 5-7 assume that the claim measurement, pre-funding and claim management difficulties are resolved without significant cost beyond that assumed in the analysis. Therefore, the

illustrative Recovery Rates in Table 5-6 and Table 5-7 can be considered 'high' rather than 'low' estimates. Given the provisions of the Equitas Reinsurance Contract, it would be difficult for Lloyd's to assist or arrange for the making of cash calls on Open Year Names.

5.7 RELIANCES

5.7.1 I am relying on Clifford Chance/Baach Robinson legal input with respect to the following issues:

Table 5-9
Reliances on Clifford Chance/Baach Robinson

Issue	Paragraphs
Death	5.4.7 - 5.4.12, 5.4.14 (UK) 5.4.13, 5.4.14 (US)
Bankruptcy	5.4.23-5.4.24
Locating Names	5.4.25
EPTL obligations and responsibilities	5.6.9
Recovery of legal expense	5.4.55
Responsibility of Original Year Names	5.5.6 (UK) 5.5.7 - 5.5.9 (US)
Policyholder recovery from RITC after death	5.5.13, 5.5.14
Consolidating claims	5.5.22
FSA's role	5.2.4

5.7.2 I was assisted by Sidley Austin in interpreting these issues.

6 ANALYSIS – LIABILITY AND COVERAGE MODELS

6.1 INTRODUCTION

6.1.1 The purpose of section 6.2 is to discuss the Liability Model and the Coverage Model that is used to evaluate the financial aspects of the Transfer.

6.1.2 The purpose of section 6.3 is to explain why I believe it is appropriate to use the Equitas unpaid claim estimate at 31 December 2008 as a starting point for selecting the range of values around that estimate to test the effect of the Transfer.

6.1.3 The purpose of sections 6.4 and 6.5 is to explain why I believe it is appropriate to use the Liability Model and Coverage Model in my analysis of the Transfer.

6.2 PURPOSE OF THE MODELS

6.2.1 The purpose of the Liability and Coverage Models is to compare the financial position of Policyholders under the current structure, with their position in the event of the Transfer. For that purpose, the main unknowns are the following:

1. Ultimate value of Policyholder claims;
2. Timing of claim payment obligations; and
3. Timing of an Equitas Insolvency, if it were to occur.

6.2.2 Of these unknowns, the financial position of Policyholders is most sensitive to variation in the ultimate value of Policyholder claims.

6.2.3 While the ultimate value of claims is not known with certainty, it is known that:

1. If the ultimate value of claims is less than "$13.1bn"[73] then resources are adequate so that all valid claims can be paid in full, in the current structure and in the event of the Transfer.
2. If the ultimate value of claims is between "$13.1bn" and "$14.4bn" then resources are adequate so that all valid claims can be paid in full in the event of the Transfer, but if there is no Transfer then resources are inadequate (before any recoveries from Names).
3. If the ultimate value of claims is over "$14.4bn" then the resources are not adequate to pay claims in full regardless of whether the Transfer occurs or not. In this case, the shortfall (before any recoveries from Names) would be larger if there is no Transfer than it would be in the event of the Transfer.

6.2.4 A more detailed understanding of the effect of the Transfer requires an analysis of the probabilities that the claims are: under "$13.1bn"; between "$13.1bn" and "$14.4bn"; or over "$14.4bn". It also requires an understanding of the probabilities of shortfalls of any size.

6.2.5 Section 6.4 describes the Liability Model that I use to estimate these probabilities.

Timing

6.2.6 The assessment of the effect of the Transfer on Policyholders also depends on two aspects of timing.

6.2.7 Firstly, the effect on Policyholders depends on when claims are paid.

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[73] For simplicity in this introductory material, "$13.1bn" refers to $13.1bn of NICO cover plus the amounts available from the Equitas group assets that accumulate until claims are paid (if there is no Transfer), where claims paid refers to claims paid from 31 March 2006 onward, the trigger date for coverage in the NICO treaty. "$14.4bn" means the same with respect to the situation in the event of the Transfer with the purchase of additional coverage from NICO. This discussion also assumes that NICO has resources to meet its obligations in full.

6.2.8 If claims are more heavily weighted towards types that arise and are paid later, e.g., Mesothelioma Claims, then Equitas assets accumulate more investment returns and there would be more money available to pay Policyholders claims. Conversely, if claims are weighted towards types that are paid earlier, e.g., liability related to the remaining Catastrophe claims, then Equitas assets accumulate less investment return and there is less money available to pay Policyholder claims.

6.2.9 Secondly, the effect on Policyholders depends on when it might be recognised that assets are insufficient to pay valid claims, i.e., when any insolvency might be recognised.

6.2.10 The later the effective date of an insolvency the more Policyholders would have been paid in full than had the Equitas Insolvency been earlier. So the later the date of Equitas Insolvency the less money there is to pay the Policyholders who have claims that have not yet been paid, or have not yet arisen, when the Equitas Insolvency is recognised.

Liability Model

6.2.11 To assess the probabilities of shortfalls of various sizes as noted in paragraph 6.2.4, and the timing issues in respect of claims payments and potential insolvency, I used a statistical model which I refer to as the Liability Model.

6.2.12 The Liability Model used is a 'stochastic simulation' model, a method commonly used by actuaries to model uncertain future events. The Liability Model randomly constructs a range of scenarios of possible future claim amounts and the related timing of these claims.

6.2.13 The results of the model depend on the assumptions that were selected. These are described in section 6.4, and in further detail in Appendix VI.

6.2.14 Each scenario produced by the Liability Model gives information on amount and timing for:

1. All Policyholders combined;
2. All direct Policyholders;
3. All reinsurance Policyholders;
4. Long duration direct Policyholders; and
5. Long duration reinsurance Policyholders.

Coverage Model

6.2.15 A second model, which I refer to as the Coverage Model, applies the coverage terms and insolvency rules, if applicable, to each scenario.

6.2.16 The Coverage Model is applied to each of the Policyholder groups listed above.

6.2.17 I describe the Coverage Model in section 6.5 and Appendix VII.

6.3 THE BEST ESTIMATE – A STARTING POINT

6.3.1 A key parameter in the Liability Model is an estimate of the expected value of unpaid claims at the initial modelling date, 1 January 2009.

6.3.2 The Equitas estimate of the ultimate unpaid claims at 31 December 2008 is $7.8bn net of External Outwards Reinsurance.

Overview of Claim Types and Jurisdictions

6.3.3 The value of claims by type of claim is as follows:

Table 6-1
Unpaid Claims Estimates by Type of Liability

Liability Type	31-Aug-07	31-Aug-08	31-Aug-08
	$m	$m	%
Asbestos – US Direct	2,363	2,285	25%
Asbestos – US Inwards Reinsurance	2,467	2,383	26%
Asbestos – Non US*	949	1,066	12%
Pollution (Direct and Reinsurance)	1,237	1,221	14%
Health Hazard	790	693	8%
Catastrophes	539	457	5%
All Other Claims	974	891	10%
Total Gross	**9,319**	**8,996**	**100%**
External Outwards Reinsurance (other than NICO)	-768	-708	-8%
Total Net	**8,551**	**8,288**	**92%**
Accruals, paids to Dec 08 and other financial adjustments		-464	-6%
Total Net of External Outwards Reinsurance (31-Dec-08)		**7,824**	**87%**
Note: Future claim handing and other operating expenses	791	721	

Notes: *Primarily related to UK ($727m) and Australia ($339m) as at 31 August 2008. 2008 figures are converted to USD at the Contract Exchange Rate, 2007 figures £1 = $1.9909.
Source: Equitas

6.3.4 The figures in Table 6-1 include an estimate of claims on Policies with known exposures, future claims against Policies with no current exposures, and possible new types of claims that have yet to arise.

6.3.5 There have been a significant number of Policy buy-backs agreed between Equitas and major direct Asbestos Policyholders. This has materially reduced the amount of claims from US Asbestos direct Policyholders and has decreased the proportion of unpaid claim liabilities of direct Policies relative to the unpaid claim liabilities to reinsurance Policyholders.

6.3.6 The Policyholders are heavily, but not entirely, US based.

6.3.7 Table 6-2 below shows the undiscounted reserves by location and type of claim.

Table 6-2
Unpaid Claim Estimate By Location and Policyholder Type

Policyholder Type		Gross Undiscounted Reserves ($m)		Gross Undiscounted Reserves (%)	
Location	**Direct /Reinsurance**	**31/08/2007**	**31/08/2008**	**31/08/2007**	**31/08/2008**
US	Direct	3,796	3,639	40.7%	40.5%
US	Reinsurance	2,738	2,836	29.4%	31.5%
US Sub-Total		**6,534**	**6,475**	**70.1%**	**72.0%**
Canada	Direct	9	10	0.1%	0.1%
Canada	Reinsurance	14	15	0.1%	0.2%
Canada Sub-Total		**22**	**25**	**0.2%**	**0.3%**
UK	Direct	565	572	6.1%	6.4%
UK	Reinsurance	1,530	1,210	16.4%	13.4%
UK Sub-Total		**2,094**	**1,781**	**22.5%**	**19.8%**
EU	Direct	137	134	1.5%	1.5%
EU	Reinsurance	188	185	2.0%	2.1%
EU Sub-total		**325**	**319**	**3.5%**	**3.5%**
Australia	Direct	208	265	2.2%	2.9%
Australia	Reinsurance	52	83	0.6%	0.9%
Australia Sub-Total		**260**	**348**	**2.8%**	**3.9%**
Other	Direct	1	0	0.0%	0.0%
Other	Reinsurance	82	48	0.9%	0.5%
Other Sub-Total		**84**	**48**	**0.9%**	**0.5%**
Sub-Total	**Direct**	**4,716**	**4,619**	**50.6%**	**51.3%**
Sub-Total	**Reinsurance**	**4,603**	**4,376**	**49.4%**	**48.7%**
TOTAL	**All**	**9,319**	**8,996**	**100.0%**	**100.0%**

Notes: Unpaid claim amounts are gross of External Outwards Reinsurance.
The allocation between locations is approximate, as reserves are not developed in this level of detail.
Direct UK and Australian liabilities are primarily Asbestos related.
Centrewrite and Lioncover Policyholders are spread among these categories. Lioncover is approximately 8% and Centrewrite is under 1% of total undiscounted reserves at 31 Aug 2007 and 2008.
2008 figures are converted to USD at the Contract Exchange Rate, 2007 figures £1 = $1.9909
Source: Equitas

6.3.8 In Appendix V, I summarise the methods that Equitas uses to derive its estimate of future claims payments.

Analysis

6.3.9 I believe that the Equitas estimate of undiscounted reserves is a reasonable estimate. I use that value and a range of values around that estimate to test the effect of the Transfer.

6.3.10 In reaching this conclusion, I considered the following:

1. The reasonableness of the overall results, and the context in which this estimate was prepared ('top-down' review); and
2. The details of the August 2007 reserve analysis, which fed into the 31 December 2007 NICO financial report and the 31 March 2008 Equitas Group financial report ('bottom-up' review
3. My review of the August 2008 reserve analysis which fed into the 31 December 2008 NICO financial report and which will feed into the 31 March 2009 Equitas Group financial report.[74].

6.3.11 My top-down review considered the following, which are detailed in the following sections:

1. Track record;
2. Actuarial reports; and
3. Internal and external reviews.

Track Record

6.3.12 The reserving exercise is a standard process at Equitas, with a reserving report produced most years since R&R (approximately 13 years).

6.3.13 The reserve team at Equitas/RMSL has had low staff turnover over the years. Some of the team members have been at Equitas since its inception. I am satisfied that they understand the liabilities in detail, the Equitas coverage and the types of methods used by the actuarial profession to analyse the reserves.

6.3.14 The history of Equitas reserve estimates is shown below in Table 6-3.

[74] The values used in my analysis of the Transfer and the values shown in Table 6-2 and Table 6-3 are based on the August 2008 analysis I have reviewed the movements between the August 2007 actuarial analysis and the August 2008 actuarial analysis. I am in the process of reviewing the details of the August 2008 analysis. Nothing has come to my attention so far that would change the conclusions in this Report. I will report on the results of that review if there is an indication that there will be any changes from conclusions stated in this Report.

Table 6-3
Equitas Claims Paid and Reserve Movement Over Time

Period	Gross Reserve $m	Cumulative Paid $m	Ultimate $m	Release / (deterioration) $m
4-Sep-96	32,910		32,910	
31-Mar-97	28,779	3,991	32,770	140
31-Mar-98	24,957	7,300	32,257	513
31-Mar-99	21,246	10,704	31,950	307
31-Mar-00	19,601	13,935	33,536	-1,587
31-Mar-01	19,045	16,924	35,969	-2,433
31-Mar-02	16,251	18,820	35,072	897
31-Mar-03	14,245	20,300	34,545	527
31-Mar-04	12,110	22,490	34,600	-56
31-Mar-05	10,538	24,239	34,777	-177
31-Mar-06	9,720	25,434	35,154	-377
31-Mar-07	9,157	26,196	35,353	-199
31-Mar-08	8,595	26,810	35,405	-53
31-Dec-08	8,835	27,029	35,863	-458
				-2,953

Notes: All values are expressed using the Contract Exchange Rate. Source: RMSL

6.3.15 From this table the following can be seen:

1. Equitas has paid a cumulative total of $27.0bn in claims since 04 September 1996;
2. This is approximately 75% of the $35.9bn estimate of Equitas liabilities at 31 December 2008;
3. Reserve movements were materially unfavourable in 2000 ($1.6bn increase) and 2001 ($2.4bn increase) when claims numbers and total costs increased more rapidly than forecast by insurance analysts at the time;
4. Even with these increases, the total change in the estimated ultimate over the period 4 September 1996 to 31 December 2008 was an increase of $3.0bn, or 9.0% of the initial estimate, at the net level the difference is even smaller;
5. Excluding the peaks in 2000 and 2001, the movement in reserves over the period 04 September 1996 to 31 December 2008 was a (favourable) decrease of $1.1bn, or 3.2% of the initial estimate; and
6. Therefore, I consider the track record of reserve estimation results to be 'good', as the estimates have been reasonably accurate except for the years when Equitas was subjected to unexpected external shocks.

6.3.16 The fact that reserve development has been reasonably stable over the past 13 years provides comfort that Equitas reserve estimation results provide a

reasonable starting point for selecting a range of best estimates for testing the effect of the Transfer.

Actuarial Reports

6.3.17 I reviewed the Equitas actuarial reports[75] for the past five years and I observed that the methods have been generally consistent over time, albeit with regular refinement, including the use of more refined data, the examination of more individual Policyholder issues, and an increasing integration of actuarial and claim input.

Internal and External Financial Reviews

6.3.18 I have reviewed the audited financial statements of the Equitas Group for their comments with respect to reserve issues. Audit reports for the years running up to 2008 were all qualified in some respect however the 2008 Audit Report included an emphasis of matter paragraph relating to the provision for claims outstanding, but the audit opinion was not qualified. Those audit reports did not indicate issues with respect to the reserve process that would adversely affect my opinions with respect to the Transfer.

6.3.19 I reviewed Equitas board and audit committee reports for the past five years. None showed any issues relating to reserving that would suggest that the reserve process was not appropriate.

Market Testing

6.3.20 The actuarial reserves are a key input to Equitas management decisions on Policy buy-backs and commutations. Equitas has achieved a large number of Policy buy-backs at prices that are consistent with their actuarial methods. This acts as a market test of the reserve process, to some degree, with respect to the direct Asbestos and Pollution segments of the reserves.[76]

6.3.21 The Equitas liabilities were reinsured by NICO in the NICO Retrocession Agreement, exposing NICO to the risk that reserves would develop above the estimates at the time. This suggests NICO viewed the reserve process and results as reasonable.

Bottom Up Review

6.3.22 In addition to the top-down review, I supervised a bottom-up review of the August 2007 Equitas reserve analysis.

6.3.23 In this detailed review I was assisted by my team at Navigant which included other actuaries, claim experts, and economists. The team is familiar with US

[75] Actuarial Review of Claims Provisions as at 30 November 2003, 2004 and 2005 and Reserving Report for Retrocession of Equitas by NICO as at 31 August 2007 and 2008.

[76] I have not reviewed any specific buy-backs or commutations, but the actuarial report discusses the effect of buy-backs on the runoff and Equitas has a description of the relationship between actuarial process and claims in the evaluation process leading to commutations and buy-backs.

Asbestos, Pollution, Health Hazard risks; and UK and Australian Asbestos risks. The team is familiar with both direct and reinsurance business.

6.3.24 In our review we focussed on:

1. Identifying key assumptions – generic or account specific;
2. Observing whether the Equitas approach:
    a. was consistent with emerging Equitas experience;
    b. was consistent with good practice in reserving for these types of claim;
    c. made reasonable choices of parameters relative to our experience; and
    d. was consistent over time.

6.3.25 Appendix V describes the Equitas methods and provides more detail on the nature of my review within each of the reserve segments.

6.3.26 My personal role in this review was to evaluate a range of accounts, discuss the generic assumptions with our economics experts and actuaries, participate in meetings between Navigant and RMSL claims personnel, discuss the more unusual accounts with the Navigant actuaries on my team, and participate in discussions with Equitas regarding their methodology.

6.3.27 I also reviewed the August 2008 analysis with less emphasis on detail[77].

6.3.28 Based on our review I believe that the approach is reasonable, consistent with emerging Equitas experience, consistent with good practice, makes reasonable choices of parameters and is consistent over time.

6.3.29 On that basis, also given the top-down review, I considered it reasonable to use the Equitas reserve estimate as the starting point for selecting a range of values for testing the effect of the Transfer.

Calculations

6.3.30 In my bottom-up review, I did not systematically verify all of the Equitas calculations.

6.3.31 I believe it is reasonable to use the Equitas calculations because of the combination of the following:

1. RSML operate a peer review and checking regime that focuses on ensuring that there are no material errors or misstatements in the overall reserves. In addition, any individual claim evaluations for claims above a $350,000 threshold are generally subject to a peer valuation process involving the claims department;

[77] See footnote 74 related to paragraph 6.3.10.

2. Many calculations are done with spreadsheet and database systems that have been constructed, used and checked over time;
3. There was no evidence in the actuarial reports of any change in estimate due to calculation errors; and
4. In our review work we repeated some of their calculations, to verify our understanding of Equitas methods and to do sensitivity checking. In the course of that work we found no errors in their calculations.

Data

6.3.32 Data used in the Equitas analysis comes from sources including the following:

1. Equitas financial systems;
2. London market data, notably London Market Claims Services Limited (LMCS) data, KRA (Asbestos Reserve worksheets) coverage information, and counsel reports.

6.3.33 I did not audit the data, however I note points made in paragraph 6.3.34 and 6.3.35:

6.3.34 I believe that the Equitas information relating to unpaid claim reserves is reasonable because:

1. The data is subject to audit review processes;
2. There was no information in Equitas board or audit committee reports to indicate any significant data accuracy issues; and
3. The data in the actuarial reviews showed no significant inconsistencies from year to year.

6.3.35 With respect to the London market systems referred to in paragraph 6.3.32(2). I believe that the data is reasonable because:

1. Each of these systems has its own control mechanisms;
2. As the data is widely used by the London Market, errors have a high chance of being identified and corrected; and
3. The data is routinely used in business transactions such as reinsurance commutations and Policy buy-backs.

6.4 LIABILITY MODEL

6.4.1 This section gives an overview of the Liability Model. A detailed description of the model is in Appendix VI.

6.4.2 The Liability Model has four elements:

1. Distribution of ultimate claim liability by type of claim;
2. Overall distribution of ultimate claim liabilities;
3. Payment pattern; and
4. Inflation shocks and Liability shocks.

6.4.3 These elements are described below.

Distribution of Ultimate Claim Liability by Type of Claim

6.4.4 The model considers each of the seven types of claims listed in Table 6-1, except for the US Asbestos category, where direct and reinsurance is considered as a single category.

6.4.5 Equitas fit a lognormal distribution to each type of claim. The mean of the lognormal distribution is equal to the best estimate by type of claim from the Equitas actuarial analysis which I described in section 6.3 above.

6.4.6 The standard deviation of the lognormal distribution was selected to give a distribution that had a 75th percentile equal to the estimated 75th percentile of claim obligations for that type of business.

6.4.7 The main risks Equitas considered in assessing the 75th percentile of claim obligations for each type of claim were the following:

1. Asbestos: increased cost of Mesothelioma Claims, increase in costs related to unimpaired claimants, deterioration in experience for specific Policyholders, risk of claim coverage arising from Policies without aggregate limits, unknown coverage for known Policyholders, unknown Policyholders and risks arising from unexpected legislation or future coverage decisions;
2. Deterioration with respect to currently known liability issues including lead paint, sexual abuse, tobacco, silica or welding rods;
3. Adverse court decisions or new legislation;
4. Cost of claim monitoring;
5. Reinsurance recoverability; and
6. New latent claim risks or deterioration of existing minor claim risk.

6.4.8 The combined 75th percentile for all types of claims is most sensitive to the 75th percentile selected for US Asbestos claims.

6.4.9 The 75th percentile point for the US Asbestos claims is approximately 22% above the Equitas best estimate. This 22% margin is sufficient to accommodate a

reasonable degree of adverse development in areas such as (a) greater than expected claim trend in Mesothelioma Claims (b) more Mesothelioma Claims because the emergence pattern is longer than expected, (c) more assureds and/or Cedents.

6.4.10 The 75th percentile level was higher (as a percentage of the best estimate) for UK Asbestos and lower for other types of claims. I believe that the selected values are reasonable.

Overall Distribution of Ultimate Claim Liabilities

6.4.11 Equitas combined the six distributions by type of claim into an overall distribution using correlation coefficients.

6.4.12 Equitas selected three sets of correlation coefficients, based on their experience with these types of claim and professional judgement.

6.4.13 For the base and higher liability assumptions sets Equitas selected coefficients of 30% and 45%, respectively, between US and UK Asbestos and lower correlations among other pairs of claim types. I believe their choices are reasonable.

Payment Pattern, Inflation Shocks and Liability Shocks

6.4.14 The overall distribution of ultimate claim liabilities models the uncertainty in the total value of claim liabilities. The next step was to model how uncertainty in claim liabilities might emerge from year to year.

6.4.15 Reserves and claims are calculated for each year using a randomly generated payment pattern, along with inflation shocks and liability shocks (described below).

6.4.16 The expected payment pattern was generated by aggregating the payment patterns from the reserve analysis, over all types of claims.

6.4.17 Twenty-one alternative payment patterns were selected, some with longer and some with shorter duration payments than the expected pattern. In each simulation of the Liability Model one of these twenty-one payment patterns is selected at random.

6.4.18 Inflation shocks represent random movements in the inflation rate.

6.4.19 The model generates inflation shocks using the Wilkie Model, which is commonly used in actuarial projections.

6.4.20 Liability shocks reflect the various factors that will ultimately affect the total cost of claims, including type and number of claims, average claim costs, legal and judicial developments and so on.

6.4.21 Liability shocks follow a 'lognormal random walk', which is a commonly used actuarial model.

6.4.22 Equitas selected the parameters of the Liability Shocks so that the sum of the yearly claim liabilities matches the overall distribution of ultimate claim

liabilities. The calculation of the claim liabilities from the payment pattern and shocks is described in Appendix VII and Appendix VIII.

Output of the Liability Model

6.4.23 The output of the Liability Model is:

1. The value of claims for each of the fifty years in the projection period; and
2. The reserves for each of the fifty years in the projection period.

My review of the Liability Model

6.4.24 I believe that it is reasonable to use the results of the Liability Model in my analysis.

6.4.25 In reaching this conclusion, I considered the following:

1. The reasonableness of the overall results ('Top-down' review); and
2. The appropriateness of the model structure and assumptions ('Bottom-up' review).

Top Down Review

6.4.26 In my top-down review, I considered the following high level tests, which are detailed in the following sections:

1. Benchmarking; and
2. Examination of large events.

Benchmarking

6.4.27 One key output statistic from the model is the amount by which the liabilities exceed the mean at each of several confidence levels, expressed as a percentage of the mean. This statistic is shown in Table 6-4 below.

Table 6-4
Amounts Required to Reach Various Confidence Levels
Expressed as a Percentage of the Mean

	Variability Parameter		
Percentile	**Lower**	**Base**	**Higher**
95.0%	161%	170%	181%
97.5%	182%	197%	214%
99.0%	208%	231%	256%

Source: Equitas

6.4.28 For example, the value is 170% for the base liability assumption at a 95.0% confidence level. The mean estimate of the liability is $7.8bn as set out in Table 6.1. Therefore from this table it can be seen that there is a 95% probability that claims will be less than $13.3bn (170% * $7.8bn= $13.3bn).

6.4.29 PwC has compared the results of the Equitas model to results that PwC prepared for other clients, relating to liabilities similar to those of Equitas, which were used for the purposes of Part VII of FSMA transfers and other transactions.

6.4.30 PwC concluded that the Equitas model, with the base assumptions, produced slightly higher values for the statistics in Table 6-4 than those of their benchmarks.

6.4.31 This means that the Equitas model uses assumptions that may be more conservative than necessary. Less conservative assumptions would show the Transfer to be more favourable to Policyholders. Therefore, if Equitas had used the PwC assumptions, the Transfer would appear to be more favourable to Policyholders.

Examination of Large Events

6.4.32 A second way to consider the appropriateness of the model is to examine the model results in dollar amounts rather than percentages.

6.4.33 Using the Equitas base assumptions[78], the probability that liabilities will reach certain levels is shown in Table 6-5.

Table 6-5
Liability Amounts for Extreme Events (Base Assumptions)
Net of Reinsurance; Amounts at Dec 08 in $bn

Confidence Level	Chance of ultimate liability being this large	Liability amounts that will not be exceeded at the indicated confidence level ($bn)	Excess over mean compared to ultimate cost of US Asbestos ($17.5bn)
Mean		$7.8	0%
90.0%	1:10	$11.6	22%
95.0%	1:20	$13.3	31%
96.4%	1:28	$14.4	38%
99.0%	1:100	$18.1	59%
99.5%	1:200	$20.7	72%
99.9%	1:1000	$27.8	111%

Notes:$7.8bn reserve is reserve net of External Outwards Reinsurance (other than NICO), at the Contract Exchange Rate. Source: Equitas Liability Model (base assumptions).

6.4.34 The current NICO Retrocession Agreement covers liabilities up to $13.1bn. If the Transfer occurs, the NICO Retrocession Agreement will cover liabilities up to $14.4bn, and the reinsurance will cover liabilities at the 96.4% confidence level.

[78] Base assumptions are that the mean value is the best estimate from the reserving work, and the variability is the base variability.

In addition, the capital held in the Equitas Group (and Speyford) and future investment return on this capital will, to the extent that it is not required for the future operating expenses, enable further claims to be paid above the level of the NICO limit.

6.4.35 The events most likely to produce adverse development involve increases in costs for currently known types of claims, rather than a new type of claim.

6.4.36 Nonetheless, it is useful to compare these estimates with the total of Lloyd's and Equitas incurred cost for Asbestos. This provides a perspective on the scale of adverse development required to produce liabilities that reach these confidence levels. The total past and future claim cost to the 1992 and Prior Business for Asbestos is estimated by Equitas to be no more than $17.5bn[79].

6.4.37 Thus, for example, as illustrated in Table 6-5 an ultimate liability of $18.2bn (1:100 event) is $10.4bn above the current mean, $7.8bn. The excess is 59% of $17.5bn, the size of the Asbestos cost to Lloyd's and Equitas. The 1:1000 events are equivalent in size to an additional event 1.11 times the cost of Asbestos.

6.4.38 The likelihood of an event the size of Asbestos for Equitas is even lower than the likelihood of another Asbestos event for the entire insurance industry because:

1. Equitas liabilities cover only Policies in 1992 and prior years, and a future event will likely spread over more recent years as well as the 1992 and prior years (if they impact the 1992 and prior years at all);
2. There were indications of the emergence of Asbestos years before the claim costs emerged; and
3. Equitas has already settled 75% of the gross liabilities estimated in 1996 (paragraph 6.3.15(2)), and only $8.8bn remains unpaid (Table 6-3, 31 Dec 08 Gross Reserves).

6.4.39 The fact that the Equitas Liability Model includes the extreme events indicated by Table 6-5 provides further comfort that it is appropriate for use in analysing this Transfer.

Bottom-up Review

6.4.40 I reviewed the methods, assumptions and calculations used by Equitas in the model.

6.4.41 The Navigant team, including economists, claims experts and actuaries, assisted me in assessing whether the risk areas identified by Equitas were the appropriate ones.

6.4.42 There is no data from which variability assumptions can be readily derived without extensive reliance on the type of judgement that Equitas has exercised.

[79] The ultimate Asbestos cost to Lloyd's underwriting is not precisely known. Equitas estimates it to be under $17.5bn.

6.4.43 In addition, in my bottom-up review I considered the following high level tests, which are detailed in paragraphs 6.4.44- 6.4.49:

1. Alternative risk distributions; and
2. Sensitivity testing of assumptions;

Alternative Distributions

6.4.44 I instructed Equitas to perform a comparison between the extreme values (tail) of the selected liability distribution, with the extreme values for lognormal, Pareto and several other distributions.

6.4.45 The selected Liability Model predicts more extreme events than those alternative models, given comparable means and variability parameters.

Sensitivity Testing of Assumptions

6.4.46 Finally, I evaluated the Transfer using not only the model with the base assumptions, but also the 'higher mean' assumption; the 'higher variability' assumption; and the 'higher variability-higher mean' assumption.

6.4.47 The higher mean assumption is based on using a mean value of ultimate claim liabilities 20% above the base assumption. I believe a 20% range is 'prudent' for the purpose of assessing the effect of the Transfer.

6.4.48 This judgement is based on the following:

1. The track record of reserving results indicates no reason for a larger range;
2. The Equitas analysis includes a non-zero estimate of the probability weighted cost for some unlikely events; and
3. The range of best estimates is not intended to cover the range of all possible outcomes. The range of outcomes is the combined effect of the best estimate and the variability around the best estimate, as discussed below.

6.4.49 The higher variability assumption uses a coefficient of variation for US Asbestos that is 13% higher (a factor of 1.13 higher) than the coefficient of variation in the base assumptions and it uses correlation coefficients between types of claims that are 50% higher (a factor of 1.5) than the correlation coefficients in the base assumptions. The combined effect of these changes is an overall distribution with a coefficient of variation 16% higher than the base assumption.

6.4.50 These assumptions were selected by Equitas and I believe that they are reasonable as a high estimate. The base assumptions, without adjustment, are more conservative (higher) than may be necessary compared to other Part VII transfers. The effect of using the higher variability assumption can be observed by looking at the benchmarking results shown in Table 6-4.

6.4.51 Using the higher variability assumption (with the base mean assumption), the 95% confidence level is 181% of the mean or $14.2bn (1.81 * $7.8bn=$14.2bn) rather than $13.3bn for the base variability assumption. This is an increase of

$0.9bn. Similar calculations show that the effect of the higher variability assumption at the 97.5% confidence level is an increase of $1.3bn and the effect at the 99.0% confidence level is $2.0bn.

6.4.52 Thus, while the output of the Model is very sensitive to assumptions that cannot be fully tested empirically, I conclude that the model is appropriate for assessing the Transfer.

Verification of Calculations

6.4.53 The Liability Model has been checked in the following ways:

1. Equitas prepared the model initially and performed internal checks;
2. PwC independently prepared a model which reproduced the Equitas results, and Equitas and PwC confirmed the results were comparable; and
3. My team reviewed key formulas and calculations and found the calculations were as intended.

6.4.54 Moreover, because of the timing of the project, Equitas prepared results based on 2007 data and then updated all the results with 2008 data. We were able to observe that the model behaved as expected with the updated data.

6.4.55 Thus, having confirmed the calculations and selected an appropriate range of input parameters, I believe that it is reasonable to use the model in my analysis.

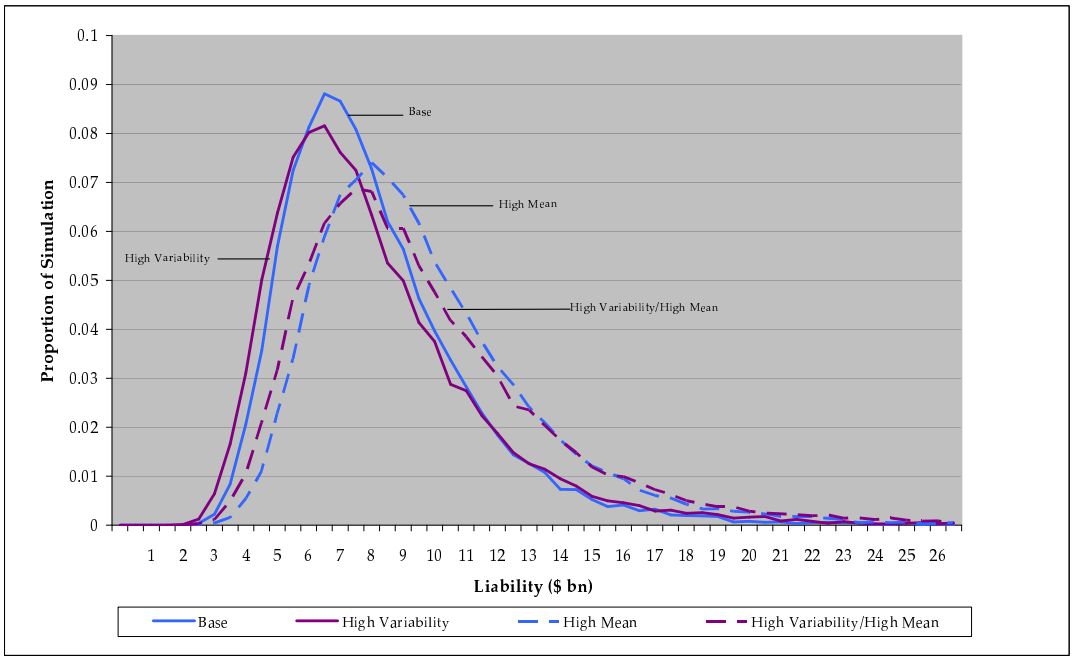
Data Accuracy

6.4.56 I discussed the data accuracy with respect to the best estimate in section 6.3. In respect of the other assumptions, the model relies on expert opinion with little additional data.

Results

6.4.57 Figure 6-6 shows the Liability Model results for the base, high mean and high variability/high mean assumptions.

Figure 6-6
Total Ultimate Claims-Base, High Mean and High Variability/High Mean Assumptions



6.5 COVERAGE MODEL

6.5.1 The Coverage Model uses the output of the Liability Model to estimate the claims that would be covered under each of the generated liability scenarios, with the current structure and in the event of the Transfer.

6.5.2 I describe the Coverage Model in Appendix VII, and give an example calculation for a given scenario in Appendix VIII.

Coverage

6.5.3 If there is no Transfer, then for each scenario from the Liability Model the amount of Policyholder protection is based on the following:

1. The existing NICO retrocession limit;
2. Assets in the Equitas Group, including investment income earned over time, less Equitas Group expenses; and
3. Recoveries from Names if the liabilities exceed the assets from (1) and (2) above. Recovery Rates ranging from 0% (no recovery) to 100% (full recovery) are evaluated.

6.5.4 In the event of the Transfer, the Coverage Model determines the amount of Policyholder protection based on the increased limit under the NICO Retrocession Agreement and the other assets in Speyford and the rest of the Equitas Group.

Initial Values / Fixed Parameters

6.5.5 The key fixed parameters used in the Coverage Model are:

1. Initial Reserves;
2. Initial Assets (including NICO cover[80] and Equitas assets);
3. Long term rate of investment return on Equitas assets and;
4. Recovery Rate from Names.

6.5.6 Note that 'Equitas' in this model includes all Equitas entities, and includes Speyford where relevant.

6.5.7 The initial reserves are the Equitas reserves at 31 December 2008.

6.5.8 Initial assets are the remaining NICO cover at 31 December 2008, plus Equitas Group capital at 31 December 2008 less the present value of future operating expenses, other than claim expenses in the event of an Equitas Insolvency.

6.5.9 Equitas estimates that the present value of future operating expenses is £30.9m in the current structure, and £24.7m in the event of a Transfer including a

[80] Including $1.3bn additional cover in the event of the Transfer and excluding the $1.3bn in respect of the current situation.

provision for additional costs associated with an Equitas Insolvency. These projections are consistent with their ongoing obligations and are small enough that the effect of the Transfer is not materially affected by this value.

6.5.10 The costs are lower in the event of the Transfer because under the NICO Retrocession Agreement, NICO will assume certain Speyford operating expenses.

6.5.11 The model uses a 4% p.a. long term investment return assumption. This is consistent with Equitas intention to adopt a conservative investment strategy which is likely to involve a significant proportion of long tail gilts.[81] My conclusion regarding the effect of the Transfer on policyholders is not sensitive to the rate of investment return within the range between 3% p.a. and 5% p.a. over the course of the payment period.

6.5.12 Claim expenses, if there are any for the Equitas Group (i.e., applicable only if there is an Equitas Insolvency, and then only after NICO cover is exhausted on a paid basis), are assumed to be 10% of claims.

Examples

6.5.13 Appendix VIII sets out an example scenario and shows the reserves and cash flows that determine the payments made to Policyholders.

6.5.14 The scenario presented in Appendix VIII is shown based on four assumption sets: base assumptions, the high mean assumption (Equitas reserve value plus 20%), the high variability assumption and the high mean and high variability assumptions. This illustrates the effect of the change in mean or change in variability on the cash flows to Policyholders and the resulting dividend rate.

Verification of Calculations

6.5.15 The Coverage Model has been checked in the following ways:

1. Equitas prepared the model initially and performed internal checks;
2. PwC independently prepared a model that reproduced the Equitas results; and
3. My team prepared a model that produced the same results.

Data Accuracy

6.5.16 The only new data in this model is from the estimated 1 January 2009 initial balance sheet for Equitas Group with pro-forma adjustments for the effects of the Transfer, if applicable.

6.5.17 I have not audited that information, but the pro-forma adjustments appear reasonable and the values are consistent with values at March 2008, and my analysis does not depend significantly on this starting position.

[81] Source: Equitas

Statistics to Evaluate the Effect on Policyholders

6.5.18 The output of the model is a variety of statistics on each simulation (25,000 simulations were run) including:

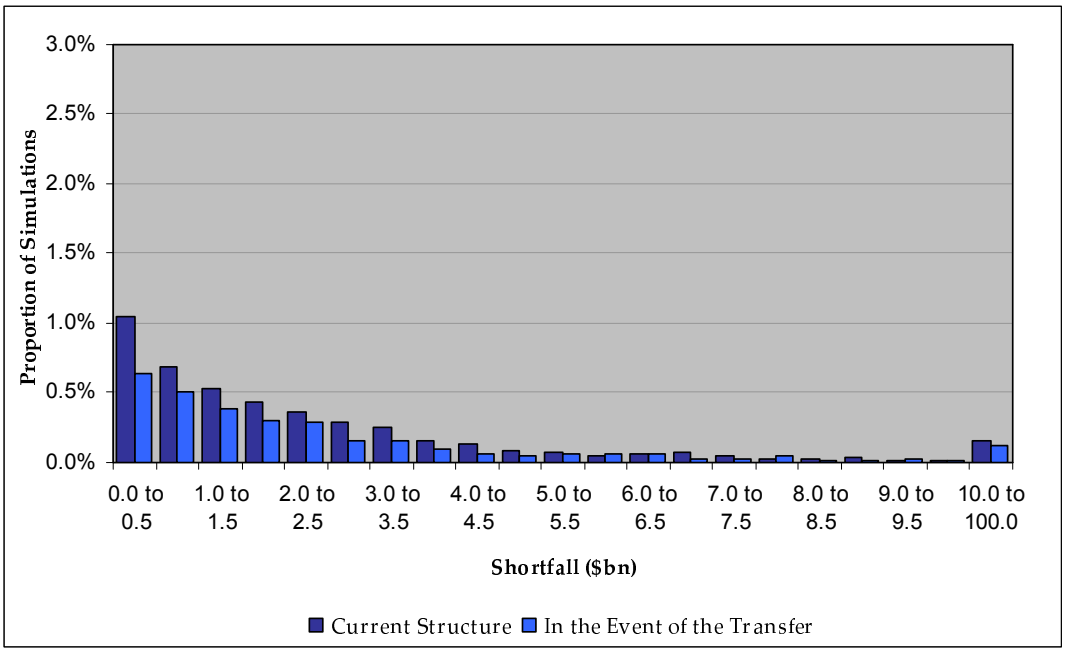
1. Full value of claims at each year;
2. Claim payments each year;
3. Year of Insolvency (if insolvency occurred);
4. Insolvency Dividend Rate (if insolvency occurred); and
5. Full value of claims and claim payments at selected times (e.g. after 50 years).

6.5.19 These statistics are measured:

1. In the current structure and in the event of the Transfer;
2. For direct, reinsurance and all Policyholders; and
3. Discounted and undiscounted where applicable.

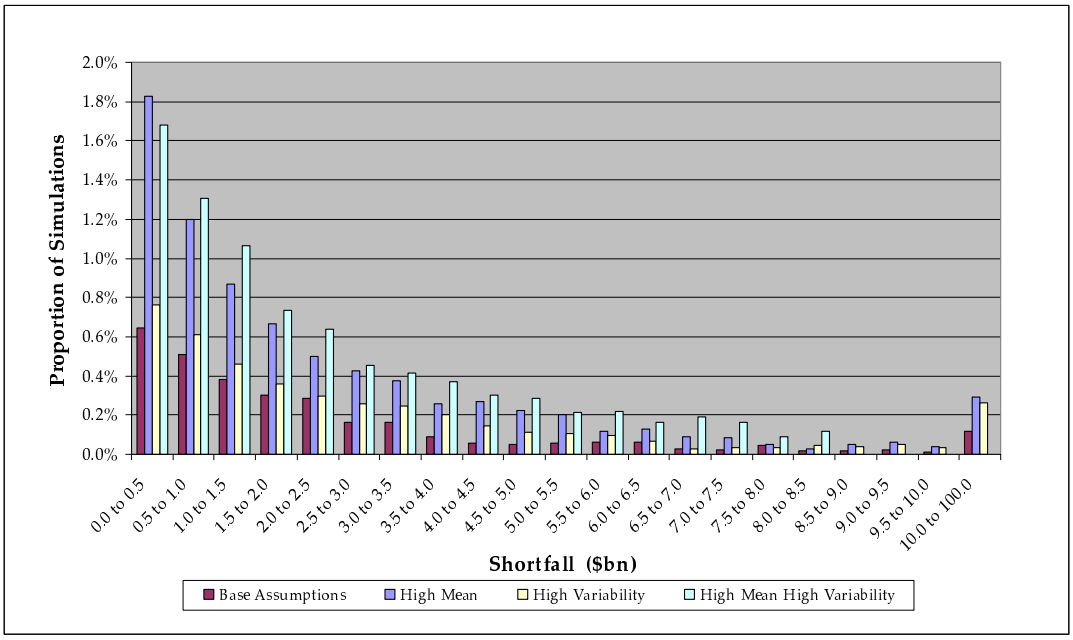
6.5.20 Figure 6-7 below shows the distribution of shortfalls by size for those scenarios where there is a shortfall (using the base assumptions).

Figure 6-7
Shortfall by Size (Base Assumptions)



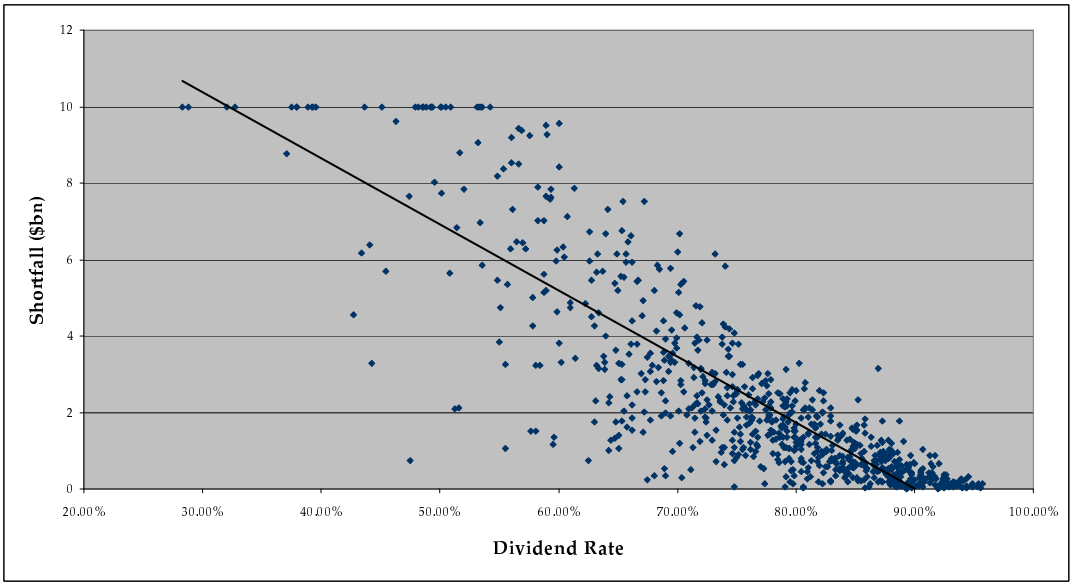
6.5.21 Figure 6-8 below shows the shortfall in the event of the Transfer for the four assumptions sets: base, high mean, high variability and high mean/high variability.

Figure 6-8
Shortfall by Size in the Event of the Transfer – Base, High Mean and High Variability Assumptions



6.5.22 Figure 6-9 below shows the scatter plot of dividend vs. shortfall for the base assumption in the event of the Transfer.

Figure 6-9
Insolvency Dividend Rate Vs Shortfall In the event of the Transfer



Note: Shortfalls over $10bn have been truncated to $10bn for illustration.

6.5.23 The scatter plot above shows that:

1. Shortfalls are generally below $2bn;
2. Insolvency dividend rates are generally over 80%;
3. The insolvency dividend rate decreases with larger shortfalls; and
4. For the largest shortfalls, the dividend rates are around 30%.

6.5.24 In section 7 I discuss how I use the results of the two models described above to analyse the effect of the Transfer on the various groups of Policyholders.

7 ANALYSIS – CONCLUSIONS – NICO COVERAGE AND SECURITY FROM NAMES

7.1 INTRODUCTION

7.1.1 The purpose of this section is to present my conclusions regarding the extent to which any Policyholder group might be materially disadvantaged in the event of the Transfer.

1. Identifying the variables I used to assess the Transfer - section 7.2;
2. Identifying the Policyholder groups I need to assess - section 7.3;
3. Illustrating the assessment measures - section 7.4;
4. Evaluating the effect of the Transfer on all Policyholders combined – section 7.5;
5. Evaluating the effect of the Transfer on average direct Policyholders and average reinsurance Policyholders - section 7.6;
6. Evaluating the effect on long duration reinsurance Policyholders – section 7.7; and
7. Evaluating the effect on long duration direct Policyholders - section 7.8.

7.2 IDENTIFYING THE VARIABLES

7.2.1 For each of the Liability Model assumption sets[82] the Liability Model produces 25,000 scenarios of future cash flows.

7.2.2 For each set of 25,000 scenarios, I focus on the following information:

1. Whether the claims are paid in full;
2. The 'Policyholder deficit', defined as the difference between the full amount of a Policyholder claim (discounted) and the amount paid to the Policyholder (discounted), usually measured as a percentage of the full amount of the claim (discounted); and
3. In most scenarios the Policyholder deficit is zero. The concept of Policyholder deficit is useful in measuring the impact on Policyholders in those events when there is an Equitas Insolvency and claims are not paid in full.

7.2.3 For scenarios in which claims are not paid in full by NICO/Equitas then the amount the Policyholder receives is the full claim amount times the dividend rate for that scenario plus any recovery from Names.

7.2.4 The information in paragraph 7.2.2 is summarised for the 25,000 scenarios combined, for each of a range of Recovery Rates from Names, for the current structure and for the structure in the event of the Transfer.

7.2.5 The summary provides four measures that I use to evaluate the effect of the Transfer on Policyholders. These four measures are as follows:

1. The difference between the following (**probability of full payment**):
   a. The probability that claims are paid in full in the current structure; and
   b. The probability that claims are paid in full in the event of the Transfer.
2. The difference between the following (**better vs. worse**):
   a. The percentage of scenarios where the Policyholder is better off in the current structure (for a given Recovery Rate from Names); and
   b. The percentage of scenarios where the Policyholder is better off in the event of the Transfer[83].

[82] The sets of assumptions are as follows: base assumptions, high mean (base variability), high variability (base mean) and high mean/high variability. The analysis is also done for lower mean and lower variability assumptions. As the Transfer is more favourable from the perspective of those more favourable assumptions, I do not discuss those.

[83] In determining whether Policyholders are better or worse off, the model compares the present value of claim payments to the Policyholder under the two coverage situations. By using present values, the model reflects the differences in timing of payments as well as amounts of payment depending on whether the Transfer is approved.

3. The difference between the following (**Expected Policyholder Deficit** or **EPD difference**):
    a. The average (also called expected value) of the discounted Policyholder deficit in the current structure (for a given Recovery Rate from Names); and
    b. The average (also called expected value) of the discounted Policyholder deficit in the event of the Transfer.
4. The **truncated EPD difference** which is the same calculation as in item 3 above, but the 0.5% of events which generate the largest EPD differences are excluded (or truncated) from the averages.

7.2.6 The first two measures describe the relative number of scenarios in which the Transfer would be beneficial, or not, for Policyholders, and I refer to them as frequency measures.

7.2.7 The last two measures consider the size of the difference, and I refer to them as severity measures.

7.2.8 EPD values are very sensitive to even a small number of tail events with extremely large values, i.e. values which are many times larger than the expected claims. That is why I also measured the EPD difference excluding the 0.5 % of events which generate the largest EPD differences.

7.3 IDENTIFYING THE POLICYHOLDER GROUPS

7.3.1 The change in Policyholder protection in the event of the Transfer varies by type of Policyholder as between:

1. Direct and reinsurance Policyholders;
2. Policyholders for whom claims are currently being paid and Policyholders for whom no claims might be paid for decades into the future. (Short Duration Policyholders vs. Long Duration Policyholders);
3. Policyholders from more recent Years of Account and Policyholders from older Years of Account; and
4. Policyholders who are not covered by Overseas Trust Funds and Policyholders who are covered by such Trust Funds.

7.3.2 Based on the Policyholder characteristics in items 1-3 there are eight Policyholder subgroups [(2 for direct vs. reinsurance) * (2 for long duration or short duration) * (2 for recent years or older years)].

7.3.3 In this section I assess the position of each of these eight Policyholder groups.

7.3.4 I discuss the position of Policyholders not covered by Overseas Trust Funds in section 9.

Direct and Reinsurance Policyholders

7.3.5 The Transfer might have a different effect on direct Policyholders than on Reinsurance Policyholders for the reasons listed in the paragraphs below.

7.3.6 Direct Policyholders have priority over reinsurance Policyholders with respect to Speyford assets in the event of an Equitas Insolvency.

7.3.7 In addition, direct and reinsurance Policyholders have different payment patterns, so earlier or later insolvencies affect these Policyholder groups differently.

Policyholders with Long Duration vs. Short Duration Claims

7.3.8 Longer duration Policyholders are potentially disadvantaged compared to shorter duration Policyholders because the long duration Policyholders have a more extended period of exposure to a possible Equitas Insolvency compared to shorter duration Policyholders. This might be offset, to some extent, with the passage of time as the protection afforded by Names would also decrease.

7.3.9 When looking for the most extreme examples of long duration Policyholders it is not simply an issue of when their last claim will be paid, it is the average time at which their claims are paid that is much more relevant. Thus when I use the term "duration" in this Report I refer to the average time of claim payments.

Direct Long Duration Policyholders

7.3.10 The most extreme long duration direct Policyholders are claims on employers liability Policies in the UK. In many cases the original employer is bankrupt, in

these circumstances employees can bring claims directly against the insurer if certain conditions are satisfied[84]. Thus for this analysis I treat an individual mesothelioma claimant in 50 years time as an individual Policyholder.

7.3.11 Whilst it is possible that there may be other examples of direct Policyholders with claims of similar long duration, based on information from Equitas, I do not believe that these will be longer in duration. Therefore for my analysis I use individual UK mesothelioma claimant in 50 years time as the most extreme type of Policyholder situation for purposes of my analysis.

Reinsurance Long Duration Policyholders

7.3.12 For reinsurance Policyholders, I need to consider the average duration of all the claims for each reinsurance Policyholder to see which such Policyholders have claims with the longest duration.

7.3.13 Based on information from Equitas, the reinsurance Policyholders with the longest duration claims are those whose Policies relate primarily to the reinsurance of US workers compensation claims and which have relatively high attachment points which most claimants will not reach for a number of years.

7.3.14 It might have been expected that reinsurance Policyholders with primarily Asbestos claims would have the longest duration; however, although they will indeed have claims that stretch out a long time into the future, they also tend to have a relatively high level of claims outgo over the shorter term as well.

Policyholders Related to Original Year Names[85] vs. Open Year Names

7.3.15 A Policyholder contract might involve both Open Year Names and Original Year Names. Some might be entirely, or more weighted towards, Original Year Names rather than Open Year Names. The position of contracts dominated by Original Year Names might differ from the position of contracts largely insured by Open Year Names, as Original Year Names are older on average (which is potentially adverse for Policyholders) and have RITC (potentially helpful for Policyholders).

7.3.16 Given that it is possible that the security for Policyholders differs depending on the extent to which their Policies are covered by Open Year Syndicates or Original Year Syndicates. Therefore I evaluate the Policyholder as if covered by an Open Year Syndicate and I also evaluate the Policyholder as if covered by an Original Year Syndicate. This shows the range of possible recoveries.

[84] The 1930 Act. Subject to criteria set out in the Act.

[85] In this section I use the term Original Year Names to refer to groups of Original Year Names who include, in part at least, some Original Year Names who are not also Open Year Names. I use the term Open Year Names to refer to groups of Names who are only Open Year Names.

7.4 ILLUSTRATION OF ASSESSMENT MEASURES

7.4.1 In this section, I apply the four tests to all direct Policyholders combined and to all reinsurance Policyholders combined.

7.4.2 I illustrate the results using a 25% Recovery Rate. The 25% Recovery Rate is representative for Policyholder contracts with Open Year Names, using the base assumptions in the Liability Model.

Probability of Full Payment Test

7.4.3 Table 7-1 shows the probability of full payment for direct Policyholders.

Table 7-1
Direct Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Scenarios Paid in Full	23,864	24,245	381
(2)	Scenarios Not paid in Full	1,136	755	381
(3)	Total Number of Scenarios	25,000	25,000	0
(4)	Probability claims paid in full (Solvency rate)	95.5%	97.0%	1.5%
(5)	Probability claims not paid in full (Insolvency rate)	4.5%	3.0%	1.5%

Notes: (1), (2), (3) Data from Coverage Model. Number of scenarios is always 25,000.
(4)=(1)/ (3) as a percentage; (5)=(2)/ (3) as a percentage
(Base Liability Assumptions – 25% Recovery Rate from Names)
*(If the "Difference" column shows a positive this means the Transfer is advantageous to Policyholders)

7.4.4 In the current structure, Table 7-1 shows that:

1. There are 23,864 scenarios in which the current coverage is sufficient. This is a 95.5% solvency rate. (Lines 1 and 4 – Current Structure); and
2. Equivalently, there are 1,136 scenarios that would produce an Equitas Insolvency with the current structure. This implies a 4.5% insolvency rate (Lines 2 and 5 - In the event of the Transfer).

7.4.5 In the event of the Transfer, Table 7-1 shows that:

3. There are 24,245 scenarios in which the current coverage is sufficient. This is a 97.0% solvency rate. (Lines 1 and 4 – Current Structure); and

4. Equivalently, there are 755 scenarios that would produce an Equitas Insolvency in the event of the Transfer. This implies a 3.0% insolvency rate (Lines 2 and 5 - In the event of the Transfer)[86].

7.4.6 Comparing the current structure to the structure in the event of the Transfer we see that:

1. The Transfer reduces the insolvency rate from 4.5% to 3.0%;
2. This reduces the risk of insolvency by 1.5 percentage points; and
3. Stated differently, the Transfer reduces the risk of insolvency by 33% (1.5% divided by 4.5%).

7.4.7 Table 7-2 below shows the same type of results for reinsurance Policyholders.

Table 7-2
Reinsurance Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Scenarios Paid in Full	23,864	24,225	361
(2)	Scenarios Not paid in Full	1,136	775	361
(3)	Total Number of Scenarios	25,000	25,000	0
(4)	Probability claims paid in full (Solvency rate)	95.5%	96.9%	1.4%
(5)	Probability claims not paid in full (insolvency rate)	4.5%	3.1%	1.4%

Notes: (1), (2), (3) Data from Coverage Model. Number of scenarios is always 25,000.
(4)= (1)/ (3) as a percentage; (5)= (2)/ (3) as a percentage
(Base Liability Assumptions – 25% Recovery Rate from Names)
*(Difference column is a positive number meaning the Transfer is advantageous to Policyholders)

7.4.8 In the current structure, Table 7-2 shows that:

1. There are 23,864 scenarios in which the current coverage is sufficient so that reinsurance Policyholder claims are paid in full. This is a 95.5% solvency rate. (Lines 1 and 4 – Current Structure); and
2. Equivalently, there are 1,136 scenarios in which reinsurance Policyholder clams are not paid in full in the current structure. This is implies a 4.5% insolvency rate (Lines 2 and 5 - In the event of the Transfer).

7.4.9 In the event of the Transfer, Table 7-2 shows that:

[86] In the event of a Transfer, there might be an insolvency in which direct Policyholders are paid in full but reinsurers are not. By solvency rate I mean the solvency rate from the perspective of the Policyholder group I am discussing, in this case, the direct Policyholders.

1. There are 24,225 scenarios in which reinsurance Policyholder claims are paid in full. This is a 96.9% solvency rate for reinsurance Policyholders. (Lines 1 and 4 – Current Structure); and
2. Equivalently, there are 775 scenarios in which reinsurance Policyholders would not be paid in full in the event of the Transfer. This implies a 3.1% insolvency rate for reinsurance Policyholders (Lines 2 and 5 - In the event of the Transfer).

7.4.10 Comparing the current structure to the structure in the event of the Transfer we see that:

1. The Transfer reduces the insolvency rate from 4.5% to 3.1% for reinsurance Policyholders;
2. This reduces the risk of insolvency by 1.4 percentage points; and
3. Stated differently, the Transfer reduces the risk of an Equitas Insolvency by about 31% (1.4% divided by 4.5%) for reinsurance Policyholders.

7.4.11 Comparing the position of direct Policyholders (Table 7-1) and reinsurance Policyholders (Table 7-2) it can be seen that:

1. In the current structure, the probability that reinsurance Policyholders will be paid in full is 95.5%, and the insolvency ratio is 4.5% (lines 4 and 5- Current Structure). These are the same solvency and insolvency ratios as for direct Policyholders because there is no difference in payment priority in the current structure;
2. In the event of the Transfer, the probability that reinsurance Policyholders are paid in full increases to 96.9% and the corresponding insolvency ratio reduces to 3.1% (lines 4 and 5 – in the event of the Transfer);
3. The reduction in risk of insolvency for reinsurance Policyholders is slightly less favourable than the reduction for direct Policyholders because of the priority in payments given to direct Policyholders with respect to Speyford assets (that is assets other than the EL and NICO reinsurances); and
4. Nonetheless, the risk that their claims will not be paid in full is reduced for both direct and reinsurance Policyholders.

Better vs. Worse Test

7.4.12 Table 7-3 shows better vs. worse information for all direct Policyholders.

Table 7-3
Direct Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Total Number of Scenarios	25,000	25,000	0
(2)	Better off in the event of the Transfer because insolvency is avoided	0	361	361
(3)	Better off even though there is an Equitas Insolvency	168	607	439
(4)	Total Better off	168	968	800
(5)	% Better off	0.7%	3.9%	3.2%

Notes: (1), (2), (3), (4) Data from Coverage Model. Number of scenarios is always 25,000.
(5)= (4)/ (1) as a percentage
(2) Note: that in 20 scenarios there is an insolvency but direct Policyholders are paid in full (due to priority with respect to Speyford assets)
(Base Liability Assumptions – 25% Recovery Rate from Names)
*(If the 'Difference' column shows a positive this means the Transfer is advantageous to Policyholders)

7.4.13 Table 7-3 shows the following:

1. In 361 of the scenarios Policyholders benefit because they would experience an Equitas Insolvency with the current structure, but no Equitas Insolvency in the event of the Transfer;
2. In 607 scenarios Policyholders are better off in the event of the Transfer, even though there is an Equitas Insolvency; and
3. In 168 scenarios Policyholders are better off with the current structure, even though there is an Equitas Insolvency.

7.4.14 In summary, direct Policyholders are better off more often in the event of the Transfer (361 + 607 = 968 times) than under the current structure (168 times).

7.4.15 Table 7-4 shows better vs. worse information for all reinsurance Policyholders.

Table 7-4
Reinsurance Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Total Number of Scenarios	25,000	25,000	0
(2)	Better off in the event of the Transfer because insolvency is avoided	0	361	361
(3)	Better off even though there is an insolvency	175	600	425
(4)	Total Better off	175	961	786
(5)	% Better off	0.7%	3.8%	3.1%

Notes: (1), (2), (3), (4) Data from Coverage Model. Number of scenarios is always 25,000.
(5)= (4)/ (1) as a percentage
(Base Liability Assumptions – 25% Recovery Rate from Names)
*(If the 'Difference' column shows a positive number this means the Transfer is advantageous to Policyholders)

7.4.16 Table 7-4 shows the following:

1. In 361 of the scenarios reinsurance Policyholders benefit because they would experience an Equitas Insolvency with the current structure, but no Equitas Insolvency in the event of the Transfer (Line 2). This is also the value from Table 7-3 line 2);
2. In 600 scenarios, reinsurance Policyholders are better off in the event of the Transfer, even though there is an Equitas Insolvency in that structure; and
3. In 175 scenarios reinsurance Policyholders are better off with the current structure even though there is an Equitas Insolvency. Thus, reinsurance Policyholders are better off in the event of the Transfer more often than under the current structure. The advantage is slightly less for reinsurance Policyholders than for direct Policyholders (3.1% vs. 3.2%).

7.4.17 However, by this measure the Transfer is advantageous for both groups of Policyholders.

EPD and Truncated EPD Tests

7.4.18 Table 7-5 and Table 7-6 show the EPD and truncated EPD values for direct Policyholders and reinsurance Policyholders respectively.

Table 7-5
Direct Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Expected Policyholder Deficit	0.73%	0.64%	0.09%
(2)	Truncated EPD (0.5% excluded)	0.45%	0.32%	0.13%

Notes: (Base Liability Assumptions – 25% Recovery Rate from Names)
*(If the 'Difference' column shows a positive number this means the Transfer is advantageous to Policyholders)

7.4.19 Table 7-5 line 1 shows that the EPD is 0.7% in the current structure and 0.6% in the event of the Transfer. As the EPD decreases in the event of the Transfer, the Policyholder is better off in the event of the Transfer.

7.4.20 The truncated EPD difference remains at 0.1 percentage points. In general, eliminating the 'worst' scenarios in the EPD calculation will make the EPD measure more favourable for the Transfer, but in some cases the difference is not significant.

7.4.21 With respect to the EPD and truncated EPD tests, direct Policyholders are better off in the event of the Transfer.

Table 7-6
Reinsurance Policyholders
Analysis of the Effect of the Transfer

Item	Description	Current Structure	In the event of the Transfer	Difference*
(1)	Expected Policyholder Deficit	0.64%	0.58%	0.06%
(2)	Truncated EPD (0.5% excluded)	0.39%	0.29%	0.10%

Notes: (Base Liability Assumptions – 25% Recovery Rate from Names)
*(If the "Difference" column shows a positive number this means the Transfer is advantageous to Policyholders)

7.4.22 Table 7-6 shows that the position is essentially the same for reinsurance Policyholders as for the direct Policyholders. The EPD and truncated EPD tests are better by 0.1 percentage points in the event of the Transfer.

7.4.23 Thus, with respect to the EPD and truncated EPD tests, reinsurance Policyholders are better off in the event of the Transfer.

7.5 EVALUATING THE EFFECT OF THE TRANSFER ON ALL POLICYHOLDERS COMBINED

7.5.1 Section 7.4 examined the results with a particular liability assumption and with respect to a particular Recovery Rate from Names.

7.5.2 This section considers the four liability assumption sets and a range of Recovery Rates from Names.

Probability of Being Paid in Full:

7.5.3 Table 7-7 shows the risk of an Equitas Insolvency under each of the liability assumptions.

Table 7-7
All Policyholders Risk of an Equitas Insolvency

Liability Assumption	Risk of an Equitas Insolvency		
	A	B	C
	In the Current Structure	In the event of the Transfer	Difference
Base Variability, Mean = 100% Reserves	4.5%	3.1%	1.4%
Higher Variability, Mean = 100% Reserves	5.9%	4.2%	1.7%
Base Variability, Mean = 120% Reserves	10.8%	7.7%	3.1%
Higher Variability, Mean = 120% Reserves	12.5%	9.2%	3.3%

7.5.4 In the current structure, in the event of an Equitas Insolvency the Recovery Rate from Names will be less than 100%.

7.5.5 Thus, in the current structure the risk that some Policyholders are not paid in full equals the risk of an Equitas Insolvency and the results of Table 7-7 apply regardless of the Recovery Rates from Names.

7.5.6 Table 7-7 shows the following:

7.5.7 The risk of an Equitas Insolvency increases as the assumptions become less favourable (looking down rows of columns A and B).

7.5.8 In the event of the Transfer the risk of an Equitas Insolvency decreases (comparing column A to column B).

7.5.9 Therefore, for all liability assumptions and all Recovery Rates, the probability of being paid in full increases in the event of the Transfer.

7.5.10 The final column on Table 7-7 shows that the improvement in the probability of being paid in full in the event of the Transfer increases as the assumptions become less favourable.

7.5.11 This is because, the $1.3bn of additional cover has more effect in reducing the risk of an Equitas Insolvency if the mean is higher and therefore closer to the attachment point (high mean). Similarly, the $1.3bn of additional cover has

more effect in reducing the risk of an insolvency if the variability is higher, increasing the chance of exceeding the attachment point.

7.5.12 Figure 7-8 shows key statistics for evaluating the Transfer using a range of liability assumptions and Recovery Rates from Names.

Figure 7-8
Sensitivity Tests/Key Statistics for All Policyholders

		All Policyholders			
Liability Assumption	**Recovery Rate from Names**	**Prob. being paid in full (change) (1)**	**% scenarios better off less % worse off (2)**	**EPD (change) (3)**	**Truncated EPD (change) (4)**
Base Variability, Mean = 100% Reserves	0%	1.4%	4.5%	0.3%	
	10%	1.4%	4.4%	0.2%	
	20%	1.4%	3.6%	0.1%	0.1%
	30%	1.4%	2.7%	0.0%	0.1%
	40%	1.4%	1.6%	**-0.1%**	0.0%
	50%	1.4%	0.7%	**-0.2%**	**0.0%**
	75%	1.4%	**-0.8%**	**-0.4%**	
Higher Variability, Mean = 100% Reserves	0%	1.7%	5.9%	0.4%	
	10%	1.7%	5.6%	0.3%	
	20%	1.7%	4.4%	0.1%	0.2%
	30%	1.7%	2.6%	**0.0%**	0.1%
	40%	1.7%	1.2%	**-0.2%**	**0.0%**
	50%	1.7%	0.2%	**-0.3%**	**-0.1%**
	75%	1.7%	**-1.6%**	**-0.7%**	
Base Variability, Mean = 120% Reserves	0%	3.1%	10.8%	0.7%	
	10%	3.1%	10.5%	0.5%	
	20%	3.1%	8.5%	0.3%	0.3%
	30%	3.1%	5.7%	0.0%	0.1%
	40%	3.1%	3.3%	**-0.2%**	**0.0%**
	50%	3.1%	1.3%	**-0.4%**	**-0.2%**
	75%	3.1%	**-2.3%**	**-0.9%**	
Higher Variability, Mean = 120% Reserves	0%	3.3%	12.3%	0.9%	
	10%	3.3%	12.0%	0.5%	
	20%	3.3%	8.8%	0.2%	0.3%
	30%	3.3%	5.5%	**-0.1%**	0.1%
	40%	3.3%	2.7%	**-0.4%**	**-0.2%**
	50%	3.3%	0.3%	**-0.7%**	**-0.4%**
	75%	3.3%	**-3.6%**	**-1.5%**	

Better off vs. worse off

7.5.13 The Policyholder is better off in the event of the Transfer for any Recovery Rates from Names up to levels in excess of 50% (to a value between 50% and 75%).

EPD Test

7.5.14 The EPD tests show the Policyholder is better off in the event of the Transfer for Recovery Rates from Names up to about 30%, for all liability assumptions.

Truncated EPD Test

7.5.15 The truncated EPD test is favourable for Recovery Rates from Names up to 40% becoming unfavourable (between 40% and 50%), for base, high mean and high variability liability assumptions.

7.5.16 The truncated EPD test is favourable up to slightly less than a 35% Recovery Rate for the high mean/high variability assumptions.

7.5.17 The EPD truncated at 1.0%, rather than 0.5% would be favourable for up to just over a 35% Recovery Rate for the higher mean / higher variability assumptions.

Analysis—Advantageous, Slightly Disadvantageous and Materially Disadvantageous

Advantageous

7.5.18 If the EPD difference is positive then the Transfer is advantageous based on that test.

Slightly Disadvantageous (not Materially Disadvantageous)

7.5.19 If the EPD difference is slightly negative the Transfer might be only slightly disadvantageous.

7.5.20 There is no actuarial standard that firmly divides between 'slightly' and 'significantly' for this context. Nor is there any standard for this division in relation to Part VII of FSMA transfers.

7.5.21 Measures of confidence used by regulators for assessing financial condition provide one reasonable benchmark.

7.5.22 The European Union Solvency II Draft Directive proposes that the solvency level is set at a 99.5% confidence level, a 0.5% chance that assets are not sufficient to cover liabilities, over a one-year time period.

7.5.23 This confidence level is discussed, in part, as equivalent to a "Triple B Rated (BBB) bond default" rate where BBB is often viewed as the level that separates investment grade from non-investment grade bonds using the S&P rating criteria.

7.5.24 Therefore, I believe 0.5% represents a reasonable basis against which to judge the impact of the Transfer (and perhaps a harsh test - when assessing the impact of the Transfer).

7.5.25 For the EPD tests the 0.5% standard means measuring the EPD excluding the 0.5% of events which generate the largest EPD differences (125 out of 25,000). I refer to the EPD excluding a set of scenarios as a truncated EPD.

7.5.26 For the better or worse test, the 0.5% standard means that a difference of up to 0.5% is only slightly disadvantageous.

7.5.27 The 0.5% test may be 'harsh' based on the following reasoning:

1. The EU 0.5% standard is based on solvency over a one year period;
2. My analysis deals with the risk over the run-off of all claims, over many years;
3. There is no standard adjustment from a one-year test to a multi-year test for this purpose; and
4. For a number of other regulatory purposes the FSA uses a 97.5% test for run-off business. For the same purposes they use a 99.5% for companies with run-off and new business.

7.5.28 Recognising that a 0.5% better or worse test may be harsh, I show the analysis at the 0.5% level but it should be recognised that a change greater than 0.5% does not necessarily indicate that the change is significantly disadvantageous to Policyholders.

7.5.29 With respect to the EPD standard, I note the following points:

1. EPD tests are very sensitive to extreme events;
2. Partly for that reason, they are not used for regulation of solvency;
3. In order to prevent undue weight being given to extreme events it is helpful to examine the EPD tests excluding the more extreme events; and
4. Using the EU 0.5% test, is one reasonable standard.

Relative Weights to Various Measures and Assumption Sets

7.5.30 There are three further related issues to consider:

1. The relative weight to frequency measure versus EPD measures;
2. The threshold for testing significance; and
3. The liability assumptions.

Frequency Measures vs. EPD

7.5.31 Frequency measures are more commonly used for financial assessment than EPD measures.

7.5.32 For example, value at risk, a common financial tool, is a frequency measure in the sense that I use in this Report.

7.5.33 Solvency regulation is more commonly based on the frequency of adverse events, rather than the size of those events.

7.5.34 Therefore, I give more weight to the frequency outcomes than the EPD outcomes.

7.5.35 The EPD and truncated EPD tests are more reliable as confirmation of the results of the other tests than they are as tests on their own.

Threshold

7.5.36 As described in paragraph 7.5.27 -7.5.29, I consider the 0.5% to be the minimum level for assessing whether the change as a result of the Transfer is significant.

Liability Assumptions.

7.5.37 My analysis of the Transfer considers a range of liability assumptions. Some are more favourable than the base assumptions, some are less favourable.

7.5.38 In this section I discuss the implications of the base, high variability, high mean and high mean/high variability assumptions. Each of those assumptions shows the Transfer to be progressively less favourable to the Policyholders.

7.5.39 In many contexts it is prudent (helpful to the Policyholder) to consider the worst case assumptions. In this Transfer, it is not that simple.

7.5.40 The Policyholders have the opportunity to exchange the uncertainty of partial recovery from Names for claims above "$13.1bn"[87] for the certainty[88] of full payment of claims up to "$14.4bn".

7.5.41 Thus using unduly prudent assumptions does not benefit Policyholders.

7.5.42 Therefore, each estimate should be positioned as realistic, rather than cautious.

7.5.43 I believe the base assumptions are realistic. I believe the high mean and high variability assumptions provide a reasonable range for testing the effect of the Transfer, although with increasing prudence.

7.5.44 I show the result of using the high mean and high variability assumptions to test the robustness of the analysis. However, assessing the Transfer based on a combination of the high mean and high variability assumption sets regarding liabilities, the 0.5% threshold for measuring materially disadvantaged; and relying on EPD measures rather than frequency measures is not realistic.

Recovery Rate from Names.

7.5.45 As discussed in Appendix XI, the Recovery Rates from Names under the high mean/high variability assumption sets differ from the Recovery Rates from Names under the base assumption set for reasons including the following:

1. Fewer claims are below the minimum claim threshold, which increases the Recovery Rate from Names;

[87] "$13.1bn" and "$14.4bn" are short-hand defined in footnote 73 on page 124.

[88] Subject to NICO meeting its obligations under the contract.

2. Insolvencies occur on average earlier under the high liability assumption sets. Earlier insolvencies are less affected by the Mortality of Names, so this increases the Recovery Rate from Names.

7.5.46 Table 7-9 below shows the Recovery Rate from Names for each liability assumption set, and each type of Name.

Table 7-9
Recovery Rate from Names (Total)

	Type of Name				
Liability Assumption	**Open Year**	**Original Year**	**RITC Chain**	**Open Year Long DIR**	**Original Year Long DIR**
Base	25%	12%	23%	15%	7%
High Variability	29%	14%	27%	18%	8%
High Mean	28%	14%	26%	18%	9%
High/High	31%	16%	29%	20%	10%

Source: Table 21-13 Part G.

Conclusion on the Effect of the Transfer on All Policyholders Combined

7.5.47 I believe that the Transfer is beneficial for all Policyholders combined for the following reasons:

1. Based on the frequency measures the Policyholders are better off in the event of the Transfer, for all liability assumptions, for Recovery Rates from Names of up to a level in excess of 50%;

2. The EPD test, for all liability assumptions, is favourable up to Recovery Rates from Names of 30% which indicates the Transfer is advantageous for Policyholders on Original Year Syndicates; and

3. The truncated EPD test is favourable for Recovery Rates from Names of up to nearly 40%, which indicates that Policyholders with only Open Year Names are not materially disadvantaged, for all assumptions sets, other than the highest assumption set.

7.5.48 Based on giving a higher weight to the frequency measures than the severity measure (paragraphs 7.5.31-7.5.34), I believe that,

3. Policyholders gain from the Transfer with respect to the portion of their Policies underwritten by Original Year Names; and

4. Policyholders are likely to gain from the Transfer with respect to the portion of their Policies underwritten by Open Year Names, but in any case they are clearly not materially disadvantaged with respect to the portion of their Policies underwritten by Open Year Names.

7.6 Evaluating the Effect of the Transfer on Average Direct and Average Reinsurance Policyholders Separately

7.6.1 Table 7-10 shows key statistics for evaluating the Transfer for the average direct and the average reinsurance Policyholder using a range of liability assumptions and Recovery Rates from Names.

Table 7-10
Sensitivity Tests for Average Direct and Average Reinsurance Policyholders

		Average Direct Policyholder				Average Reinsurance Policyholder		
Liability Assumption	Recovery Rate from Names	Prob. being paid in full (change) (1)	% scenarios better off less % worse off (2)	EPD (change) (3)	Truncated EPD (change) (4)	% scenarios better off less % worse off (5)	EPD (change) (6)	Truncated EPD (change) (7)
Base Variability, Mean = 100% Reserves	0%	1.50%	4.50%	0.30%		4.50%	0.30%	
	10%	1.50%	4.40%	0.20%		4.40%	0.20%	
	20%	1.50%	3.60%	0.10%	0.20%	3.60%	0.10%	0.10%
	30%	1.50%	2.80%	0.00%	0.10%	2.70%	0.00%	0.10%
	40%	1.50%	1.60%	**-0.10%**	0.00%	1.50%	**-0.10%**	0.00%
	50%	1.50%	0.80%	**-0.20%**	**0.00%**	0.50%	**-0.10%**	**0.00%**
	75%	1.50%	**-0.70%**	**-0.40%**		**-1.00%**	**-0.40%**	
Higher Variability, Mean = 100% Reserves	0%	1.70%	5.90%	0.50%		5.90%	0.40%	
	10%	1.70%	5.60%	0.30%		5.60%	0.30%	
	20%	1.70%	4.40%	0.10%	0.20%	4.30%	0.10%	0.20%
	30%	1.70%	2.70%	**0.00%**	0.10%	2.50%	**0.00%**	0.10%
	40%	1.70%	1.30%	**-0.20%**	**0.00%**	1.00%	**-0.20%**	**0.00%**
	50%	1.70%	0.50%	**-0.30%**	**-0.10%**	0.00%	**-0.30%**	**-0.10%**
	75%	1.70%	**-1.40%**	**-0.80%**		**-1.90%**	**-0.70%**	
Base Variability, Mean = 120% Reserves	0%	3.30%	10.80%	0.70%		10.80%	0.60%	
	10%	3.30%	10.50%	0.50%		10.50%	0.40%	
	20%	3.30%	8.50%	0.30%	0.30%	8.30%	0.20%	0.30%
	30%	3.30%	5.80%	0.10%	0.20%	5.50%	0.00%	0.10%
	40%	3.30%	3.60%	**-0.20%**	**0.00%**	3.00%	**-0.20%**	**-0.10%**
	50%	3.30%	1.70%	**-0.40%**	**-0.20%**	1.00%	**-0.40%**	**-0.20%**
	75%	3.30%	**-1.90%**	**-1.00%**		**-2.90%**	**-0.90%**	
Higher Variability, Mean = 120% Reserves	0%	3.50%	12.30%	0.90%		12.30%	0.80%	
	10%	3.50%	12.00%	0.60%		11.90%	0.50%	
	20%	3.50%	8.80%	0.30%	0.30%	8.70%	0.20%	0.30%
	30%	3.50%	5.60%	**-0.10%**	0.10%	5.30%	**-0.10%**	0.00%
	40%	3.50%	3.00%	**-0.40%**	**-0.20%**	2.30%	**-0.40%**	**-0.20%**
	50%	3.50%	0.70%	**-0.70%**	**-0.40%**	**-0.10%**	**-0.70%**	**-0.40%**
	75%	3.50%	**-3.20%**	**-1.60%**		**-4.20%**	**-1.50%**	

Note: Bold indicate values less than zero.

7.6.2 For direct Policyholders the position is slightly more favourable than for all Policyholders. Therefore my conclusion with regard to direct Policyholders is as I described it above, in section 7.5, for all Policyholders combined.

7.6.3 For reinsurance Policyholders the position is similar. In particular:

1. Based on the frequency measures the direct and reinsurance Policyholders are better off in the event of the Transfer for all liability assumptions for Recovery Rates from Names up to 40%;
2. Moreover, Policyholders are better off in the event of a Transfer for Recovery Rates from Names up to 50 % for all but the highest liability assumptions sets, where it is slightly unfavourable (under 0.5%);
3. The EPD test is favourable up to Recovery Rates from Names of up to 30% for all liability assumptions, and up to 20% for the high mean / high variability assumption set; and
4. The truncated EPD result is favourable up to Recovery Rates from Names of 50% for the base liability assumptions, and up 40% Recovery Rates from Names for the high variability liability assumptions, up to 35% for the high mean assumption and up to 30% for the high mean/high variability assumption set.

7.6.4 Based on giving a higher weight to the frequency measures than the severity measures (paragraphs 7.5.31-7.5.34), I believe that

1. Policyholders gain from the Transfer with respect to the portion of their Policies underwritten by Original Year Names; and
2. I believe that Policyholders are likely to gain from the Transfer with respect to the portion of their Policies underwritten by Open Year Names, but in any case they are not materially disadvantaged with respect to the portion of their Policies underwritten by Open Year Names.

Summary of Frequency Statistics

7.6.5 Figure 7-11 and Figure 7-12 below summarise the frequency statistics shown in Table 7-10 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open and Original Year Names.

Figure 7-11
Average Direct Policyholders
% Scenarios Better Off Less % Worse Off

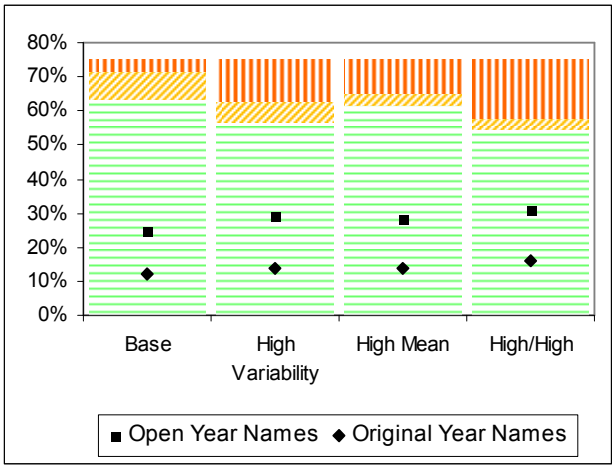
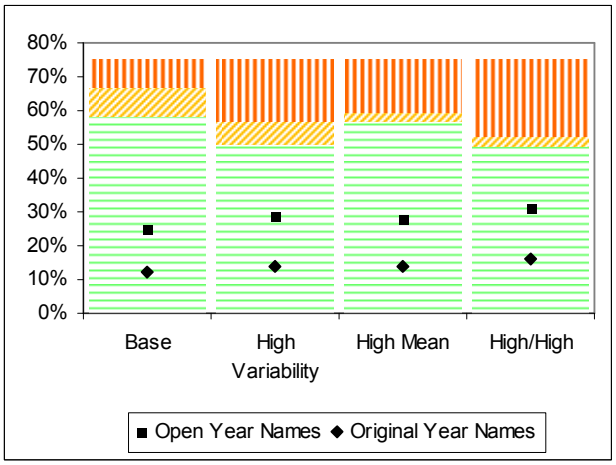


Figure 7-12
Average Reinsurance Policyholders
% Scenarios Better Off Less % Worse Off



7.6.6 The areas of Figure 7-11 and Figure 7-12 with green horizontal lines corresponds to the level of Recovery Rates from Names for which Policyholders are better off in the event of the Transfer more often than they are worse off in the event of the Transfer.

7.6.7 The areas with light orange diagonal lines corresponds to the level of Recovery Rates from Names for which Policyholders are worse off in the event of the Transfer in fewer than 0.5% of scenarios.

7.6.8 The areas with dark orange vertical lines corresponds to the level of Recovery Rates from Names for which Policyholders are worse off in the event of the Transfer in more than 0.5% of scenarios.

7.6.9 The boundaries of the shaded areas were calculated by interpolation using the values in Table 7-10.

7.6.10 The square marks correspond to the expected recovery from Names for Open Year Names.

7.6.11 The diamond marks correspond to the expected recovery from Names for Original Year Names.

7.6.12 These figures show that average direct and average reinsurance Policyholders are better off in the event of the Transfer based on the frequency measure, for all liability assumption sets.

Summary of Severity Statistics

7.6.13 The following figures summarise the severity statistics shown in Table 7-10 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open Year Names and Original Year Names.

Figure 7-13
Average Direct Policyholders
EPD Measures

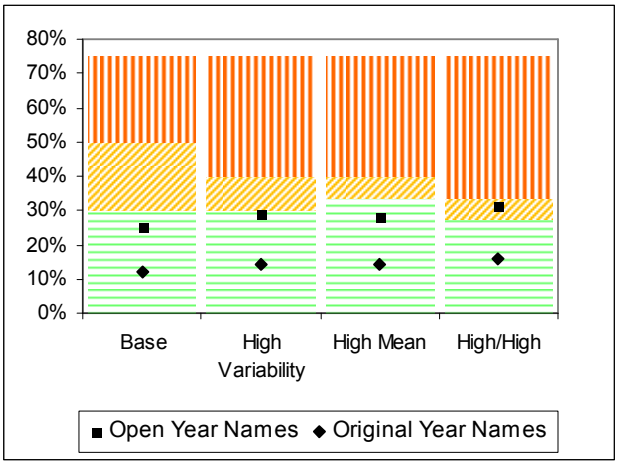
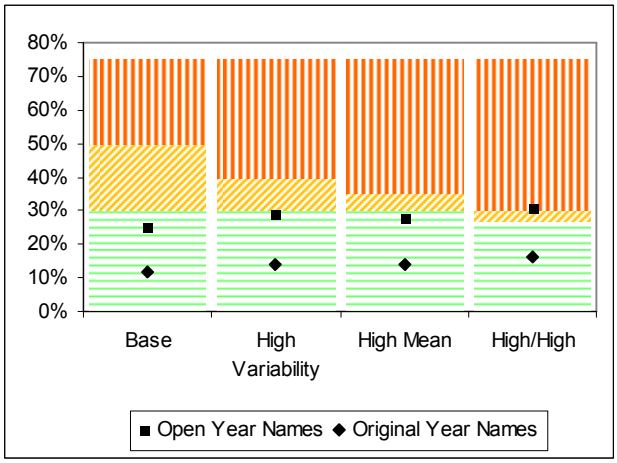


Figure 7-14
Average Reinsurance Policyholders
EPD Measures



7.6.14 The areas of Figure 7-13 and Figure 7-14 with green horizontal lines corresponds to the level of Recovery Rates from Names for which the EPD is lower in the event of the Transfer than in the current structure.

7.6.15 The areas with light orange diagonal lines corresponds to the level of Recovery Rates from Names for which the truncated EPD is lower in the event of the Transfer than in the current structure.

7.6.16 The areas with dark orange vertical lines corresponds to the level of Recovery Rates from Names for which the truncated EPD is higher in the event of the Transfer than in the current structure.

7.6.17 The square and diamond marks have the same meaning as in Figure 7-11and Figure 7-12.

7.6.18 These figures show that average direct and average reinsurance Policyholders are better off in the event of the Transfer based on the severity measure, for all liability assumptions except for the high mean/high variability assumption set, for Open Names.

7.6.19 For the high mean/high variability assumption set average direct Policyholders of Open Names have a slightly higher EPD in the event of the Transfer, but have a lower truncated EPD. Average reinsurance Policyholders have a slightly higher truncated EPD in the event of the Transfer.

7.7 Evaluating the Effect of the Transfer on Long Duration Reinsurance Policyholders

7.7.1 Longer duration Policyholders are potentially disadvantaged compared to shorter duration Policyholders because the long duration Policyholders have a longer period of exposure to a possible Equitas Insolvency than shorter duration Policyholders.

7.7.2 Equitas selected a 'worst case' example by examining the situation for a reinsurance Policyholder who will make no claim until ten years after the starting date for this projection (in excess of 25 years from when the Policy was written for the most recent such Policy).

7.7.3 Based on my experience, I agree that this would be an extreme situation.

7.7.4 Table 7-15 shows the key statistics for evaluating the Transfer for average long duration reinsurance Policyholders.

Table 7-15
Sensitivity Tests for Long Duration Reinsurance Policyholders

		Long (from yr 10) IRI ph		
Liability Assumption	Recovery Rate from Names	% scenarios better off less % worse off (1)	EPD (change) (2)	Truncated EPD (change) (3)
Base Variability, Mean = 100% Reserves	0%	4.4%	0.6%	
	10%	3.9%	0.4%	
	20%	3.1%	0.2%	0.3%
	30%	2.1%	**0.0%**	0.1%
	40%	1.2%	**-0.2%**	0.0%
	50%	0.2%	**-0.5%**	**-0.1%**
	75%	**-1.1%**	**-1.0%**	
Higher Variability, Mean = 100% Reserves	0%	5.7%	0.8%	
	10%	4.8%	0.5%	
	20%	3.4%	0.1%	0.3%
	30%	1.8%	**-0.2%**	0.1%
	40%	0.6%	**-0.6%**	**-0.2%**
	50%	**-0.3%**	**-0.9%**	**-0.4%**
	75%	**-2.0%**	**-1.8%**	
Base Variability, Mean = 120% Reserves	0%	10.1%	1.0%	
	10%	8.9%	0.6%	
	20%	6.2%	0.2%	0.3%
	30%	3.7%	**-0.2%**	0.0%
	40%	1.7%	**-0.7%**	**-0.3%**
	50%	**-0.1%**	**-1.1%**	**-0.7%**
	75%	**-3.2%**	**-2.2%**	
Higher Variability, Mean = 120% Reserves	0%	11.4%	1.2%	
	10%	9.5%	0.6%	
	20%	6.1%	**0.0%**	0.2%
	30%	3.3%	**-0.6%**	**-0.2%**
	40%	0.7%	**-1.2%**	**-0.7%**
	50%	**-1.3%**	**-1.8%**	**-1.2%**
	75%	**-4.5%**	**-3.4%**	

7.7.5 Table 7-15 shows that:

1. Based on the frequency measures, the long duration reinsurance Policyholders are better off in the event of the Transfer for all liability assumption sets, for Recovery Rates from Names of up to at least 40%;

2. Moreover, for Recovery Rates from Names up to 50%, Policyholders are disadvantaged in less than 0.5% of scenarios except the higher mean / higher variability liability assumption set;

3. The EPD test, for all liability assumption sets, is favourable for Recovery Rates from Names of up to 20%; and

4. The truncated EPD test is favourable for Recovery Rates from Names of up to 40% for the base liability assumption set, and up to 30% for the high variability and high mean liability assumption set, and up to 20% for the high mean / high variability assumption set.

7.7.6 Based on giving a higher weight to the frequency measures than the severity measure (paragraphs 7.5.31-7.5.34), I believe:

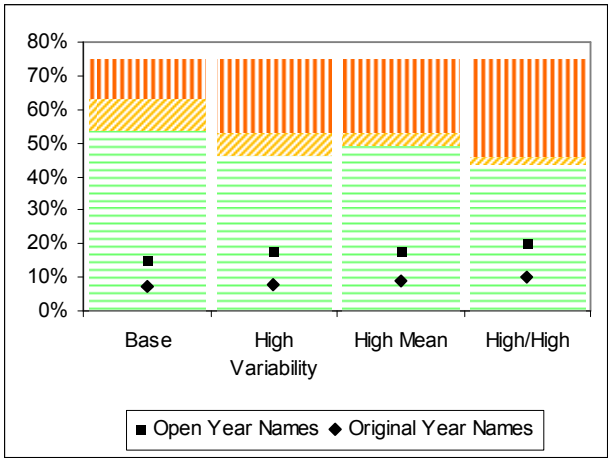
1. Policyholders are likely to gain from the Transfer with respect to the portion of their Policies underwritten by Original Year Names, but in any case they are clearly not materially disadvantaged with respect to the portion of their Policies underwritten by Original Year Names; and

2. Policyholders are not materially disadvantaged with respect to their Policies with Open Year Names.

Summary of Frequency Statistics

7.7.7 Figure 7-16 below summarises the frequency statistics shown in Table 7-15 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open and Original Year Names.

Figure 7-16
Long Duration Reinsurance Policyholders
% Scenarios Better off less % Worse Off



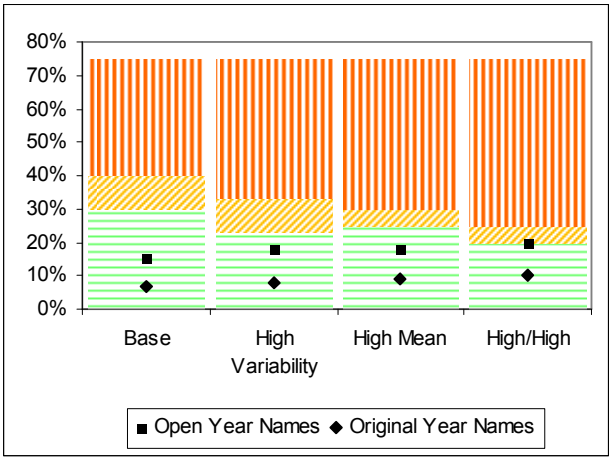
7.7.8 This figure uses the same conventions as in Figure 7-11 and Figure 7-12,.

7.7.9 This figure shows that long duration reinsurance Policyholders are better off in the event of the Transfer based on the frequency measure, for all liability assumption sets.

Summary of Severity Statistics

7.7.10 The following figure summarises the severity statistics shown in Table 7-15 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open and Original Year Names.

Figure 7-17
Long Duration Reinsurance Policyholders
EPD Measures



7.7.11 This figure uses the same conventions as in Figure 7-13 and Figure 7-14.

7.7.12 This figure shows that long duration reinsurance Policyholders are better off in the event of the Transfer based on the severity measure, for all liability assumption sets.

7.8 Evaluating the Effect of the Transfer on Long Duration Direct Policyholders

7.8.1 In this section I consider the implications of the Transfer from four perspectives as follows:

1. Claimants (in the case of UK Employers' Liability Policies for example);
2. Policyholders; and
3. Insurers other than Names (with respect to UK Mesothelioma Claims).

7.8.2 Table 7-18 shows the key statistics for evaluating the situation for the individual mesothelioma claimant, making a claim under The 1930's Act, whose claims are paid in 50.

7.8.3 This is most extreme example of a long duration Policy.

Table 7-18
Sensitivity Test for Long Duration Direct Policyholders

		Long (yr 50) DIR ph		
Liability Assumption	**Recovery Rate from Names**	**% scenarios better off less % worse off (1)**	**EPD (change) (2)**	**Truncated EPD (change) (3)**
Base Variability, Mean = 100% Reserves	0%	4.0%	1.0%	
	10%	3.3%	0.4%	
	20%	2.5%	**-0.2%**	0.5%
	30%	1.6%	**-0.8%**	0.3%
	40%	0.8%	**-1.4%**	0.0%
	50%	0.1%	**-2.0%**	**-0.2%**
	75%	**-0.8%**	**-3.5%**	
Higher Variability, Mean = 100% Reserves	0%	5.2%	1.4%	
	10%	4.3%	0.5%	
	20%	2.8%	**-0.4%**	0.6%
	30%	1.4%	**-1.3%**	0.2%
	40%	0.4%	**-2.2%**	**-0.2%**
	50%	**-0.4%**	**-3.1%**	**-0.6%**
	75%	**-1.7%**	**-5.4%**	
Base Variability, Mean = 120% Reserves	0%	9.5%	1.5%	
	10%	8.2%	0.6%	
	20%	5.6%	**-0.3%**	0.5%
	30%	3.1%	**-1.2%**	0.0%
	40%	1.2%	**-2.1%**	**-0.5%**
	50%	**-0.2%**	**-3.0%**	**-1.0%**
	75%	**-2.5%**	**-5.3%**	
Higher Variability, Mean = 120% Reserves	0%	10.6%	1.6%	
	10%	8.8%	0.3%	
	20%	5.4%	**-0.9%**	0.4%
	30%	2.8%	**-2.2%**	**-0.3%**
	40%	0.7%	**-3.4%**	**-1.0%**
	50%	**-1.0%**	**-4.7%**	**-1.7%**
	75%	**-3.8%**	**-7.8%**	

7.8.4 Long duration direct Policies of the type discussed in this section are likely to have been written by Original Year Names, other than Open Year Names in that UK Employers Liability Policies with Asbestos exposure relate primarily to the 1970's and in any case only rarely extend later than the mid-1980's.

7.8.5 Thus, it is reasonable to assess the long duration direct Policies with respect to Original Year Policies only. Nonetheless, I show the results for Open Year Policies as well.

7.8.6 These assessment statistics show the following:

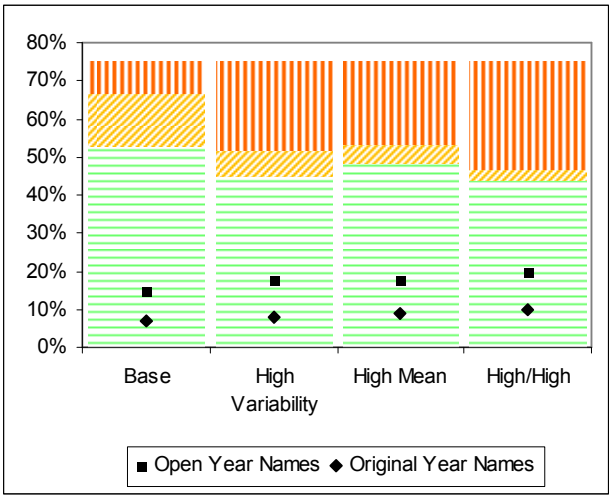
1. Based on the frequency measures the long duration direct Policyholders (claimants in this case) are better off in the event of the Transfer for all liability assumptions for Recovery Rates from Names in up to around 40% of the scenarios in the model;
2. The EPD test, for all liability assumptions, is favourable up to Recovery Rates from Names of 10%;
3. The truncated EPD is favourable:
   a. Up to around 40% Recovery Rates from Names for the base liability assumptions and the high variability liability assumption set;
   b. Up to 30% for the high variability liability assumption set; and
   c. Up to 20% for the high mean and the high mean / high variability assumption sets.
4. Based on the weights described above, I believe that:
   a. Policyholders may gain from the Transfer with respect to the portion of their Policies underwritten by Original Year Names; and
   b. In any case they are clearly not materially disadvantaged with respect to the portion of their Policies underwritten by Open Year Names.

7.8.7 Overall, I believe that these claimants gain from the Transfer with respect to their Policies, and in any case they are not materially disadvantaged with respect to the portion of their Policies underwritten by Original Year Names.

Summary of Frequency Statistics

7.8.8 Figure 7-19 below summarises the frequency statistics shown in Table 7-18 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open and Original Year Names.

Figure 7-19
Long Duration Direct Policyholders
% Scenarios Better Off Less % Worse Off



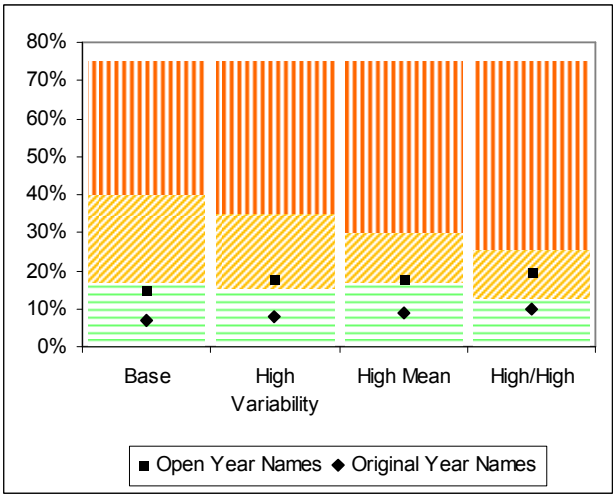
7.8.9 This figure uses the same conventions as in Figure 7-11 and Figure 7-12.

7.8.10 This figure shows that long duration direct Policyholders are better off in the event of the Transfer based on the frequency measure, for all liability assumption sets.

Summary of Severity Statistics

7.8.11 The following figures summarise the severity statistics shown in Table 7-18 for each liability assumption set, and compares the results to the expected Recovery Rate from Names for Open and Original Year Names.

Figure 7-20
Long Duration Direct Policyholders
EPD Measures



7.8.12 This figure uses the same conventions as in Figure 7-13 and Figure 7-14.

7.8.13 This figure shows that in each liability assumption set long duration direct Policyholders of Open Year Names have a lower truncated EPD in the event of the Transfer than in the current structure, and a lower EPD in respect of Policies of Original Year Names.

7.8.14 In addition, I observe that these claimants, might have lower recovery expectations than anticipated in section 5. For example:

1. An early insolvency might be resolved by a global settlement that did not include enough funds for these late-paying and possibly late emerging claims; and
2. Any mechanism to pre-fund liabilities by collecting funds from Names at the date of insolvency might not be fully successful. If so, the long duration Policyholders have the greater risk of not being paid so that funds might not be adequate for these late paying and late emerging claims.

Insurers and Policyholders

7.8.15 Policyholders and insurers have the benefit of Equitas cover largely over long periods of time, even if some claims are paid only at the end.

7.8.16 Hence, in part, the position of these parties is largely the same as the position of the Direct Policyholder that was analyzed in section 7.6. In that case I have shown that the parties are not materially disadvantaged in the event of the Transfer.

7.8.17 To the extent that the longer duration of claims from these parties affects the way the Transfer affects them, then the analysis of long duration direct Policies above, shows that from that perspective they are also not materially disadvantaged in the event of the Transfer.

8.1.1 Policyholders of Names reinsured by Equitas strongly rely on NICO's ability to pay claims with respect to the NICO Retrocession Agreement, regardless of whether the Transfer is approved, and with respect to the proposed increase in the NICO Retrocession Agreement if the Transfer is approved.

Financial Rating

8.1.2 NICO has an Insurer Financial Strength rating of A++ by AM Best, Aaa by Moody's, and AAA by S & P. These are the highest ratings given by those rating agencies.

8.1.3 NICO is one of the few property & casualty insurers with the above ratings. For Moody's, as of August 2008, Berkshire Hathaway's NICO and General Re Group are the only two reinsurers with an Exceptional rating (Aaa).

8.1.4 The rating agencies attribute NICO's high ratings to the company's extremely strong capitalisation, strong competitive position and strong financial flexibility/liquidity.

8.1.5 NICO's ability to generate a substantial amount of 'float' (e.g., the assets that can be used for investment purposes) is key to their financial strength and is based on their large capital base and their ability to generate strong investment returns with their buy and hold investment strategy.

8.1.6 On 13 March 2009, Fitch reduced Berkshire Hathaway's rating from AAA to AA+. Fitch did not change NICO's Insurer Financial Strength (IFS) rating which remains AAA.

8.1.7 On 25 March 2009, S&P affirmed Berkshire Hathaway's AAA rating but downgraded its outlook from stable to negative. S&P did not change NICO's IFS rating which remains AAA.

Other Tests of Financial Condition

8.1.8 It is beyond the scope of this Report to fully analyse the financial condition of NICO. However, I have examined publicly available information regarding NICO to determine whether there are indications that the above financial ratings are not appropriate.

8.1.9 Table 8-1 through Table 8-3 at the end of this section shows a number of favourable financial ratios, consistent with the high financial ratings noted above.

8.1.10 The tables also indicate a number of risk factors:

1. NICO assets include a high proportion of equities, 169% of surplus compared to 62% on average for US insurers and reinsurers at December 2007 and 186% compared to 63% on average for US insurers and reinsurers at September 2008 (Table 8-1 and Table 8-2);

2. NICO's decrease in surplus from $35.6bn to $33.6bn between December 2007 and September 2008 was likely driven by unrealized investment losses (Table 8-3); and
3. NICO has a high proportion of Asbestos liabilities, from transactions similar to this transfer (Table 8-1).

8.1.11 Also, two non-financial risk factors are apparent from the general press:

1. Berkshire Hathaway is a large group, and group risks from outside NICO might adversely affect NICO; and
2. Warren Buffet is seen to be central to Berkshire Hathaway. Thus, regardless of the depth of the management team, there may be a key man risk.

Additional Policyholder Protection Related to the Transfer

8.1.12 For the Transfer, from the affected Policyholders' perspective, the security associated with NICO's financial position is enhanced. The NICO Retrocession Agreement provides that in the event that NICO ceases to have an IFS rating published by S&P of AA- or higher (provided that it does not have an IFS rating lower than A-), NICO must procure the establishment of a LOC for an amount equal to, amongst other matters, the lower of 102% of technical reserves or the remaining NICO retrocessional cover or place an equivalent amount in trust. If the IFS of NICO falls below A-, the required collateral level moves to 125% of technical reserves or the remaining NICO retrocessional cover (whichever is the lower).

8.1.13 This limits the risk of non-payment to circumstances when the LOCs or trust might not be established. Such situations might arise because:

1. NICO's financial condition declines so quickly that there is no time to purchase the LOCs or establish the Trust Funds;

   This risk might be increased because NICO has or will have other LOC obligations similar to those owed to Equitas such that NICO could not obtain the LOCs required by all of its agreements (those in place now and those put in place in the future); and
2. LOCs or Trust Funds are provided initially, but increases in the LOCs or Trust Funds, required as claims increase, are not provided for reasons such as those noted above.

8.1.14 Trust Funds provide limited protection for this layer of reinsurance, as the Trust Funds might be fully utilized in the first layer of NICO coverage.

NICO and Speyford will have Correlated Risks -Asbestos

8.1.15 The risk to Policyholders in this Transfer is heightened because NICO has a substantial amount of Asbestos and other long duration liabilities like Equitas. Events requiring large payments from NICO to Equitas might also take place at times of financial stress for NICO.

8.1.16 The risk in this regard is mitigated because NICO Policies generally have aggregate limits.

8.1.17 Moreover, on some of the larger NICO contracts, NICO recorded liabilities are generally at or near the aggregate limits.

8.1.18 NICO estimates that its maximum losses payable under retroactive policies are not expected to exceed approximately $24.8bn, due to caps on the amounts payable for each contract; 70% of this figure is reserved.[89]

8.1.19 The NICO Retrocession Agreement appears to be unusual compared with other large NICO contracts in having an aggregate limit well above the best estimate of the liability.

Equity Risk

8.1.20 Based on data through 30 September 2008, equity values would need to fall 45% before NICO premium-to-surplus ratios were equal to the industry's ratio.

8.1.21 Events triggering NICO's inability to pay claims (e.g., falling equity markets) might also affect Names' ability to pay. This reduces the relative impact of having purchased reinsurance compared to relying on any potential recovery from Names.

Risk for Policyholders is only Marginally Increased in the Event of the Transfer

8.1.22 The analysis also considers that the risk of NICO's claims paying ability has already been accepted by virtue of the original NICO Retrocession Agreement.

8.1.23 Even if NICO were in financial difficulty and could not pay all claims in full, it is likely to make partial payments.

Effect of the Transfer on NICO

8.1.24 In the event of the Transfer, NICO exposure to Asbestos and other long duration liabilities will increase.

8.1.25 I do not believe that increase will have a material affect on NICO's ability to meet its obligations to Equitas or other NICO Policyholders for reasons including the following:

1. The additional $1.3bn cover is not large compared to NICO surplus ($33.6bn at September 2008); and
2. The rating agency Insurer Financial Strength Ratings in 2008 and in March 2009 have had the opportunity to consider whether the Equitas Part VII Transfer would affect NICO's financial strength.

[89] Source: Berkshire 2007 10-K and NICO 2007 Annual Statement

Summary of Selected NICO Financial Indicators

8.1.26 The following tables summarise some key NICO financial information from the December 2007 and September 2008 NICO Audited Statutory Statements, and Key Schedules from the National Association of Insurance Commissioners (NAIC) Annual Statement.

Conclusion

8.1.27 I do not believe the change in the risk of non-payment by NICO in the event of the Transfer compared to the current structure represents a significant disadvantage to any group of Policyholders.

Table 8-1
National Indemnity Company and Industry
Key Ratios—December 2007 Annual Statement Key Schedules

Ratio	NICO Value	Industry Value***	Significance
Premium as a percentage of surplus*	12%	83%	Favourable
Surplus as a percentage of Risk Based Capital	383%	N/A	Favourable
Outward reinsurance as a percentage of surplus	3%	39%	Favourable
Exposure to Asbestos and Pollution as a percentage of reserves net of reinsurance[90]	24% **	5%	Moderately unfavourable
Equities as a percentage of surplus	169%	62%	Unfavourable

Notes: * Surplus equals "surplus as regards Policyholders" as defined in US statutory reporting.
** For the reasons described in paragraphs 8.1.15-8.1.19 this ratio is not as unfavourable as it appears.
***Source http://www.snl.com/default.aspx (SNL Financial)

[90] NICO and industry values are not quite comparable due to lack of information regarding retroactive reinsurance/write-in liabilities for the industry. Industry percentage is direct only, NICO includes retroactive reinsurance (Equitas and other contracts).

Table 8-2
National Indemnity Company and Industry
Key Ratios—Updated as of September 2008

Ratio	NICO Value	Industry Value	Significance
Premium as a percentage of surplus	14%	88%	Favourable
Surplus as a percentage of Risk Based Capital	NA	NA	
Outward reinsurance as a percentage of surplus	NA	NA	
Exposure to Asbestos and Pollution as a percentage of reserves net of reinsurance[91]	NA	NA	
Equities as a percentage of surplus	186%	63%	Unfavourable

Table 8-3
National Indemnity Company
Statutory Balance Sheet December 2007 and September 2008

Item	$ (bn) 2007	$ (bn) 2008
Assets		
Bonds	$2.3	$1.8
Common stocks (1)	36.8	39.5
Cash and equivalent	9.2	3.3
Other invested assets (2)	23.5	23.0
All other	2.4	3.8
Total	$74.2	$71.4
Liabilities		
Losses and loss adjustment expenses	$10.8	$11.8
Net retroactive reinsurance	16.9	16.0
Deferred tax	6.6	5.1
Other	4.3	4.8
Total	$38.6	$37.7
Capital and surplus	$35.6	$33.6

Notes: (1) Coke, Amex, Proctor and Gamble, Other
(2) "Harney Trust"

[91] NICO and industry values are not quite comparable due to lack of information regarding retroactive reinsurance/write-in liabilities for the industry. Industry percentage is direct only, NICO includes retroactive reinsurance (Equitas and other contracts).

Table 8-4
National Indemnity Company
December 2007 Data Used in Table 8-1 Ratios

Item	$(bn)
Premium (net of reinsurance)	$4.2
External Outwards Reinsurance asset	1.0
Risk based capital authorised controls level	9.3
Asbestos and Pollution (excluding retroactive reinsurance)	1.0
Unused limits on major retroactive contracts	N/A

9.1.1 There are two types of Trust Fund that protect Policyholders - 'stand-by' Trust Funds and 'operating Trust Funds. Most Trust Funds are 'stand-by' Trust Funds, where a LOC is established based on an estimate of the outstanding claims covered by the relevant Trust Fund at the start of each year.

9.1.2 The EATF is an 'operating' Trust Fund, where Trust Fund assets are used to pay claims as they arise.

9.1.3 Equitas has Policyholder Trust Funds in the USA, Canada, Australia and South Africa.

9.1.4 The EATF, which covers liabilities on all Policies with premium or limits denominated in USD, is by far the largest Trust Fund.

9.1.5 These Trust Funds are not required under the contracts between the Policyholders and the Names. They are a regulatory requirement for Lloyd's to be able to carry out business in the relevant countries. The rules can, and have been, modified in the past, and may be modified in the future. As a long term trend, I note that the regulation of insurance is moving towards the elimination of Trust Fund mechanisms.

9.1.6 The purpose of the analysis in this section is to assess whether Policyholders without access to the Trust Funds are disadvantaged in the event of the Transfer compared to their position under the current structure.

9.1.7 The analysis in this section differs from the analysis in section 4.10, where I evaluated whether Policyholders with access to Trust Funds are disadvantaged in the event of the Transfer compared to their position under the current structure.

EATF

9.1.8 The EATF covers liabilities on all Policies with premium or limits denominated in USD (USD Policies). It works in conjunction with the LATF[92].

9.1.9 Subtractions from Trust Fund assets arise from expenditures for the following purposes:

1. The EATF is used to pay ERL's reinsurance obligations in respect of USD Policies;
2. In connection with litigation by a Policyholder of a Name; to secure and or pay the obligations of ERL, EL or NICO; and
3. To secure Letters of Credit.

9.1.10 Additions to EATF assets arise from investment income, and any reinsurance funds assigned or transferred from NICO or ERL/EL. Neither NICO nor EL is

[92] Sometimes called NATF (for NICO American Trust Fund)

required to top up the EATF, even if the EATF assets are exhausted (subject to paragraph 9.1.15).

9.1.11 If the amount held in the Trust Fund exceed 102% of the amount certified by RMSL as the amount required to fund the entire US obligations, the balance may be paid to NICO (with the consent of the NYID). The consent of the NYID is not required for such balance payments to NICO if the amount held in the Trust Fund exceeds 137.5% of the amount certified by RMSL as the amount required to fund the entire US obligations.

9.1.12 In Appendix XII, I discuss the two circumstances when the EATF becomes relevant to the analysis of the Transfer. These are in the case of an Equitas Insolvency or a NICO Insolvency.

9.1.13 In each of the scenarios given in Appendix XII, the EATF shares in the case of an Equitas Insolvency is under 40% of USD liabilities and generally under 35%. Those ratios are less than the dividend ratios to 'all Policies' in even the most extreme insolvencies. This means that in each of these scenarios, all Policyholders (including USD Policyholders) are paid the same 'all Policyholders' dividend.

9.1.14 Thus, in these Equitas Insolvency scenarios the USD Policyholders are not in a better position than non-USD Policyholders due to the EATF.

9.1.15 In the event of a NICO downgrade or material default triggering the LOC or trust provisions described in paragraph 8.1.12, NICO and Equitas have agreed that the benefit of the LOC will be applied to the EATF to the extent of the EATF pro-rata share of the discounted remaining limits of the NICO Retrocession.

9.1.16 In Appendix XII, I give examples of the effect of a NICO Insolvency (in the absence of a LOC) on Policyholders. In each of the examples in Appendix XII, the 'all Policyholder' dividend rate exceeds the EATF share.

9.1.17 Therefore, I conclude that the operation of the EATF arrangements does not materially disadvantage any group of Policyholders, including Policyholders not protected by the EATF.

Other Trust Funds

9.1.18 The Trust Funds in Canada, Australia and South Africa are 'stand-by' Trust Funds.

9.1.19 For the Australian Trust Funds, a LOC is established based on an estimate of the outstanding claims covered by the relevant Trust Fund at the start of each year. The Canadian and South African Trust Funds hold other assets.

9.1.20 The following table shows the size of these Trust Funds at 31 December 2008.

Table 9-1
Other Trust Funds

Trust Fund	Size
Australia	Aus$150m at December 2008 (Aus$155m at December 2007)
Canada	Can$34m at December 2008 (Can$35m at December 2007)
South Africa	14.5m ZAR – Funded by Lloyd's

9.1.21 If the estimate of outstanding claims for these Policyholders is equal to the actual ultimate claims, then these Policyholders will be paid 100% of the value of their claims in the event of an Equitas Insolvency (It is expected, however that no Policyholder would receive less than the percentage of Policyholder claim that would have been paid in the absence of the Trust Fund).

9.1.22 If the estimate of outstanding claims for these Policyholders is less than the actual ultimate claims, then these Policyholders will be paid less than 100% of the value of their claims in the event of an Equitas Insolvency.

9.1.23 If assets are ultimately insufficient to cover claims on Policies not protected by these Trust Funds, for example UK Policyholders, this will reduce the dividend payment available to these Policyholders.

9.1.24 However, the same Trust Fund rules apply in the current structure and in the event of the Transfer.

9.1.25 These 'stand-by' Trust Funds are intended to have sufficient Funds to pay valid claims in full.

9.1.26 Accordingly, Policyholders in other jurisdictions have the benefit of the $1.3bn additional NICO coverage in exchange for no longer having the right to seek recovery for shortfalls from Names.

9.1.27 I have shown that $1.3bn of additional NICO coverage is more advantageous to Policyholders than the right to seek recovery from Names. That finding applies to the set of Policyholders who do not have the benefit of trust fund protection, in the expected event that those Policyholders (those who do not have the benefit of trust fund protection) have first use of the additional $1.3bn.

9.1.28 Therefore, I conclude that the operation of the Canada, Australia and South Africa Trust Fund arrangements do not materially disadvantage any group of Policyholders, including Policyholders not protected by the EATF, or any other stakeholders.

10 CONCLUSIONS

10.1.1 I have considered the Transfer and its likely effect on Policyholders of 1992 and Prior Business written at Lloyd's which is reinsured by ERL.

10.1.2 I have analysed the likely effect of replacing the current structure, including the current security offered by the NICO Retrocession Agreement and the unlimited liability of Names with the limited liability of Speyford plus an additional $1.3bn of coverage under the NICO Retrocession Agreement.

10.1.3 I have analysed the other changes in the structure associated with the Transfer.

10.1.4 I have examined the position of all Policyholders combined, and I have considered the position of each relevant Policyholder group separately.

10.1.5 I have also examined the likely effect on the other parties identified in Table 2-4.

10.1.6 I will provide a Supplemental Report addressing the effect, if any, on the FSCS in the event of a Transfer and the result of my review of the material identified in Appendix XIV.

10.1.7 Subject to the findings in that Supplemental Report, and any other Supplemental Reports, I have concluded that there are no groups of Policyholders, or other parties, listed in Table 2-4, that are materially disadvantaged in the event of the Transfer.

11 APPENDIX I - INDEPENDENT EXPERT – SCOPE OF WORK

Scope of Work of the Independent Expert

1. Allan Kaufman (the 'Independent Expert') is appointed to review the terms of the Transfer and produce a Report on the Transfer ('Report') and a supplementary report should one be required.

2. The preparation of the Report and its contents shall comply with the requirements set out in the relevant rules of the court, Civil Procedures Rules Part 35, the relevant applicable Practice Direction and the Protocol for the Instruction of Experts to give Evidence in Civil Claims.

3. The Report shall also comply with the guidance in paragraphs SUP 18.2.31G to 18.2.41G inclusive of the FSA Handbook (or any provisions replacing or updating these) and appropriate professional guidance notes.

4. The Report shall include a summary of the Independent Expert's professional qualifications and experience.

5. The Report shall comment on the likely effects of the Transfer on all categories of Policyholders and reinsurers of the 1992 and prior years non-life Lloyd's business and on any other persons as may be appropriate.

6. For the avoidance of doubt, the Report (and the summary required by paragraph 3(4) of the Financial Services and Markets Act 2000 (Control of Business Transfers) (Requirements on Applicants) Regulations 2001 (the 'Transfer Regulations')) will be available:

   (a) to the FSA for it to approve pursuant to section 109 of the Financial Services and Markets Act 2000 and SUP 18; and

   (b) to Equitas/RMSL in sufficient time to make suitable arrangements for the Report and summary being made available (with other items) to Policyholders, reinsurers and others pursuant to the Transfer Regulations.

7. The Independent Expert will contact the FSA (pursuant to paragraph SUP 18.2.32G of the FSA Handbook), in order to establish whether there are any additional matters relating to the Transfer or the parties to the Transfer to which the FSA wishes to draw the Independent Expert's attention and whether there are particular issues that the FSA wishes the Independent Expert to address in the Report.

8. In the first instance the Independent Expert will prepare a draft Report for circulation to Equitas and its advisers for discussion and review. There is no obligation to reflect the comments of Equitas and its advisers in the Report

except to the extent that such comments relate to any factual inaccuracies, errors and/or omissions.

9. Throughout the period of engagement, the Independent Expert will use all reasonable endeavours to make himself available to the FSA who may wish to discuss various aspects of the Transfer. Equitas will make copies of the draft Report available to the FSA. The FSA and the High Court will be provided with a final version of the Report signed by the Independent Expert.

10. Pursuant to paragraph 3 of the Transfer Regulations notices and statements will be sent by or on behalf of Equitas to Policyholders, reinsurers and others as part of the Transfer process and the Independent Expert is required to produce brief summaries of the Report to be included in the statement. The Report and statement will be made available by or on behalf of Equitas free of charge to any person who requests them and may be published on the Equitas website.

11. The Independent Expert will be required, after consultation with Equitas, to comment on and respond to any reasonable enquiries raised by Policyholders, reinsurers and other interested parties in relation to the Report and review and respond to, or assist with the response to, any complaints or objections that are made in respect of the Transfer.

12. The Independent Expert is required to attend the hearings in the High Court concerning the Transfer and to be available to provide such evidence as the High Court may require in respect of the Report.

Allan Kaufman FCAS, MAAA FIA (Hon), CPCU

ALLAN KAUFMAN
Managing Director

Navigant Consulting
Centurion House
24 Monument Street
London EC3R 8AJ
United Kingdom

Tel: +44 (0)20 7469 1111
Fax: +44 (0)20 7469 1112

allan.kaufman@navigantconsulting.com

Education

Brooklyn College
B.S. in Mathematics and Physics (1968)
University of Wisconsin
M.S. in Physics (1969)

Professional Designations

Fellow of the Casualty Actuarial Society (FCAS)
Member of the American Academy of Actuaries (MAAA)
Honorary Fellow of the Institute of Actuaries (FIA, Hon)
Chartered Property and Casualty Underwriter (CPCU)
Associate in Risk Management (ARM)

Publications

Papers published in the CAS Forum (2000, 1992, 1990, 1982 and 1980)

Allan Kaufman is a Managing Director in Navigant Consulting in the Insurance and Reinsurance group in London. He is a Fellow of the Casualty Actuarial Society with 35 years experience as a consulting actuary, over 25 in the USA and nine in the UK. Allan has worked in the USA, Europe and Asia on all types of casualty insurance actuarial consulting assignments including ratemaking and rating plans, merger and acquisition analyses, loss reserving, dynamic financial analysis, new product development, financial planning, risk assessment, and regulatory issues. He has testified in court and before regulators on a variety of insurance issues.

Allan's clients have included multi-line primary and reinsurance companies, Lloyd's Syndicates and other London market reinsurers, and specialty companies in areas including workers compensation, medical malpractice, professional liability, health, title and warranty insurance.

Allan has University degrees in Mathematics and Physics, and is a Fellow of the Casualty Actuarial Society (1974), a Member of the American Academy of Actuaries (1995) and an Honorary Fellow of the Institute of Actuaries (1998). He holds the designation Certified Property/Casualty Underwriter and a Lloyd's Reserve Practicing Certificate.

Allan has served in various capacities with the Casualty Actuarial Society and the American Academy of Actuaries, including President, President Elect and Board Member for each of the organisations and as Examination Chairman and Vice-President-Research for the CAS. He has served on the General Insurance Board of the Institute of Actuaries and on a number of the Institute's committees.

INDUSTRY EXPERIENCE

Independent Consultant

- Navigant Consulting, Inc (2007 – present)
- Pembroke Managing Agency, Non-Executive Director and Audit Committee Chair and Ironshore UK – Non-Executive Director (2008-present)
- AMK Consulting (2005-2007)
- Deloitte – (2001-2005) – Actuarial & Insurance Solutions Practice Leader
- Bacon & Woodrow – (2000-2001) - Head of Insurance Practice
- Milliman & Robertson – (1985-2000) – NY Casualty Practice Leader, National Casualty Director, Member-Board of Directors, Chair-International Insurance Steering Group
- Peat Marwick Mitchell & Co – (1977-1985) – Principal
- Martin Segal Company – (1976-1977) – Actuary

Insurance Company

- The Home Insurance Company - (1971-1976) - Assistant Secretary & Actuary

PROFESSIONAL SOCIETY ACTIVITIES (MAIN POSITIONS)

Casualty Actuarial Society (CAS)

2004, 2007-09	Liaison to UK General Insurance Practice Executive Committee
2004-2007	Member, Board of Directors
1993-1996	Board Chairman, President, President-elect
1990-1993	Vice President Research and Development
1988-89, 1993-94	Long Range Planning Committee
1988-1989	Member, Board of Directors
1975-1986	Examination Committees - Chair (1983-86), Vice Chair (1981-83)

American Academy of Actuaries

1996-1999	President, Past-President, President-elect
1986-1990	Committee on Property/Liability Financial Reporting Principles

International Actuarial Association

1998-2000	Member-Education Committee, Chairman-Audit Committee
2006 -present	Risk Margins Working Party

Institute of Actuaries (UK)

2002, 2007-8	Member, General Insurance Board/General Insurance Practice Executive Committee
2006-present	Various Working Parties on Risk Margins and Solvency II

PUBLICATIONS

- CAS Forum (2000, 1992, 1990, 1982 and 1980) - Various papers on pricing, reserving, and financial analysis
- British Actuarial Journal (2006) *Assessment of Target Capital for General Insurance Firms*
- GIRO (2006) - *Interim Report on General Insurance Reserves for accounting and Solvency: Incorporating Provision for Risk*
- GIRO (2007) - *Cost of Capital Method of Risk Margins – Dealing with Neglected Issues*
- GIRO (2008)—*Actuarial Aspects of Internal Models for Solvency II*
- British Actuarial Journal - *Actuarial Aspects of Internal Models for Solvency II*

NAIC ADVISORY COMMITTEES

- 1990-93 NAIC Risk-Based Capital Actuarial Advisory Committee
- 1993-94 NAIC Title Insurance Schedule P Advisory Committee

13 APPENDIX III – EXPERT'S DECLARATION

I, Allan M Kaufman, declare that:

13.1.1 I understand that my duty includes providing written reports and giving evidence to help the court, and that this duty overrides any obligation to the party who has engaged me. I confirm that I have complied with my duty.

13.1.2 I confirm that insofar as the facts stated in my Report are within my own knowledge I have made clear which they are and I believe them to be true and that the opinions I have expressed represent my true and complete professional opinion.

13.1.3 I have endeavoured to include in my Report those matters, which I have knowledge of, or of which I have been made aware, that might adversely affect the validity of my opinion. I have clearly stated any qualifications to my opinion.

13.1.4 I have indicated the sources of all information I have used.

13.1.5 I have not, without forming an independent view, included or excluded anything which has been suggested to me by others.

13.1.6 I will notify those instructing me immediately and confirm in writing if for any reason my existing Report requires any correction or qualification.

13.1.7 I understand that:

13.1.8 My Report, subject to any corrections before swearing as to its correctness, will form evidence to be given under oath or affirmation;

13.1.9 I may be cross-examined on my Report by a cross-examiner assisted by an expert;

13.1.10 I confirm that I have not entered into any arrangement where the amount or payment of my fees is in any way dependent on the outcome of the case.

13.1.11 STATEMENT OF TRUTH

13.1.12 I confirm that insofar as the facts stated in my Report are within my own knowledge I have made clear which they are and I believe them to be true, and that the opinions I have expressed represent my true and complete professional opinion.

Allan M Kaufman, FCAS, FIA (Hon)

Equitas Actuarial Analysis

14.1.1 Equitas Reserve Reports for 1999-2008 and supporting data for 2007 and 2008.

14.1.2 Equitas Liability, Coverage & Mortality Models with supporting data – Reports and supporting data

14.1.3 Names Mortality Analysis

Background Legal Documentation

14.1.4 PCW and Lioncover Syndicates Insurance Co. Ltd.

14.1.5 Warrilow and Syndicates and Centrewrite

14.1.6 Speyford Ltd.

14.1.7 Other Lloyd's Guarantees

14.1.8 Hardship Agreements

14.1.9 Estate Protection Plans

14.1.10 EPTL

14.1.11 US Trust Funds

14.1.12 Other Overseas Trust Funds (Australia, Canada, South Africa)

14.1.13 FSCS

14.1.14 NICO Retrocession Contract

14.1.15 Reconstruction & Renewal Settlement

14.1.16 Reinsurance contracts related to Equitas, NICO, Centrewrite and Lioncover

Legal Documentation

14.1.17 Scheme document

14.1.18 Memoranda related to areas in which I relied on Clifford Chance legal advice.

PricewaterhouseCoopers (PwC) Reviews

14.1.19 Equitas has received additional advice and verification from PwC and provided me with copies of that information. The material from PwC is as follows:

1. Benchmarking of the Liability Model;
2. Parallel testing of the Liability Model and Coverage Model calculations;
3. Mortality study; and
4. Collectability study of retail debt.

Equitas Financial Reports

14.1.20 Equitas reports and accounts 1996 - 2008 (Year end 31 March)

14.1.21 Equitas Board and Audit Committee minutes 2004 – 2008.

15 APPENDIX V – BEST ESTIMATE OF LIABILITIES – UNDERLYING ASSUMPTIONS & METHODS

15.1 OVERVIEW

15.1.1 A key parameter in the Liability Model is the current best estimate of the value of Equitas liabilities.

15.1.2 Equitas has produced a reserving report in most years since R&R, the latest of which was as at 31 August 2008.

15.1.3 The following categories are considered in the reserving reports:

1. US Asbestos Direct;
2. US Asbestos Reinsurance;
3. Non-US Asbestos;
4. Pollution;
5. Health Hazards;
6. Catastrophes;
7. All Other Inwards; and
8. External Outwards Reinsurance.

15.1.4 This Appendix gives an overview of the methods Equitas used in assessing these liabilities.

15.1.5 This Appendix is organised as follows:

1. Current best estimate of liabilities; and
2. Reserve methodology and our review for each category of claim.

15.1.6 Our detailed review was done on the 2007 reserving work, along with updated 2008 work when this became available.

Navigant Team

15.1.7 The team involved in this review included:

1. Myself;
2. Actuaries;
3. Claim experts; and
4. Economists, with respect to observations regarding parameters and data on emerging experience.

15.1.8 All of the work was conducted under my direction.

15.1.9 The Equitas best estimate of the gross liability at 31 August 2007 is $9.3bn. This is divided by type of liability as shown in Table 6-1.

15.2 US Asbestos Direct

15.2.1 This category relates to direct Asbestos claims originating in the USA and Canada.

15.2.2 Equitas projected US Asbestos Direct claims separately for each known Policyholder.

15.2.3 Equitas reserving methodology involves the following three steps for each known Policyholder:

1. Determine the current claim severity and frequency (paragraph 15.2.4);
2. Project ultimate claims (paragraph 15.2.5); and
3. Apply coverage to determine Equitas share of the ultimate claims (paragraph 15.2.6).

15.2.4 Equitas selected an average cost per claim and current level of claims based on recent data. The methodology Equitas used for this selection varied by assured, based on the data available. Where information is available from the Policyholder, Equitas uses the claims paid by year and the number of injured workers by disease type. Where that detail is not available, Equitas uses the information provided by the Policyholder, supplemented by generic assumptions.

15.2.5 Equitas projected future claims by combining these starting points with the following general assumptions:

1. Epidemiological projections of future disease incidence;
2. Inflation;
3. Disease mix of reported but unpaid claims, recent filings and recent settlements;
4. Proportions of valid claimants by disease type;
5. Relative severities by disease type; and
6. The impact of differences in severity by age of claimant.

15.2.6 Equitas then applied coverage terms for the assured to the projected claims to determine their share of the ultimate claims.

Our Review of Claim Severity and Frequency

15.2.7 We selected a sample of Policyholders for review. Our review included Policyholders of various sizes. We reviewed Policyholders where substantial data was available, and Policyholders where Equitas needed to make assumptions because data is incomplete.

15.2.8 For each of the reviewed Policyholders, we determined how Equitas selected their assumptions, and we assessed whether the assumptions were consistent with the reported experience and our market knowledge. We verified that

Equitas made use of the latest information in their actuarial files. They have told us the files reflect all of the information that they have received from lawyer reports and otherwise. The lawyer reports are the standard basis for London Market reserving.

Our Review of Projection of Assured Level Ultimate Claims

15.2.9 For most Policyholders, Equitas project ultimate claims following a standard methodology. We reviewed this methodology and the assumptions listed in paragraph 15.2.5

15.2.10 We reviewed and discussed the general assumptions with our actuaries and our economics group.

Our Review of Coverage Application

15.2.11 The issues involved in interpreting coverage and applying coverage to claims varied significantly by Policyholder.

15.2.12 We reviewed the coverage assumptions for over half of the assureds by value, and discussed issues with RMSL's claims staff. We conducted this review in conjunction with Navigant's claims experts.

15.3 US Asbestos Reinsurance

15.3.1 This category relates to inwards reinsurance Asbestos claims originating in the USA and Canada.

15.3.2 It includes both US and non-US Cedents (in respect of claims originating in the USA and Canada) but is primarily US Cedents.

15.3.3 Equitas performed modelling on selected Cedents (in respect of reinsurance that is not retrocession) and Policyholders, as discussed below.

Reviewed Inward Reinsurance Claims

15.3.4 Policyholders whose claims were projected as part of the US Asbestos Direct work are referred to as modelled Policyholders.

15.3.5 For larger ceding insurers, referred to as the reviewed Cedents, Equitas then applied the Cedent's direct coverage to the ultimate claims for each modelled Policyholder to determine the Cedent's share of the ultimate claims. Equitas then estimated their ultimate claims by applying the reinsurance cover to the projected Cedent liabilities for each Policyholder.

15.3.6 For each reviewed Cedent, the non-modelled Policyholders are reserved based on their case reserves plus a provision for IBNR. This IBNR is selected when the Cedent is reviewed, and then rolled forward each year. When unexpected incurred movements occur, adjustments are made to the IBNR.

Non-Reviewed Inward Reinsurance Claims

15.3.7 In 2005 Equitas set an IBNR reserve in respect of non-reviewed claims, based primarily on a set of ratios of IBNR to paid claims. Information from the modelled claims was used to provide benchmarks, and ratios were selected to reflect the characteristics of the Policyholders and Cedents involved.

15.3.8 Since 2005 the approach for the non-reviewed claims has been to monitor the incurred development in the period, to compare it with the expected incurred development and to judgementally update the reserve held to reflect the experience.

15.3.9 All material reinsurance claims on which case reserves have been set are discussed periodically between the RMSL actuaries and the claims staff.

Our Review of US Asbestos Reinsurance

15.3.10 We reviewed Equitas assured level projections as a part of our review of the US Asbestos Direct work, as discussed in section 15.2.

15.3.11 We reviewed the selected ratios of IBNR to paid and assessed whether these were consistent with Equitas experience.

15.3.12 We reviewed the coverage assumptions for over half of the assureds by value, and discussed issues with RMSL's claim staff. We conducted this review in conjunction with Navigant's claims experts.

15.4 NON-US ASBESTOS

15.4.1 This category relates to bodily injury claims, resulting from Asbestos exposure, that originate outside the USA and Canada. It includes both direct and inward reinsurances. The majority of the liability is from direct UK employer's liability claims.

Direct UK Asbestos

15.4.2 Equitas projected the majority of the UK Asbestos direct liabilities at an aggregate level (all assureds/Cedents combined). Equitas selected an average cost per claim for each disease type based on a weighted average of the average cost per claim in recent years. The current annual rate of claims was, for each disease type, based on recent experience, using judgement, taking into account recent trends.

15.4.3 Equitas projected future claim numbers by applying a claim pattern to the estimated current annual rate of claims. The claim pattern was derived from projections performed by the Health and Safety Executive (HSE) and also utilised work undertaken by external consultants.

15.4.4 Equitas estimated the total future claims cost by multiplying the future claim numbers by the average cost of claim, taking into account claims inflation.

Other Direct International Asbestos

15.4.5 Equitas estimated the direct international (other than UK or US) Asbestos claims on a case by case basis.

Inwards Reinsurance

15.4.6 For Cedents with reliable historical paid data, Equitas' standard approach is to estimate an incurred development factor and use this to calculate the reserve. The reserves for other Cedents are based on judgement.

Our Review of Non-US Asbestos

15.4.7 We reviewed Equitas' assumptions and assessed whether they were consistent with the reported experience and our market knowledge.

15.4.8 We reviewed the methodology Equitas used to project future claims.

15.5 POLLUTION

15.5.1 This category relates to gradual environmental damage claims. This excludes one-off catastrophic events such as an oil tanker leakage, which are covered within the Catastrophe category.

15.5.2 Equitas estimated the future claims on large known Pollution cases on a case by case basis.

15.5.3 For their direct exposure, Equitas projected unknown (IBNR) claims and small known claims in aggregate. Equitas estimated the frequency of IBNR claims based on the rate at which new claims have emerged in the past. For these IBNR and small claims, Equitas estimated the average cost per claim based on recent experience of settlements, closures and claim reviews. For inwards reinsurance, the IBNR claims were estimated based upon the historical experience for each Cedent.

Our Review of Pollution

15.5.4 We reviewed Equitas' assumptions used in projecting IBNR and small claims, and assessed whether they were consistent with the reported experience.

15.5.5 We reviewed the Pollution reserves for over half of the Pollution cases by value, and discussed issues with RMSL's claim staff. We conducted this review in conjunction with Navigant's claims experts.

15.6 HEALTH HAZARDS

15.6.1 This category relates to claims in respect of all Health Hazards.

15.6.2 Equitas estimated the future claims on Health Hazards for each hazard separately, based on judgement, and in collaboration with claims staff.

15.6.3 Equitas also holds a reserve for unexpected development on known and unknown risks. Equitas selected the size of these reserves based on judgement.

Our Review of Health Hazards

15.6.4 We reviewed the Health Hazard reserves for over half of the Health Hazards by value, and discussed issues with RMSL's claim staff. We conducted this review in conjunction with Navigant's claims experts.

15.7 CATASTROPHES

15.7.1 This category relates to Catastrophe losses.

15.7.2 Equitas evaluated Catastrophe claims on a case by case basis.

Our Review of Catastrophes

15.7.3 We reviewed the Catastrophe methodology, and discussed issues with RMSL.

15.8 ALL OTHER INWARDS

15.8.1 This category relates to all inwards claims (direct and reinsurance) not included in the other categories.

15.8.2 Equitas reserved selected claim types within this category on a case by case basis.

15.8.3 Equitas projected the remainder of the claims on an aggregate basis, using standard actuarial projection techniques.

Our Review of All Other Inwards

15.8.4 We reviewed the composition of claims in this category and the aggregate projections.

15.9 EXTERNAL OUTWARDS REINSURANCE

15.9.1 This category relates to External Outwards Reinsurance recoveries.

15.9.2 Equitas evaluated the reinsurance asset using the following main steps:

1. Evaluate the appropriate reinsurance Recovery Rate, plus allowance for un-issued accruals by category of claim;
2. Estimate the proportion of these reinsurance recoveries that relate to external non-commuted reinsurance; and
3. Estimate the bad debt on reinsurance recoveries.

Reinsurance Recovery Rate by Category of Claim

15.9.3 Equitas estimated the Recovery Rate applicable to future claims for each category of claim using a combination of modelling work, historical Recovery Rates and judgement.

15.9.4 This Recovery Rate includes both recoveries on commuted and non-commuted reinsurance. It also includes both external reinsurance and Inter-Syndicate Reinsurance.

Estimation of External Non-Commuted Reinsurance

15.9.5 Equitas allocated the estimated reinsurance recoveries to the following three categories:

1. External non-commuted;
2. External commuted; and
3. Inter-Syndicate Reinsurance.

15.9.6 Equitas estimated these proportions based on the profile of outstanding reinsurance recoveries by category of claim.

Bad Debt

15.9.7 The bad debt was estimated at the reinsurer level, with an additional margin then added to this figure.

Our Review of External Outwards Reinsurance

15.9.8 We reviewed the Recovery Rates assumed for each category of claim.

16 APPENDIX VI – LIABILITY MODEL – UNDERLYING ASSUMPTIONS AND METHODS

16.1 OVERVIEW OF LIABILITY MODEL

16.1.1 This Appendix describes the Liability Model prepared by RMSL on behalf of Equitas.

16.1.2 There are four elements of the Liability Model:

1. Distribution of ultimate claim liability by type of claim;
2. Overall distribution of ultimate claim liabilities;
3. Payment pattern; and
4. Liability and inflation shocks.

16.1.3 These elements are described in the following sections.

16.2 Distribution of Ultimate Claim Liabilities by Type of Claim

16.2.1 The model considers the following types of claim:

1. US Asbestos (Direct and reinsurance combined);
2. Non-US Asbestos (Mostly UK);
3. Pollution;
4. Health Hazards;
5. Catastrophes; and
6. Balance of Account and Other.

16.2.2 Equitas fit a lognormal distribution to each type of claim The mean of the distribution was set equal to the mean gross reserve from the reserve analysis for each type of business. The standard deviation was selected to give a distribution that had a 75th percentile equal to the 75th percentile of the reserve from the reserve analysis for each type of claim.

16.2.3 For Non-US Asbestos, an adjustment was made to select a lognormal with slightly lower variability. This was done by using a mean assumption higher than the mean from the reserve Report, but not adjusting the 75th percentile.

16.2.4 For Pollution and Health Hazards, the 75th percentile from the reserve Report was approximately equal to the mean, so an adjustment was made to the mean to select a less extreme distribution.

16.2.5 The adjustments to the mean were balanced by adjustments to the overall distribution (described in section 16.3).

16.2.6 US Asbestos was considered on two bases. The first was using the mean and 75th percentile from the reserve analysis, and the second was using the mean from the reserve analysis and a higher 75th percentile. The 'US Asbestos with Base Variability' assumption was an average of the two fitted lognormal distributions, while the 'US Asbestos with High Variability' assumption uses only the lognormal distribution with the higher 75th percentile.

16.3 Overall Distribution of Ultimate Claim Liabilities

16.3.1 Equitas selected a matrix of linear correlations based on their experience of the types of claim and professional judgement.

16.3.2 The overall distribution of ultimate claims was estimated based on the distributions of the individual types of claim and the correlation matrix.

16.3.3 The distribution of the ultimates was generated for three assumption sets:

Base Assumptions

1. US Asbestos with base variability (see paragraph 16.2.6); and
2. Base correlation assumptions.

High Variability Assumption

1. US Asbestos with high variability (see paragraph 16.2.6); and
2. An alternative higher set of correlation assumptions (chosen using judgement).

Low Variability Assumption

1. US Asbestos with base variability (see paragraph 16.2.6); and
2. No correlation between types of claim.

16.4 PAYMENT PATTERN

16.4.1 The next step was to model the timing in how uncertainty in claim amounts might emerge from year to year.

16.4.2 The expected payment pattern was generated by aggregating the payment patterns from the reserve analysis, over all types of claim.

16.4.3 Twenty one alternative payments patterns were selected, some with longer and some with shorter duration payments than the expected pattern. Equitas selected these payments patterns using judgement.

16.4.4 The following table shows the mean term of each payment pattern, along with the probability of the pattern being selected for each scenario in the output.

Table 16-1 – Payment Patterns

Pattern	Probability	Mean Term
1	0.000%	31.51
2	0.002%	29.06
3	0.018%	26.53
4	0.109%	24.00
5	0.462%	21.58
6	1.479%	19.33
7	3.696%	17.30
8	7.393%	15.52
9	12.013%	13.98
10	16.018%	12.66
11	17.620%	11.54
12	16.018%	10.59
13	12.013%	9.78
14	7.393%	9.09
15	3.696%	8.50
16	1.479%	7.99
17	0.462%	7.54
18	0.109%	7.15
19	0.018%	6.80
20	0.002%	6.49
21	0.000%	6.22

16.4.5 The relative split between direct and inwards reinsurance business for each future year was selected based on the results of the reserve analysis. The selected split between direct and inwards reinsurance in each year is used regardless of which of the twenty one alternative payment patterns is used in each simulation.

16.5 LIABILITY AND INFLATION SHOCKS

16.5.1 There are two types of shocks – liability shocks, and inflation shocks.

Inflation Shocks

16.5.2 Inflation shocks represent unexpected inflation.

16.5.3 The model generates inflation shocks using the Wilkie Model, which is commonly used in actuarial projections.

Liability Shocks

16.5.4 Liability shocks reflect the various factors that will ultimately affect the total cost of claims, including type and number of claims, average claim costs, legal and judicial developments and so on.

16.5.5 Liability shocks were generated as a lognormal random-walk. The annual shocks were generated using a lognormal distribution for each of the fifty years in the projection period, with their impact on the future reserves carried at the beginning of each year being cumulative. The mean of the annual lognormal distribution and hence of the cumulative shocks, i.e. the lognormal random-walk, is 1.'

16.5.6 The standard deviation of the annual shocks was selected as described below.

16.5.7 The selected liability shock for the fourth year onward was the weighted average of the liability shocks over four years - that year and the previous three years.

Selection of the Standard Deviation of Liability Shocks

16.5.8 Claim scenarios (25,000 simulations) were projected using

1. Initial level of reserves (from the balance sheet);
2. Randomly selected Payment Patterns;
3. Random sets of Inflation Shocks; and
4. Random sets of Liability Shocks.

16.5.9 The results of these claim scenarios were compared with the desired overall distribution of ultimate claim liabilities.

16.5.10 The standard deviation of the annual liability shocks was selected to give a good match between the results and the desired distribution (the overall distribution of ultimate claim liabilities described in section 16.3).

16.5.11 This was an iterative process, with a number of trial values being tested for the standard deviation of liability shocks.

16.6 OUTPUT OF THE MODEL

16.6.1 The outputs from the steps above (section 16.2 to section 16.5) are:

1. A payment pattern, randomly selected from the twenty one alternatives; and
2. A set of shocks (liability and inflation shocks combined).

16.6.2 This output is produced for 25,000 random scenarios.

16.6.3 For each of the random scenarios, these outputs are used to calculate:

3. The reserves for each of the fifty years in the projection period; and
4. The value of claims for each of the fifty years in the projection period.

16.6.4 The calculation of items 3 and 4 (paragraph 16.6.3) above is easiest to explain in the context of the Coverage Model. The Coverage Model is described, along with these calculations, in Appendix VII.

17 APPENDIX VII – COVERAGE MODEL - UNDERLYING ASSUMPTIONS AND METHODS

17.1 OVERVIEW OF COVERAGE MODEL

17.1.1 Equitas used the Coverage Model to project claim scenarios, and calculate when and what proportion of these claims are paid.

17.1.2 The stages in the Coverage Model calculations are:

1. Project cash flows, reserves and assets (prior to insolvency);
2. Determine if and when an insolvency occurs;
3. Calculate the ultimate Insolvency Dividend Rate; and
4. Project cash flows, reserves and assets during insolvency.

17.1.3 The key assumptions used in the Coverage Model (Discussed in further detail in section 17.2) are:

1. Reserves at 31 December 2008;
2. Remaining NICO cover at 31 December 2008;
3. Equitas assets at 31 December 2008;
4. Long term investment return on Equitas assets; and
5. Recovery Rate from Names.

17.1.4 Each simulation uses the following output from the Liability Model:

1. Payment pattern (percentage of claims expected to be paid each year); and
2. Set of shocks (the unexpected movement in claims and reserves each year).

17.1.5 The model projects on a yearly basis for 50 years.

17.1.6 Note that 'Equitas' in this model includes all Equitas entities, and includes Speyford where relevant.

17.1.7 This description of the model illustrates the calculations without Lloyd's guarantees such as Lioncover.

17.2 KEY ASSUMPTIONS

17.2.1 The key assumptions used in the Coverage Model are:

Table 17-1 – Key Assumptions in Coverage Model

Assumption	Value Without Transfer	Value With Transfer
Reserve at 31 Dec 08	**$7,824m***	**$7,824m***
Remaining NICO cover at 31 Dec 08	**$13,109m**	**$14,389m**
Equitas assets at 31 Dec 08	**$132m**	**$81m**
Long Term Investment Return on Equitas Assets	**4% p.a.**	**4% p.a.**
Recovery Rate from Names	**Variable****	**n/a**

* The reserve assumption in this table is for the base assumption set. For the high mean assumption sets the reserves at 31 December 2008 are $9,389m.

** The Coverage Model can be parameterised with any level of Recovery Rate from Names

Reserves

17.2.2 The reserves as at 31 December 2008 are equal to $7,824m (see Table 6-1) for the base assumption set. For the high mean assumption sets the reserve at 31 December 2008 is $9,389m, which is 20% higher than the base assumption. The value of the reserves is unaffected by the Transfer.

Remaining NICO Cover

17.2.3 In the current structure the remaining NICO cover at 31 December 2008 is $13,109m, which is $5,285m above the reserves (see Table 3-18).

17.2.4 In the event of the Transfer the remaining NICO cover is increased by $1,300m to $14,409m, which is $6,585m above the reserves (see Table 3-18).

17.2.5 For the purpose of the Coverage Model, Equitas subtracted $20m from the NICO cover available to pay claims in the event of the Transfer, leaving $14,389m. This was done to test the effect of establishing trust funds funded with part of the NICO limit. The effect is immaterial.

Equitas Assets

17.2.6 In the current structure, Equitas assets at 31 December 2008 are equal to £123m (see Table 3-18). The modelling assets are equal to $132m (£92m), which is the Equitas assets (£123m) minus the present value of estimated future operating and governance costs (£21m), minus insolvency costs (£10m).

17.2.7 Equitas estimated the future operating and governance costs by projecting expected costs, using judgement, on a yearly basis until 2059.

17.2.8 Equitas estimated the costs associated with an insolvency process using judgement.

17.2.9 In the event of the Transfer, Equitas assets at 31 December 2008 are equal to £81m (see Table 3-18). The modelling assets are equal to $81m (£56m), which is

the Equitas assets (£81m) minus future operating and governance costs (£15m), minus insolvency costs (£10m).

17.2.10 Equitas has assumed that the future operating and governance costs are the same in the event of the Transfer as in the current structure, except with respect to certain costs that NICO is obliged to reimburse Equitas for in the event of the Transfer (the most significant being the Equitas audit fee).

17.2.11 Equitas has assumed that the insolvency costs are the same in the event of the Transfer as in the current structure.

Long Term Investment Return

17.2.12 Equitas estimated that long term investment returns are just under 4%, which was equal to the rate of return on long term gilts at the time of modelling.

17.2.13 This assumption is the same in the current structure as in the event of the Transfer.

Recovery Rate from Names

17.2.14 Equitas ran the Coverage Model using a range of assumptions for the Recovery Rate, from 0% to 100%.

17.3 CASH FLOWS, RESERVES AND ASSETS

Full Value of Claims

17.3.1 The full value of claims represents the value of claims made by Policyholders against Equitas. In the event of insolvency, the claim payments made to Policyholders will be less than this amount.

17.3.2 The full value of claims is calculated as follows:

Table 17-2 - Calculation of Full Value of Claims

	Full value of claims during the year
Equals	**The reserve at the beginning of the year**
Multiplied by	**Percentage of the Reserve expected to be paid out during the year (from the payment pattern)**

Reserves

17.3.3 Each year reserves are reduced by the full value of claims paid during the year. A shock is then applied to the reserve, which represents the unexpected change in the future liabilities.

17.3.4 Since the value of claims is calculated as a proportion of the reserves, movement in the reserves affects future claims.

Table 17-3 - Calculation of Reserves

	Reserve at the beginning of the year
Equals	**The reserve at the beginning of the previous year**
Minus	**Full value of claims during the previous year**
Multiplied by	**The shock for the year**

Estimate of Ultimate Claims

17.3.5 For each year in the projection period the estimate of the ultimate claims is equal to the reserve in that year (the estimate of all future claims), plus the sum of all past claims.

Table 17-4 - Calculation of Estimate of Ultimate Claims

	Estimate of ultimate claims at the beginning of the year
Equals	**Reserve at the beginning of the year**
Plus	**Sum of full value of claims in all previous years**

Claim Payments

17.3.6 If there is no insolvency, all claims are paid in full. In the event of insolvency claims are paid at the insolvency dividend rate. Calculation of the insolvency dividend rate is discussed in section 17.4.

Table 17-5 - Calculation of Claim Payments

	Claim payments during the year
Equals	**Full value of claims during the year**
Multiplied by	**Insolvency dividend rate (if during insolvency)**

Payments Made by NICO to Equitas

17.3.7 NICO pays Equitas the full value of claims while cover remains. In the event of and Equitas Insolvency, these payments are made to EPTL (considered here to be a part of 'Equitas'). Once cover is exhausted, NICO no longer makes any payments.

Table 17-6 - Calculation of Payments Made by NICO to Equitas

	Payments made by NICO to Equitas during the year
Equals	**Full value of claims during the year**
Or	**Remaining cover (if this is less than the full value of claims)**

Remaining NICO Cover

17.3.8 Each year the remaining NICO cover is reduced by the payments they make to Equitas.

Table 17-7 - Calculation of Remaining NICO Cover

	Remaining NICO cover at the beginning of the year
Equals	**The Remaining NICO cover at the beginning of the previous year**
Minus	**Payments made by NICO to Equitas during the year**

Expenses

17.3.9 Equitas has estimated the annual operating expenses, all expenses other than claim expenses, for the Equitas Group in the future.

17.3.10 For modelling purposes the initial assets are set equal to the actual assets minus the present value of those future operating expenses.

17.3.11 Claims handling expenses are paid by NICO while their reinsurance cover remains. Once NICO's cover runs out, expenses are paid by Equitas. The model assumes expenses are 10% of the full value of claims.

Table 17-8 - Calculation of Expenses

	Equitas claims handling expenses during the year
Equals	**Full value of claims during the year**
Minus	**Payments made by NICO to Equitas during the year**
Multiplied by	**Expense rate**

Equitas Assets

17.3.12 If there is no insolvency, or prior to insolvency if there is one, payments by NICO exactly match the payments by Equitas to Policyholders. However, Equitas assets grow with investment return each year.

Table 17-9 - Calculation of Equitas Assets (Prior to Insolvency)

	Equitas assets at the beginning of the year
Equals	**Equitas assets at the beginning of the previous year**
Plus	**Investment return earned on Equitas assets during the previous year**

17.3.13 In the event of insolvency NICO continues to pay the full value of claims to Equitas (specifically EPTL) until cover runs out. Equitas pays claims at the insolvency dividend rate, so a surplus is accumulated within Equitas.

17.3.14 Once NICO cover is exhausted assets decrease with claim payments and increase with investment return until all assets are paid out in year 50.

Table 17-10 - Calculation of Equitas Assets (During Insolvency)

	Equitas assets at the beginning of the year
Equals	**Equitas assets at the beginning of the previous year**
Plus	**Payments made by NICO to Equitas during the previous year**
Minus	**Claim payments during the previous year**
Minus	**Expenses during the previous year**
Plus	**Investment return earned on Equitas assets during the previous year**

Investment Return Earned on Equitas Assets

17.3.15 Investment return (used in Table 17-9 and Table 17-10) is calculated as 4% of Equitas assets at the beginning of the year.

Table 17-11 - Calculation of Investment Return on Equitas Assets

	Investment return earned on Equitas assets during the year
Equals	**Equitas assets at the beginning of the year**
Multiplied by	**Assumed long term investment return**

Total Remaining Assets

17.3.16 Total remaining assets is the sum of the remaining NICO cover (Table 17-7) and the Equitas assets.

Table 17-12- Calculation of Total Remaining Assets

	Total remaining assets at the beginning of the year
Equals	**The remaining NICO cover at the beginning of the year**
Plus	**Equitas assets at the beginning of the year**

Recoveries from Names

17.3.17 In the current structure, the model assumes that a percentage of the shortfall is recovered from Names. In the event of the Transfer there is no recovery from Names.

17.3.18 The recoveries from Names in this description include recoveries from PCW and Warrilow Names at the average rate, prior to the effect of the Lloyd's bonds and undertaking.

Table 17-13 - Calculation of Recoveries from Names

	Recoveries from Names during the year
Equals	**Full value of claims during the year**
Minus	**Claim payments during the year**
Multiplied by	**Recovery Rate from Names**

Shortfall

17.3.19 The shortfall is the full value of claims minus Equitas claim payments and recoveries from Names.

Table 17-14 - Calculation of Shortfall

	Shortfall during the year
Equals	**Full value of claims during the year**
Minus	**Claim payments during the year**
Minus	**Recoveries from Names during the year**

17.4 INSOLVENCY AND THE INSOLVENCY DIVIDEND RATE

Timing of Insolvency

17.4.1 Equitas is estimated to be insolvent in a given year if the reserve (defined in paragraph 17.3.3 at the beginning of the year is greater than the assets (defined in section 17.3 at the beginning of the year.

Insolvency Dividend Rate

17.4.2 The Insolvency Dividend Rate is equal to the present value of assets, minus the present value of claims handling expenses, divided by the present value of liabilities.

17.4.3 This represents the proportion of the liabilities that can be paid using the available assets, taking into consideration claims handling expenses and future investment return.

17.4.4 The Insolvency Dividend Rate does not vary by year, so a claim in year 50 is paid at the same rate as a claim in the year of insolvency.

17.4.5 Present values are used to take into account the investment return earned on assets during insolvency.

Table 17-15 - Calculation of Insolvency Dividend Rate

	Insolvency Dividend Rate
Equals	**Present value of assets at the insolvency date**
Minus	**Present value of claims handling expenses at the insolvency date**
Divided by	**Present value of liabilities at the insolvency date**

Present Value of Assets

17.4.6 The present value of assets is equal to the accumulated assets at the insolvency date, plus the present value of the future payments made by NICO to Equitas. The timing of the NICO payments to Equitas is important, as interest can be earned on any surplus built up in Equitas (EPTL).

Table 17-16 - Calculation of Present Value of Assets

	Present value of assets at the insolvency date
Equals	**Equitas assets at the date of insolvency**
Plus	**Present value of future NICO payments to Equitas during insolvency**

Present Value of Claims handling Expenses

17.4.7 Claims handling expenses are paid by Equitas once NICO cover is exhausted (see Table 17-8). The present value of these expenses is subtracted from the assets available to meet claims (see Table 17-15).

Present Value of Liabilities

17.4.8 In calculating the unpaid claims at the insolvency date the actual future claims (rather than expected) are used, taking into account future shocks. Although the future shocks cannot be known at the insolvency date they are used in the calculation to allow an Insolvency Dividend Rate to be chosen so that all assets are paid out.

17.4.9 This is a simplification of the likely actual process in which there would be an interim dividend rate set at a low level and a final dividend when there is sufficient information about the liabilities as a whole. In the actual situation Policyholders would recover a higher nominal dividend on a delayed basis, but an equivalent dividend on a present value basis.

Table 17-17 - Calculation of Present Value of Liabilities

	Present value of liabilities at the insolvency date
Equals	**Present value of unpaid claims at the insolvency date**
Plus	**Present value of expenses during insolvency**

Estimated vs. Actual Insolvency

17.4.10 In some scenarios assets temporarily dip below reserves, but ultimately they are sufficient to pay all claims in full. If so, then all claims are paid in full, and the simulation is not treated as an insolvency. Such 'temporary insolvencies' are likely to incur additional costs, but they are less frequent in the event of the Transfer.

17.4.11 If the Insolvency Dividend Rate is less than 100%, then this is treated as an actual Insolvency, and during Insolvency claims are paid at this rate.

17.5 Direct and Reinsurance Claims

17.5.1 The Coverage Model calculates the claims relating to direct and reinsurance Policyholders using an assumption on the relative proportion of direct and reinsurance claims in each year. Equitas' selection of this assumption was discussed in section 16.4.

Full Value of Claims

17.5.2 The full value of claims relating to direct Policyholders in each year are equal to the full value of claims relating to 'all Policyholders', described in paragraph 17.3.1, multiplied by the proportion of claims relating to direct Policyholders for that year.

Table 17-18 - Calculation of Full Value of Claims for Direct Policyholders

	Full value of claims during the year for direct Policyholders
Equals	**Full value of claims during the year**
Multiplied by	**Percentage of the full value of claims during the year relating to direct Policyholders**

17.5.3 Similarly, the full value of claims relating to reinsurance Policyholders in each year are equal to the full value of claims relating to 'all Policyholders', described in paragraph 17.3.1, multiplied by the proportion of claims relating to reinsurance Policyholders for that year.

Table 17-19 - Calculation of Full Value of Claims for Reinsurance Policyholders

	Full value of claims during the year for reinsurance Policyholders
Equals	**Full value of claims during the year**
Multiplied by	**Percentage of the full value of claims during the year relating to reinsurance Policyholders**

Claim Payments

17.5.4 If there is no insolvency, all claims are paid in full. In the event of insolvency claims are paid at the insolvency dividend rate. Calculation of the insolvency dividend rate for direct and reinsurance Policyholders is discussed in paragraph 17.5.5.

Table 17-20 - Calculation of Claim Payments for Direct and Reinsurance Policyholders

	Direct or reinsurance claim payments during the year
Equals	**Direct or reinsurance full value of claims during the year**
Multiplied by	**Direct or reinsurance insolvency dividend rate (if during insolvency)**

Direct and Reinsurance Dividend Rates

17.5.5 The insolvency dividend rate is calculated for all Policyholders, as discussed in section 17.4, and separately for direct and reinsurance Policyholders. As with

the insolvency dividend rate for all Policyholders, the insolvency dividend rate for direct and reinsurance Policyholders does not vary by year of claim.

17.5.6 In the current structure, these Insolvency Dividend Rate are the same.

17.5.7 In the event of the Transfer, direct Policyholders have priority over Speyford assets, so Speyford assets are included in the assets available to meet direct claims.

Table 17-21 - Calculation of Present Value of Assets Available to Meet Direct Policyholder Claims

	Present value of assets at the insolvency date available to meet direct Policyholder claims
Equals	**Equitas assets (excluding Speyford assets) at the date of insolvency**
Plus	**Present value of future NICO payments to Equitas during insolvency**
Multiplied by	**The proportion of unpaid claims relating to direct Policyholders**
Plus	**Speyford assets at the date of insolvency**

17.5.8 In the event of the Transfer, as direct Policyholders have priority over Speyford assets, Speyford assets are not included in the assets available to meet reinsurance claims.

Table 17-22 - Calculation of Present Value of Assets Available to Meet Reinsurance Policyholder Claims

	Present value of assets at the insolvency date available to meet reinsurance Policyholder claims
Equals	**Equitas assets (excluding Speyford assets) at the date of insolvency**
Plus	**Present value of future NICO payments to Equitas during insolvency**
Multiplied by	**The proportion of unpaid claims relating to reinsurance Policyholders**

17.5.9 Calculation of the present value of liabilities and claims handling expenses, and thence the insolvency dividend rate, is calculated for direct and reinsurance Policyholders as shown in section 17.4, for direct and reinsurance Policyholders separately.

17.5.10 For simplicity, when calculating payments (in paragraph 17.3.6) to 'all Policyholders' a single insolvency dividend rate is used, and does not reflect the change in mix between direct and reinsurance Policies year by year.

17.6 OUTPUT OF THE COVERAGE MODEL

17.6.1 The output of the Coverage Model is a variety of statistics on each simulation (25,000 simulations were run) including:

1. Full value of claims at each year;
2. Claim payments each year;
3. Year of insolvency (if insolvency occurred);
4. Insolvency dividend rate (if insolvency occurred); and
5. Full value of claims and claim payments at selected times (e.g. after 50 years).

17.6.2 These statistics are measured:

1. In the current structure, and in the event of the Transfer;
2. For direct, reinsurance and all Policyholders combined; and
3. Discounted and undiscounted where applicable.

17.6.3 The model was run for a number of assumption sets including:

1. Low, base and high mean;
2. Low, base and high variability; and
3. Various assumptions on recoveries from Names.

18 APPENDIX VIII – COVERAGE MODEL - EXAMPLE SCENARIO

18.1.1 The following tables and figures show the output of the Coverage Model for a given scenario.

18.1.2 The scenario chosen has an ultimate liability at the 96th percentile of the distribution. This scenario causes an insolvency in the current structure, and does not cause insolvency in the event of the Transfer.

18.1.3 Results are shown both in the event of the Transfer and in the current structure, and under two assumption sets: the Base Assumptions, and the High Mean Assumption. In the event of the Transfer, the example assumes a 30% shortfall Recovery Rate from Names.

18.1.4 Under the High Mean Assumption, the scenario causes an insolvency in the current structure and in the event of the Transfer.

References for Scenario Results Table

18.1.5 The following is a list of the columns in the operating results table, along with a reference to the table in Appendix VII that shows the formula used in each column.

Table 18-1 - References for Scenario Results Calculations

Column	Name	Table in Appendix VII
(1)	Estimate of Ultimate Claims	Table 17-4
(2)	Reserve	Table 17-3
(3)	Remaining NICO Cover	Table 17-7
(4)	Equitas Assets	Table 17-9, Table 17-10
(5)	Total Remaining Assets	Table 17-2
(6)	Investment Return Earned on Equitas Assets	Table 17-11
(7)	Equitas Claim Expenses	Table 17-8
(8)	Full Value of Claims	Table 17-12
(9)	Claim Payments	Table 17-5
(10)	Payments Made by NICO to EPTL	Table 17-6
(11)	Recovery From Names	Table 17-13
(12)	Shortfall	Table 17-14

18.1.6 Columns (2) and (8) are outputs from the Liability Model (See section 16.6)

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Table 18-2 - Scenario Results in the Current Structure
Base Assumptions

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	10,284	10,284	13,109	132	13,241	5	-	1,262	1,262	1,262	-	-
2	10,801	9,539	11,847	138	11,985	6	-	976	976	976	-	-
3	12,790	10,553	10,871	143	11,015	6	-	1,000	1,000	1,000	-	-
4	12,265	9,028	9,872	149	10,020	6	-	904	904	904	-	-
5	13,051	8,910	8,968	155	9,122	6	-	873	873	873	-	-
6	13,601	8,587	8,095	161	8,256	6	-	869	846	869	7	16
7	14,078	8,195	7,226	191	7,417	8	-	856	833	856	7	16
8	14,307	7,568	6,370	221	6,591	9	-	822	800	822	7	15
9	14,398	6,837	5,548	252	5,800	10	-	776	755	776	6	14
10	13,981	5,644	4,773	283	5,055	11	-	659	641	659	5	12
11	13,743	4,747	4,114	311	4,425	12	-	555	540	555	4	10
12	13,709	4,159	3,559	339	3,898	14	-	485	472	485	4	9
13	13,952	3,917	3,074	365	3,439	15	-	457	445	457	4	9
14	13,993	3,501	2,617	392	3,009	16	-	402	391	402	3	7
15	13,614	2,721	2,216	418	2,634	17	-	313	305	313	3	6
16	13,461	2,254	1,902	443	2,346	18	-	260	253	260	2	5
17	13,334	1,868	1,643	468	2,111	19	-	216	211	216	2	4
18	13,425	1,743	1,426	493	1,919	20	-	203	198	203	2	4
19	13,488	1,602	1,223	518	1,741	21	-	188	183	188	2	4
20	13,452	1,378	1,035	543	1,579	22	-	163	159	163	1	3
21	13,473	1,236	872	569	1,442	23	-	147	143	147	1	3
22	13,540	1,156	725	596	1,321	24	-	139	135	139	1	3
23	13,571	1,048	586	624	1,210	25	-	126	123	126	1	2
24	13,535	886	460	652	1,112	26	-	107	104	107	1	2
25	13,575	819	352	681	1,033	27	-	100	97	100	1	2
26	13,651	795	253	711	964	28	-	98	95	98	1	2
27	13,749	795	155	742	897	30	-	98	96	98	1	2
28	13,868	815	57	774	831	31	4	101	99	57	1	2
29	13,963	810	-	759	759	30	10	102	99	-	1	2
30	14,032	777	-	680	680	27	10	98	96	-	1	2
31	13,996	643	-	602	602	24	8	82	80	-	1	2
32	13,988	552	-	537	537	21	7	72	70	-	1	1
33	13,987	480	-	482	482	19	6	63	61	-	1	1
34	13,993	423	-	434	434	17	6	56	55	-	0	1
35	14,000	373	-	391	391	16	5	51	49	-	0	1
36	13,997	319	-	352	352	14	4	44	43	-	0	1
37	14,024	302	-	318	318	13	4	43	42	-	0	1
38	14,035	270	-	285	285	11	4	40	38	-	0	1
39	14,038	233	-	254	254	10	4	35	34	-	0	1
40	14,044	204	-	226	226	9	3	32	31	-	0	1
41	14,061	189	-	200	200	8	3	31	30	-	0	1
42	14,088	184	-	175	175	7	3	32	31	-	0	1
43	14,107	172	-	147	147	6	3	32	31	-	0	1
44	14,115	148	-	119	119	5	3	30	29	-	0	1
45	14,107	110	-	92	92	4	2	25	24	-	0	0
46	14,102	81	-	69	69	3	2	20	20	-	0	0
47	14,099	57	-	50	50	2	2	17	16	-	0	0
48	14,096	37	-	34	34	1	1	14	14	-	0	0
49	14,094	21	-	20	20	1	1	11	11	-	0	0
50	14,093	9	-	9	9	0	1	9	9	-	0	0
51	14,093	-	-	-	-	-	-	-	-	-	-	-
Total						708	98	14,093	13,851	13,109	73	170

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Table 18-3 - Scenario Results in the Event of the Transfer
Base Assumptions

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	10,284	10,284	14,389	81	14,470	3	-	1,262	1,262	1,262	-	-
2	10,801	9,539	13,127	84	13,211	3	-	976	976	976	-	-
3	12,790	10,553	12,151	87	12,239	3	-	1,000	1,000	1,000	-	-
4	12,265	9,028	11,152	91	11,243	4	-	904	904	904	-	-
5	13,051	8,910	10,248	95	10,342	4	-	873	873	873	-	-
6	13,601	8,587	9,375	98	9,473	4	-	869	869	869	-	-
7	14,078	8,195	8,506	102	8,608	4	-	856	856	856	-	-
8	14,307	7,568	7,650	106	7,756	4	-	822	822	822	-	-
9	14,398	6,837	6,828	111	6,939	4	-	776	776	776	-	-
10	13,981	5,644	6,053	115	6,168	5	-	659	659	659	-	-
11	13,743	4,747	5,394	120	5,513	5	-	555	555	555	-	-
12	13,709	4,159	4,839	124	4,963	5	-	485	485	485	-	-
13	13,952	3,917	4,354	129	4,483	5	-	457	457	457	-	-
14	13,993	3,501	3,897	135	4,032	5	-	402	402	402	-	-
15	13,614	2,721	3,496	140	3,635	6	-	313	313	313	-	-
16	13,461	2,254	3,182	146	3,328	6	-	260	260	260	-	-
17	13,334	1,868	2,923	151	3,074	6	-	216	216	216	-	-
18	13,425	1,743	2,706	157	2,864	6	-	203	203	203	-	-
19	13,488	1,602	2,503	164	2,667	7	-	188	188	188	-	-
20	13,452	1,378	2,315	170	2,485	7	-	163	163	163	-	-
21	13,473	1,236	2,152	177	2,329	7	-	147	147	147	-	-
22	13,540	1,156	2,005	184	2,189	7	-	139	139	139	-	-
23	13,571	1,048	1,866	191	2,057	8	-	126	126	126	-	-
24	13,535	886	1,740	199	1,939	8	-	107	107	107	-	-
25	13,575	819	1,632	207	1,840	8	-	100	100	100	-	-
26	13,651	795	1,533	215	1,748	9	-	98	98	98	-	-
27	13,749	795	1,435	224	1,659	9	-	98	98	98	-	-
28	13,868	815	1,337	233	1,570	9	-	101	101	101	-	-
29	13,963	810	1,235	242	1,478	10	-	102	102	102	-	-
30	14,032	777	1,134	252	1,386	10	-	98	98	98	-	-
31	13,996	643	1,035	262	1,297	10	-	82	82	82	-	-
32	13,988	552	953	273	1,226	11	-	72	72	72	-	-
33	13,987	480	882	283	1,165	11	-	63	63	63	-	-
34	13,993	423	819	295	1,113	12	-	56	56	56	-	-
35	14,000	373	762	307	1,069	12	-	51	51	51	-	-
36	13,997	319	711	319	1,030	13	-	44	44	44	-	-
37	14,024	302	667	332	998	13	-	43	43	43	-	-
38	14,035	270	624	345	969	14	-	40	40	40	-	-
39	14,038	233	584	359	943	14	-	35	35	35	-	-
40	14,044	204	549	373	922	15	-	32	32	32	-	-
41	14,061	189	517	388	905	16	-	31	31	31	-	-
42	14,088	184	486	403	889	16	-	32	32	32	-	-
43	14,107	172	454	420	873	17	-	32	32	32	-	-
44	14,115	148	422	436	858	17	-	30	30	30	-	-
45	14,107	110	392	454	845	18	-	25	25	25	-	-
46	14,102	81	367	472	839	19	-	20	20	20	-	-
47	14,099	57	347	491	838	20	-	17	17	17	-	-
48	14,096	37	330	510	840	20	-	14	14	14	-	-
49	14,094	21	316	531	847	21	-	11	11	11	-	-
50	14,093	9	305	552	857	22	-	9	9	9	-	-
51	14,093	-	296	574	870	23	-	-	-	-	-	-
Total						516	-	14,093	14,093	14,093	-	-

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Table 18-4 - Scenario Results in the Current Structure
High Mean Assumption

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	12,340	12,340	13,109	132	13,241	5	-	1,514	1,514	1,514	-	-
2	12,961	11,447	11,595	138	11,733	6	-	1,171	1,171	1,171	-	-
3	15,348	12,663	10,424	143	10,567	6	-	1,200	1,002	1,200	59	139
4	14,718	10,833	9,224	347	9,571	14	-	1,085	906	1,085	54	125
5	15,661	10,692	8,139	539	8,679	22	-	1,047	875	1,047	52	121
6	16,322	10,305	7,092	734	7,826	29	-	1,042	870	1,042	52	120
7	16,893	9,834	6,049	935	6,984	37	-	1,027	858	1,027	51	119
8	17,169	9,082	5,022	1,142	6,164	46	-	986	824	986	49	114
9	17,278	8,205	4,036	1,350	5,386	54	-	931	777	931	46	107
10	16,777	6,773	3,105	1,558	4,663	62	-	791	660	791	39	91
11	16,491	5,697	2,314	1,750	4,065	70	-	666	556	666	33	77
12	16,451	4,991	1,649	1,930	3,579	77	-	582	486	582	29	67
13	16,743	4,701	1,067	2,103	3,170	84	-	548	458	548	27	63
14	16,792	4,202	519	2,278	2,797	91	-	482	402	482	24	56
15	16,337	3,265	37	2,448	2,485	98	34	376	314	37	19	43
16	16,153	2,705	-	2,236	2,236	89	31	312	260	-	15	36
17	16,001	2,242	-	2,034	2,034	81	26	260	217	-	13	30
18	16,110	2,091	-	1,872	1,872	75	24	244	204	-	12	28
19	16,186	1,923	-	1,719	1,719	69	23	226	188	-	11	26
20	16,143	1,654	-	1,577	1,577	63	20	195	163	-	10	23
21	16,167	1,483	-	1,457	1,457	58	18	177	148	-	9	20
22	16,248	1,387	-	1,350	1,350	54	17	167	139	-	8	19
23	16,285	1,258	-	1,248	1,248	50	15	151	126	-	7	17
24	16,242	1,063	-	1,156	1,156	46	13	129	107	-	6	15
25	16,290	982	-	1,082	1,082	43	12	120	100	-	6	14
26	16,382	954	-	1,014	1,014	41	12	117	98	-	6	14
27	16,499	954	-	945	945	38	12	118	98	-	6	14
28	16,641	979	-	872	872	35	12	122	102	-	6	14
29	16,756	971	-	793	793	32	12	122	102	-	6	14
30	16,838	932	-	711	711	28	12	118	99	-	6	14
31	16,796	772	-	629	629	25	10	99	83	-	5	11
32	16,785	662	-	562	562	22	9	86	72	-	4	10
33	16,784	576	-	504	504	20	8	76	63	-	4	9
34	16,792	507	-	453	453	18	7	68	57	-	3	8
35	16,800	448	-	408	408	16	6	61	51	-	3	7
36	16,797	383	-	368	368	15	5	53	44	-	3	6
37	16,829	362	-	333	333	13	5	52	43	-	3	6
38	16,842	324	-	298	298	12	5	47	40	-	2	5
39	16,846	280	-	265	265	11	4	42	35	-	2	5
40	16,853	245	-	236	236	9	4	39	32	-	2	4
41	16,873	227	-	209	209	8	4	37	31	-	2	4
42	16,905	221	-	183	183	7	4	39	32	-	2	4
43	16,929	206	-	154	154	6	4	38	32	-	2	4
44	16,939	178	-	124	124	5	4	36	30	-	2	4
45	16,929	132	-	96	96	4	3	29	25	-	1	3
46	16,923	97	-	72	72	3	2	24	20	-	1	3
47	16,919	68	-	52	52	2	2	20	17	-	1	2
48	16,915	44	-	35	35	1	2	17	14	-	1	2
49	16,913	25	-	21	21	1	1	13	11	-	1	2
50	16,911	10	-	9	9	0	1	10	9	-	1	1
51	16,911	-	-	-	-	-	-	-	-	-	-	-
Total						1,704	380	16,911	14,565	13,109	704	1,642

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Table 18-5 - Scenario Results in the Event of the Transfer
High Mean Assumption

Year	(1) Estimate of Ultimate Claims (BOY)	(2) Reserve (BOY)	(3) Remaining NICO Cover (BOY)	(4) Equitas Assets (BOY)	(5) Total Remaining Assets (BOY)	(6) Interest Earned on Equitas Assets	(7) Equitas Claim Expenses	(8) Full Value of Claims	(9) Claim Payments	(10) Payments Made by NICO to Equitas	(11) Recovery From Names	(12) Shortfall
1	12,340	12,340	14,389	81	14,470	3	-	1,514	1,514	1,514	-	-
2	12,961	11,447	12,875	84	12,959	3	-	1,171	1,171	1,171	-	-
3	15,348	12,663	11,704	87	11,791	3	-	1,200	1,090	1,200	-	110
4	14,718	10,833	10,504	201	10,705	8	-	1,085	986	1,085	-	99
5	15,661	10,692	9,419	308	9,727	12	-	1,047	952	1,047	-	96
6	16,322	10,305	8,372	416	8,788	17	-	1,042	947	1,042	-	95
7	16,893	9,834	7,329	528	7,858	21	-	1,027	933	1,027	-	94
8	17,169	9,082	6,302	643	6,946	26	-	986	896	986	-	90
9	17,278	8,205	5,316	759	6,075	30	-	931	845	931	-	85
10	16,777	6,773	4,385	875	5,260	35	-	791	718	791	-	72
11	16,491	5,697	3,594	982	4,577	39	-	666	605	666	-	61
12	16,451	4,991	2,929	1,082	4,011	43	-	582	529	582	-	53
13	16,743	4,701	2,347	1,179	3,526	47	-	548	498	548	-	50
14	16,792	4,202	1,799	1,276	3,075	51	-	482	438	482	-	44
15	16,337	3,265	1,317	1,371	2,688	55	-	376	341	376	-	34
16	16,153	2,705	941	1,461	2,402	58	-	312	283	312	-	29
17	16,001	2,242	629	1,547	2,177	62	-	260	236	260	-	24
18	16,110	2,091	370	1,633	2,003	65	-	244	222	244	-	22
19	16,186	1,923	126	1,721	1,847	69	10	226	205	126	-	21
20	16,143	1,654	-	1,701	1,701	68	20	195	178	-	-	18
21	16,167	1,483	-	1,572	1,572	63	18	177	161	-	-	16
22	16,248	1,387	-	1,456	1,456	58	17	167	151	-	-	15
23	16,285	1,258	-	1,346	1,346	54	15	151	138	-	-	14
24	16,242	1,063	-	1,247	1,247	50	13	129	117	-	-	12
25	16,290	982	-	1,167	1,167	47	12	120	109	-	-	11
26	16,382	954	-	1,093	1,093	44	12	117	106	-	-	11
27	16,499	954	-	1,019	1,019	41	12	118	107	-	-	11
28	16,641	979	-	941	941	38	12	122	111	-	-	11
29	16,756	971	-	856	856	34	12	122	111	-	-	11
30	16,838	932	-	767	767	31	12	118	107	-	-	11
31	16,796	772	-	678	678	27	10	99	90	-	-	9
32	16,785	662	-	606	606	24	9	86	78	-	-	8
33	16,784	576	-	544	544	22	8	76	69	-	-	7
34	16,792	507	-	489	489	20	7	68	62	-	-	6
35	16,800	448	-	440	440	18	6	61	55	-	-	6
36	16,797	383	-	397	397	16	5	53	48	-	-	5
37	16,829	362	-	359	359	14	5	52	47	-	-	5
38	16,842	324	-	321	321	13	5	47	43	-	-	4
39	16,846	280	-	286	286	11	4	42	39	-	-	4
40	16,853	245	-	255	255	10	4	39	35	-	-	4
41	16,873	227	-	226	226	9	4	37	34	-	-	3
42	16,905	221	-	197	197	8	4	39	35	-	-	4
43	16,929	206	-	166	166	7	4	38	35	-	-	4
44	16,939	178	-	134	134	5	4	36	33	-	-	3
45	16,929	132	-	103	103	4	3	29	27	-	-	3
46	16,923	97	-	78	78	3	2	24	22	-	-	2
47	16,919	68	-	56	56	2	2	20	18	-	-	2
48	16,915	44	-	38	38	2	2	17	15	-	-	2
49	16,913	25	-	23	23	1	1	13	12	-	-	1
50	16,911	10	-	10	10	0	1	10	10	-	-	1
51	16,911	-	-	0	0	0	-	-	-	-	-	-
Total						1,392	252	16,911	15,610	14,389	-	1,302

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Table 18-6 - Scenario Results in the Current Structure
High Variability Assumption

Year	(1) Estimate of Ultimate Claims (BOY)	(2) Reserve (BOY)	(3) Remaining NICO Cover (BOY)	(4) Equitas Assets (BOY)	(5) Total Remaining Assets (BOY)	(6) Interest Earned on Equitas Assets	(7) Equitas Claim Expenses	(8) Full Value of Claims	(9) Claim Payments	(10) Payments Made by NICO to Equitas	(11) Recovery From Names	(12) Shortfall
1	10,714	10,714	13,109	132	13,241	5	-	1,314	1,314	1,314	-	-
2	11,335	10,021	11,795	138	11,932	6	-	1,025	1,025	1,025	-	-
3	13,744	11,404	10,769	143	10,912	6	-	1,080	999	1,080	24	57
4	13,089	9,669	9,689	230	9,919	9	-	968	895	968	22	51
5	14,040	9,652	8,721	313	9,033	13	-	946	874	946	21	50
6	14,739	9,405	7,775	397	8,172	16	-	951	880	951	22	50
7	15,327	9,042	6,824	484	7,308	19	-	944	873	944	21	50
8	15,582	8,352	5,879	575	6,454	23	-	907	839	907	21	48
9	15,684	7,548	4,972	667	5,639	27	-	856	791	856	19	45
10	15,177	6,184	4,116	758	4,874	30	-	722	667	722	16	38
11	14,881	5,166	3,394	843	4,237	34	-	604	558	604	14	32
12	14,848	4,530	2,790	922	3,713	37	-	528	488	528	12	28
13	15,144	4,297	2,262	999	3,261	40	-	501	463	501	11	26
14	15,189	3,842	1,761	1,077	2,838	43	-	441	407	441	10	23
15	14,719	2,930	1,321	1,153	2,474	46	-	337	312	337	8	18
16	14,530	2,405	983	1,225	2,208	49	-	277	256	277	6	15
17	14,378	1,975	706	1,295	2,001	52	-	229	211	229	5	12
18	14,489	1,858	478	1,364	1,841	55	-	217	200	217	5	11
19	14,557	1,709	261	1,435	1,695	57	-	201	185	201	5	11
20	14,507	1,459	60	1,507	1,567	60	11	172	159	60	4	9
21	14,529	1,308	-	1,457	1,457	58	16	156	144	-	4	8
22	14,605	1,228	-	1,356	1,356	54	15	148	136	-	3	8
23	14,638	1,114	-	1,259	1,259	50	13	134	124	-	3	7
24	14,592	934	-	1,172	1,172	47	11	113	105	-	3	6
25	14,639	867	-	1,103	1,103	44	11	106	98	-	2	6
26	14,729	852	-	1,038	1,038	42	10	104	97	-	2	6
27	14,848	866	-	973	973	39	11	107	99	-	2	6
28	14,993	904	-	902	902	36	11	113	104	-	3	6
29	15,111	910	-	823	823	33	11	114	106	-	3	6
30	15,199	883	-	739	739	30	11	112	103	-	3	6
31	15,153	725	-	654	654	26	9	93	86	-	2	5
32	15,140	620	-	585	585	23	8	80	74	-	2	4
33	15,138	538	-	526	526	21	7	71	65	-	2	4
34	15,146	475	-	475	475	19	6	63	59	-	1	3
35	15,154	419	-	429	429	17	6	57	53	-	1	3
36	15,150	358	-	387	387	15	5	50	46	-	1	3
37	15,183	341	-	352	352	14	5	49	45	-	1	3
38	15,196	306	-	316	316	13	4	45	41	-	1	2
39	15,200	265	-	283	283	11	4	40	37	-	1	2
40	15,208	233	-	253	253	10	4	37	34	-	1	2
41	15,230	218	-	226	226	9	4	36	33	-	1	2
42	15,266	218	-	198	198	8	4	38	35	-	1	2
43	15,292	207	-	167	167	7	4	38	36	-	1	2
44	15,303	179	-	134	134	5	4	36	33	-	1	2
45	15,293	132	-	102	102	4	3	29	27	-	1	2
46	15,285	96	-	76	76	3	2	24	22	-	1	1
47	15,280	66	-	55	55	2	2	20	18	-	0	1
48	15,277	43	-	36	36	1	2	16	15	-	0	1
49	15,273	23	-	21	21	1	1	12	11	-	0	1
50	15,272	10	-	10	10	0	1	10	9	-	0	1
51	15,272	-	-	0	0	0	-	-	-	-	-	-
Total						1,270	216	15,272	14,295	13,109	293	684

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Table 18-7 - Scenario Results in the Event of the Transfer
High Variability Assumption

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	10,714	10,714	14,389	81	14,470	3	-	1,314	1,314	1,314	-	-
2	11,335	10,021	13,075	84	13,159	3	-	1,025	1,025	1,025	-	-
3	13,744	11,404	12,049	87	12,137	3	-	1,080	1,080	1,080	-	-
4	13,089	9,669	10,969	91	11,060	4	-	968	968	968	-	-
5	14,040	9,652	10,001	95	10,095	4	-	946	946	946	-	-
6	14,739	9,405	9,055	98	9,153	4	-	951	927	951	-	24
7	15,327	9,042	8,104	126	8,230	5	-	944	921	944	-	24
8	15,582	8,352	7,159	155	7,314	6	-	907	884	907	-	23
9	15,684	7,548	6,252	184	6,436	7	-	856	834	856	-	22
10	15,177	6,184	5,396	213	5,609	9	-	722	704	722	-	18
11	14,881	5,166	4,674	240	4,914	10	-	604	588	604	-	15
12	14,848	4,530	4,070	265	4,336	11	-	528	515	528	-	13
13	15,144	4,297	3,542	289	3,831	12	-	501	488	501	-	13
14	15,189	3,842	3,041	313	3,354	13	-	441	429	441	-	11
15	14,719	2,930	2,601	337	2,938	13	-	337	329	337	-	9
16	14,530	2,405	2,263	359	2,622	14	-	277	270	277	-	7
17	14,378	1,975	1,986	380	2,367	15	-	229	223	229	-	6
18	14,489	1,858	1,758	401	2,159	16	-	217	211	217	-	5
19	14,557	1,709	1,541	423	1,964	17	-	201	195	201	-	5
20	14,507	1,459	1,340	445	1,785	18	-	172	168	172	-	4
21	14,529	1,308	1,168	467	1,635	19	-	156	152	156	-	4
22	14,605	1,228	1,012	490	1,502	20	-	148	144	148	-	4
23	14,638	1,114	864	513	1,377	21	-	134	131	134	-	3
24	14,592	934	730	537	1,267	21	-	113	110	113	-	3
25	14,639	867	617	561	1,179	22	-	106	103	106	-	3
26	14,729	852	512	586	1,098	23	-	104	102	104	-	3
27	14,848	866	407	612	1,019	24	-	107	104	107	-	3
28	14,993	904	300	640	940	26	-	113	110	113	-	3
29	15,111	910	188	668	856	27	-	114	111	114	-	3
30	15,199	883	73	698	771	28	4	112	109	73	-	3
31	15,153	725	-	686	686	27	9	93	91	-	-	2
32	15,140	620	-	614	614	25	8	80	78	-	-	2
33	15,138	538	-	552	552	22	7	71	69	-	-	2
34	15,146	475	-	498	498	20	6	63	62	-	-	2
35	15,154	419	-	450	450	18	6	57	56	-	-	1
36	15,150	358	-	406	406	16	5	50	49	-	-	1
37	15,183	341	-	369	369	15	5	49	47	-	-	1
38	15,196	306	-	332	332	13	4	45	44	-	-	1
39	15,200	265	-	297	297	12	4	40	39	-	-	1
40	15,208	233	-	266	266	11	4	37	36	-	-	1
41	15,230	218	-	237	237	9	4	36	35	-	-	1
42	15,266	218	-	207	207	8	4	38	37	-	-	1
43	15,292	207	-	175	175	7	4	38	37	-	-	1
44	15,303	179	-	141	141	6	4	36	35	-	-	1
45	15,293	132	-	107	107	4	3	29	29	-	-	1
46	15,285	96	-	80	80	3	2	24	24	-	-	1
47	15,280	66	-	57	57	2	2	20	19	-	-	1
48	15,277	43	-	38	38	2	2	16	16	-	-	0
49	15,273	23	-	22	22	1	1	12	12	-	-	0
50	15,272	10	-	10	10	0	1	10	9	-	-	0
51	15,272	-	-	0	0	0	-	-	-	-	-	-
Total						639	88	15,272	15,021	14,389	-	251

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Table 18-8 - Scenario Results in the Current Structure
High Mean / High Variability Assumption

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	12,856	12,856	13,109	132	13,241	5	-	1,577	1,577	1,577	-	-
2	13,602	12,025	11,532	138	11,669	6	-	1,230	972	1,230	77	181
3	16,492	13,685	10,302	401	10,703	16	-	1,297	1,025	1,297	82	190
4	15,706	11,602	9,005	689	9,694	28	-	1,162	918	1,162	73	171
5	16,849	11,583	7,843	960	8,803	38	-	1,135	897	1,135	71	167
6	17,687	11,286	6,708	1,237	7,945	49	-	1,142	902	1,142	72	168
7	18,393	10,850	5,567	1,526	7,092	61	-	1,133	896	1,133	71	166
8	18,698	10,022	4,433	1,824	6,258	73	-	1,089	860	1,089	68	160
9	18,821	9,057	3,345	2,126	5,470	85	-	1,027	812	1,027	65	151
10	18,212	7,421	2,317	2,426	4,743	97	-	866	685	866	55	127
11	17,857	6,199	1,451	2,705	4,156	108	-	724	572	724	46	106
12	17,818	5,435	727	2,965	3,692	119	-	634	501	634	40	93
13	18,173	5,157	93	3,216	3,309	129	51	601	475	93	38	88
14	18,227	4,610	-	2,912	2,912	116	53	529	418	-	33	78
15	17,662	3,516	-	2,558	2,558	102	40	405	320	-	25	59
16	17,436	2,886	-	2,300	2,300	92	33	333	263	-	21	49
17	17,254	2,371	-	2,096	2,096	84	27	274	217	-	17	40
18	17,387	2,230	-	1,935	1,935	77	26	260	205	-	16	38
19	17,469	2,051	-	1,781	1,781	71	24	241	190	-	15	35
20	17,409	1,751	-	1,638	1,638	66	21	207	163	-	13	30
21	17,434	1,569	-	1,520	1,520	61	19	187	148	-	12	27
22	17,526	1,474	-	1,414	1,414	57	18	177	140	-	11	26
23	17,566	1,336	-	1,313	1,313	53	16	161	127	-	10	24
24	17,511	1,121	-	1,222	1,222	49	14	136	107	-	9	20
25	17,567	1,041	-	1,150	1,150	46	13	127	100	-	8	19
26	17,675	1,022	-	1,083	1,083	43	13	125	99	-	8	18
27	17,818	1,039	-	1,015	1,015	41	13	128	101	-	8	19
28	17,992	1,085	-	941	941	38	14	135	107	-	8	20
29	18,134	1,092	-	858	858	34	14	137	108	-	9	20
30	18,239	1,060	-	771	771	31	13	134	106	-	8	20
31	18,183	870	-	682	682	27	11	111	88	-	7	16
32	18,169	744	-	610	610	24	10	96	76	-	6	14
33	18,166	645	-	548	548	22	8	85	67	-	5	12
34	18,175	570	-	495	495	20	8	76	60	-	5	11
35	18,185	503	-	447	447	18	7	68	54	-	4	10
36	18,180	430	-	404	404	16	6	60	47	-	4	9
37	18,219	409	-	367	367	15	6	58	46	-	4	9
38	18,235	367	-	330	330	13	5	54	42	-	3	8
39	18,240	318	-	295	295	12	5	48	38	-	3	7
40	18,250	280	-	264	264	11	4	44	35	-	3	6
41	18,276	262	-	235	235	9	4	43	34	-	3	6
42	18,319	261	-	206	206	8	5	46	36	-	3	7
43	18,351	248	-	174	174	7	5	46	36	-	3	7
44	18,364	215	-	140	140	6	4	43	34	-	3	6
45	18,351	159	-	107	107	4	4	35	28	-	2	5
46	18,343	115	-	80	80	3	3	29	23	-	2	4
47	18,337	80	-	57	57	2	2	24	19	-	1	3
48	18,332	51	-	38	38	2	2	19	15	-	1	3
49	18,328	28	-	22	22	1	1	15	12	-	1	2
50	18,327	12	-	10	10	0	1	12	9	-	1	2
51	18,327	-	-	(0)	(0)	(0)	-	-	-	-	-	-
Total						2,094	522	18,327	14,814	13,109	1,054	2,459

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Table 18-9 - Scenario Results in the Event of the Transfer
High Mean / High Variability Assumption

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Year	Estimate of Ultimate Claims (BOY)	Reserve (BOY)	Remaining NICO Cover (BOY)	Equitas Assets (BOY)	Total Remaining Assets (BOY)	Interest Earned on Equitas Assets	Equitas Claim Expenses	Full Value of Claims	Claim Payments	Payments Made by NICO to Equitas	Recovery From Names	Shortfall
1	12,856	12,856	14,389	81	14,470	3	-	1,577	1,577	1,577	-	-
2	13,602	12,025	12,812	84	12,896	3	-	1,230	1,230	1,230	-	-
3	16,492	13,685	11,582	87	11,669	3	-	1,297	1,092	1,297	-	204
4	15,706	11,602	10,285	295	10,580	12	-	1,162	979	1,162	-	183
5	16,849	11,583	9,123	490	9,613	20	-	1,135	956	1,135	-	179
6	17,687	11,286	7,988	688	8,676	28	-	1,142	962	1,142	-	180
7	18,393	10,850	6,847	895	7,742	36	-	1,133	955	1,133	-	178
8	18,698	10,022	5,713	1,109	6,823	44	-	1,089	917	1,089	-	171
9	18,821	9,057	4,625	1,325	5,950	53	-	1,027	866	1,027	-	162
10	18,212	7,421	3,597	1,540	5,137	62	-	866	730	866	-	136
11	17,857	6,199	2,731	1,738	4,469	70	-	724	610	724	-	114
12	17,818	5,435	2,007	1,921	3,928	77	-	634	534	634	-	100
13	18,173	5,157	1,373	2,098	3,471	84	-	601	507	601	-	95
14	18,227	4,610	772	2,277	3,048	91	-	529	445	529	-	83
15	17,662	3,516	243	2,451	2,694	98	16	405	341	243	-	64
16	17,436	2,886	-	2,435	2,435	97	33	333	280	-	-	52
17	17,254	2,371	-	2,219	2,219	89	27	274	231	-	-	43
18	17,387	2,230	-	2,049	2,049	82	26	260	219	-	-	41
19	17,469	2,051	-	1,886	1,886	75	24	241	203	-	-	38
20	17,409	1,751	-	1,734	1,734	69	21	207	174	-	-	33
21	17,434	1,569	-	1,609	1,609	64	19	187	158	-	-	29
22	17,526	1,474	-	1,497	1,497	60	18	177	149	-	-	28
23	17,566	1,336	-	1,390	1,390	56	16	161	136	-	-	25
24	17,511	1,121	-	1,294	1,294	52	14	136	114	-	-	21
25	17,567	1,041	-	1,217	1,217	49	13	127	107	-	-	20
26	17,675	1,022	-	1,147	1,147	46	13	125	106	-	-	20
27	17,818	1,039	-	1,074	1,074	43	13	128	108	-	-	20
28	17,992	1,085	-	996	996	40	14	135	114	-	-	21
29	18,134	1,092	-	909	909	36	14	137	115	-	-	22
30	18,239	1,060	-	816	816	33	13	134	113	-	-	21
31	18,183	870	-	722	722	29	11	111	94	-	-	18
32	18,169	744	-	646	646	26	10	96	81	-	-	15
33	18,166	645	-	581	581	23	8	85	71	-	-	13
34	18,175	570	-	524	524	21	8	76	64	-	-	12
35	18,185	503	-	473	473	19	7	68	58	-	-	11
36	18,180	430	-	428	428	17	6	60	50	-	-	9
37	18,219	409	-	388	388	16	6	58	49	-	-	9
38	18,235	367	-	349	349	14	5	54	45	-	-	8
39	18,240	318	-	312	312	12	5	48	41	-	-	8
40	18,250	280	-	279	279	11	4	44	37	-	-	7
41	18,276	262	-	249	249	10	4	43	36	-	-	7
42	18,319	261	-	218	218	9	5	46	38	-	-	7
43	18,351	248	-	184	184	7	5	46	39	-	-	7
44	18,364	215	-	148	148	6	4	43	37	-	-	7
45	18,351	159	-	113	113	5	4	35	30	-	-	6
46	18,343	115	-	84	84	3	3	29	24	-	-	5
47	18,337	80	-	60	60	2	2	24	20	-	-	4
48	18,332	51	-	40	40	2	2	19	16	-	-	3
49	18,328	28	-	24	24	1	1	15	13	-	-	2
50	18,327	12	-	11	11	0	1	12	10	-	-	2
51	18,327	-	-	(0)	(0)	(0)	-	-	-	-	-	-
Total						1,807	394	18,327	15,883	14,389	-	2,443

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18.2 CASH FLOW FIGURES AND KEY STATISTICS

18.2.1 The figures and tables shown in this section are based on the output of the Coverage Model for the selected scenario.

18.2.2 There are four types of figures and tables as follows:

1. Figure of Undiscounted Claim Payments and Shortfall in the current structure;
2. Figure of Undiscounted Claim Payments and Shortfall in the event of the Transfer;
3. Figure of Estimated Ultimate Liability and Total Assets Plus Claims to Date; and
4. Key Statistics Table.

18.2.3 The Undiscounted Claim Payments and Shortfall Figures show the claim payments made before insolvency, the claim payments made during insolvency, and the shortfall during insolvency.

18.2.4 The Estimated Ultimate Liability and Total Assets Plus Claims to Date Figure shows the movement over time of the Estimated Ultimate Liability and Total Assets Plus Claims to Date (defined in the section above) both in the current structure and in the event of the Transfer.

18.2.5 The Key Statistics Tables contain the following information, for three Policyholder groups: All Policyholders, Reinsurance Policyholders, Direct Policyholders, and Long Tail Direct Policyholders.

1. **Paid Before Equitas Insolvency**: The claims paid (in full) prior to insolvency;
2. **Unpaid at Equitas Insolvency:** The full value of claims unpaid at insolvency;
3. **Ultimate Liability:** The full value of all claims, (1)+(2);
4. **Insolvency Dividend Rate (%):** The proportion of claims paid during insolvency;
5. **Insolvency Dividend ($):** The value of claims paid after insolvency, (2)*(4).
6. **Shortfall:** The difference between the full value of unpaid claims and the amount paid to Policyholders during insolvency, (2) – (5);
7. **Break Even Recovery Ratio:** The Recovery Rate from Names that would make Policyholders equally well off in the event of the transfer as in the current structure, 1 - (post 6)/(pre 6);
8. **Ultimate Paid:** The total amount paid to Policyholders, (1) + (5); and
9. **Ultimate Payout:** The overall proportion of claims paid to Policyholders, (8)/(3).

18.2.6 There is a set of figures and tables for each of the following assumption sets:

1. Base assumptions;
2. High mean assumption;
3. High variability assumption; and
4. High variability, high mean assumption.

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Figure 18-10- Key Statistics- Base Assumptions

	Post	Pre
Insolvency Year	N/A	6

All Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	14,093	5,014
(2)	Unpaid at Insolvency	-	9,079
(3)	Ultimate Liability	14,093	14,093
(4)	**Insolvency Dividend Rate (%)**	**100.0%**	**97.3%**
(5)	Insolvency Dividend ($)	-	8,836
(6)	**Shortfall**	**-**	**242**
(7)	**Break Even Recovery Ratio**	**100.0%**	
(8)	Ultimate Paid	14,093	13,851
(9)	**Ultimate Payout**	**100.0%**	**98.3%**

Reinsurance Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	6,517	2,354
(2)	Unpaid at Insolvency	-	4,163
(3)	Ultimate Liability	6,517	6,517
(4)	**Insolvency Dividend Rate (%)**	**100.0%**	**97.3%**
(5)	Insolvency Dividend ($)	-	4,052
(6)	**Shortfall**	**-**	**111**
(7)	**Break Even Recovery Ratio**	**100.0%**	
(8)	Ultimate Paid	6,517	6,406
(9)	**Ultimate Payout**	**100.0%**	**98.3%**

Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	7,575	2,660
(2)	Unpaid at Insolvency	-	4,915
(3)	Ultimate Liability	7,575	7,575
(4)	**Insolvency Dividend Rate (%)**	**100.0%**	**97.3%**
(5)	Insolvency Dividend ($)	-	4,784
(6)	**Shortfall**	**-**	**131**
(7)	**Break Even Recovery Ratio**	**100.0%**	
(8)	Ultimate Paid	7,575	7,444
(9)	**Ultimate Payout**	**100.0%**	**98.3%**

Long Tail Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	6.6	-
(2)	Unpaid at Insolvency	-	6.6
(3)	Ultimate Liability	6.6	6.6
(4)	**Insolvency Dividend Rate (%)**	**100.0%**	**97.3%**
(5)	Insolvency Dividend ($)	-	6.4
(6)	**Shortfall**	**-**	**0.2**
(7)	**Break Even Recovery Ratio**	**100.0%**	
(8)	Ultimate Paid	6.6	6.4
(9)	**Ultimate Payout**	**100.0%**	**97.3%**

Figure 18-11-Estimated Ultimate Liability and Total Assets Plus Claims to Date (Scenario)- Base Assumptions

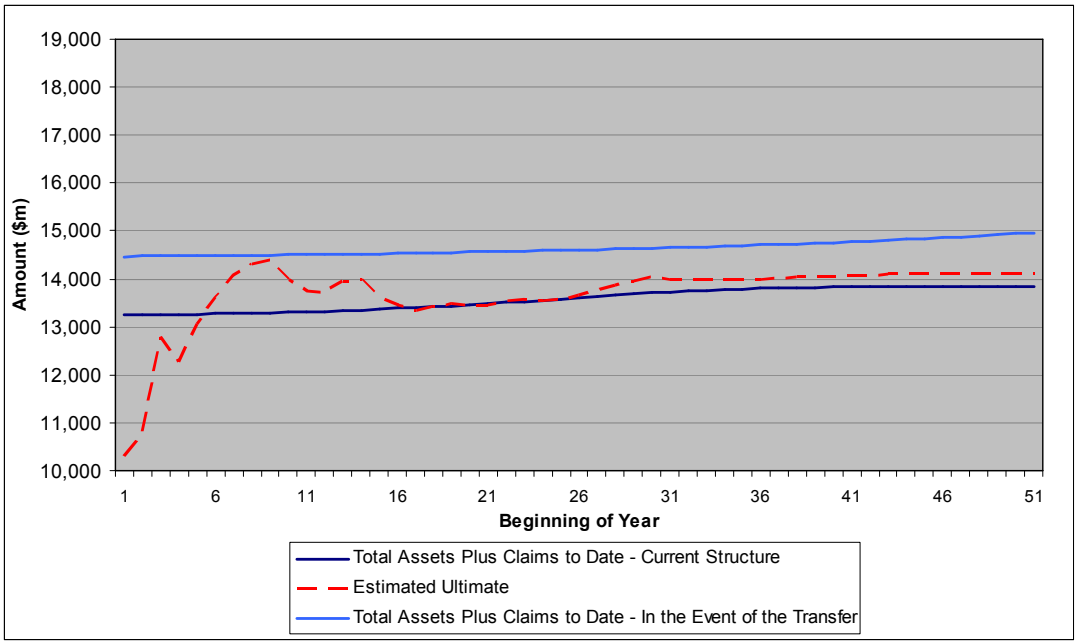


Figure 18-12- Undiscounted Claim Payments and Shortfall (Scenario) Base Assumptions-Current Structure

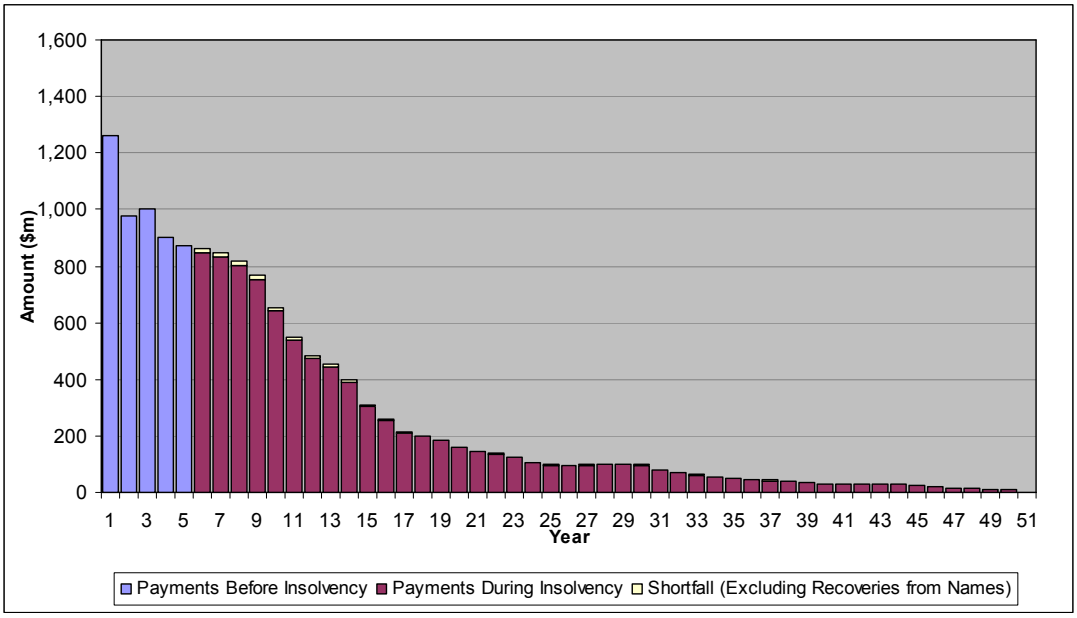


Figure 18-13- Undiscounted Claim Payments and Shortfall (Scenario) Base Assumptions-In the Event of the Transfer Structure

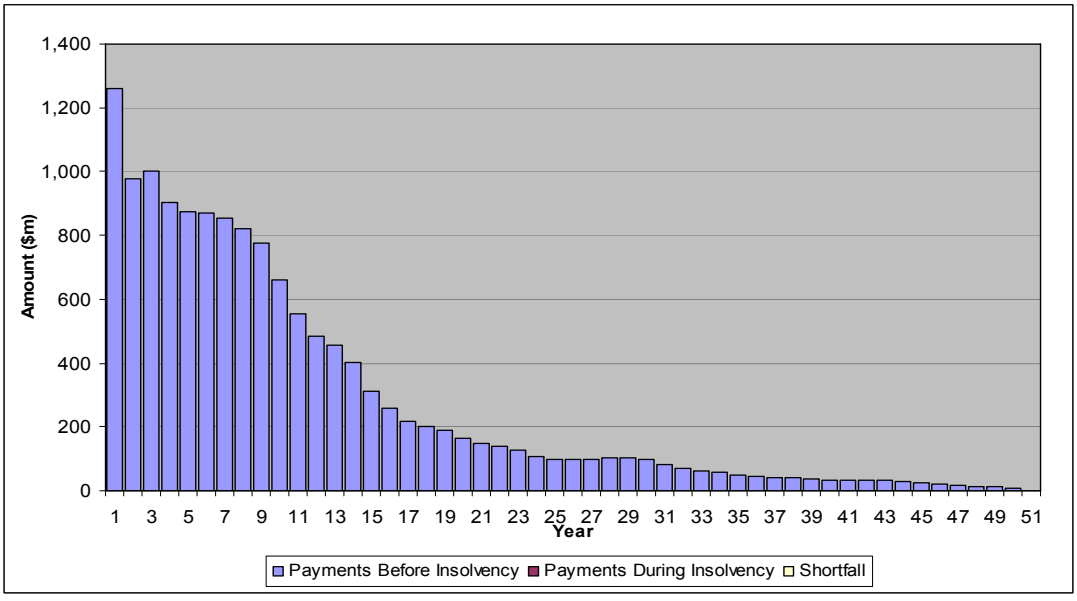


Figure 18-14- Key Statistics – High Mean Assumption

	Post	Pre
Insolvency Year	3	3

All Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	2,685	2,685
(2)	Unpaid at Insolvency	14,226	14,226
(3)	Ultimate Liability	16,911	16,911
(4)	**Insolvency Dividend Rate (%)**	**90.8%**	**83.5%**
(5)	Insolvency Dividend ($)	12,925	11,880
(6)	**Shortfall**	**1,302**	**2,346**
(7)	**Break Even Recovery Ratio**	**44.5%**	
(8)	Ultimate Paid	15,610	14,565
(9)	**Ultimate Payout**	**92.3%**	**86.1%**

Reinsurance Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	1,259	1,259
(2)	Unpaid at Insolvency	6,562	6,562
(3)	Ultimate Liability	7,821	7,821
(4)	**Insolvency Dividend Rate (%)**	**90.5%**	**83.5%**
(5)	Insolvency Dividend ($)	5,941	5,480
(6)	**Shortfall**	**621**	**1,082**
(7)	**Break Even Recovery Ratio**	**42.6%**	
(8)	Ultimate Paid	7,200	6,739
(9)	**Ultimate Payout**	**92.1%**	**86.2%**

Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	1,426	1,426
(2)	Unpaid at Insolvency	7,664	7,664
(3)	Ultimate Liability	9,090	9,090
(4)	**Insolvency Dividend Rate (%)**	**91.1%**	**83.5%**
(5)	Insolvency Dividend ($)	6,984	6,400
(6)	**Shortfall**	**680**	**1,264**
(7)	**Break Even Recovery Ratio**	**46.2%**	
(8)	Ultimate Paid	8,410	7,826
(9)	**Ultimate Payout**	**92.5%**	**86.1%**

Long Tail Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	-	-
(2)	Unpaid at Insolvency	7.9	7.9
(3)	Ultimate Liability	7.9	7.9
(4)	**Insolvency Dividend Rate (%)**	**91.1%**	**83.5%**
(5)	Insolvency Dividend ($)	7.2	6.6
(6)	**Shortfall**	**0.7**	**1.3**
(7)	**Break Even Recovery Ratio**	**46.2%**	
(8)	Ultimate Paid	7.2	6.6
(9)	**Ultimate Payout**	**91.1%**	**83.5%**

Figure 18-15- Estimated Ultimate Liability and Total Assets Plus Claims to Date (Scenario)- High Mean Assumption

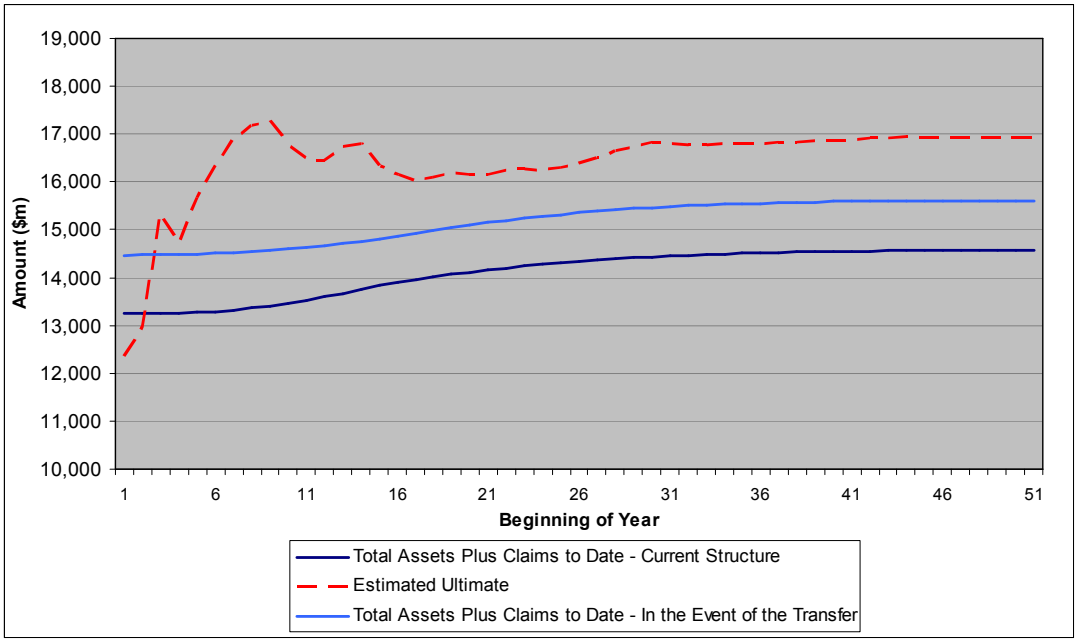


Figure 18-16 Undiscounted Claim Payments and Shortfall (Scenario) High Mean Assumption-Current Structure

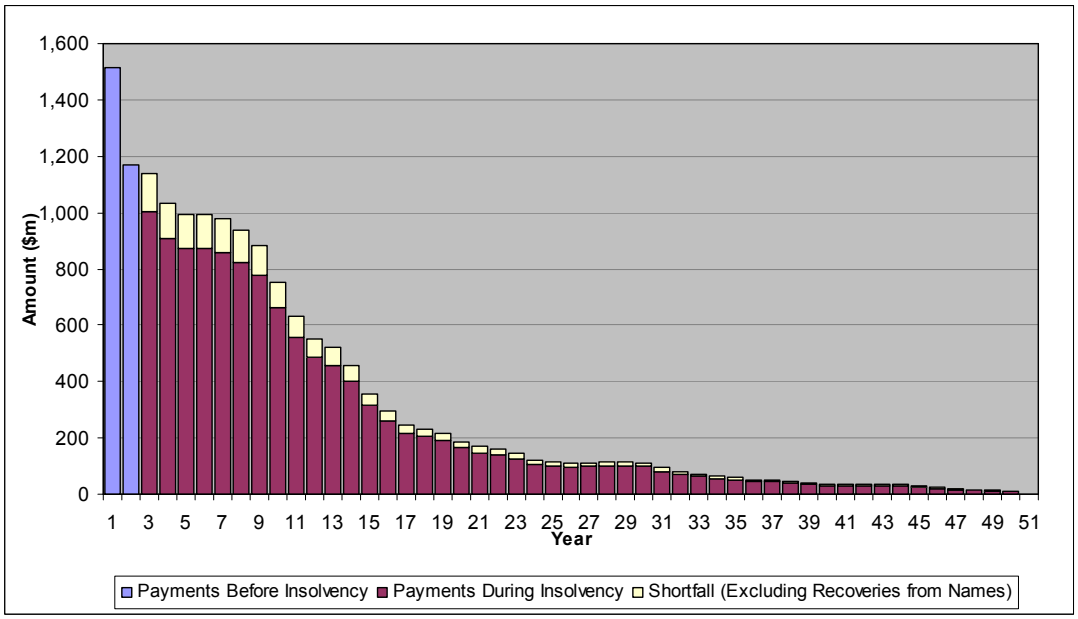


Figure 18-17 Undiscounted Claim Payments and Shortfall (Scenario) High Mean Assumption-In the Event of the Transfer Structure

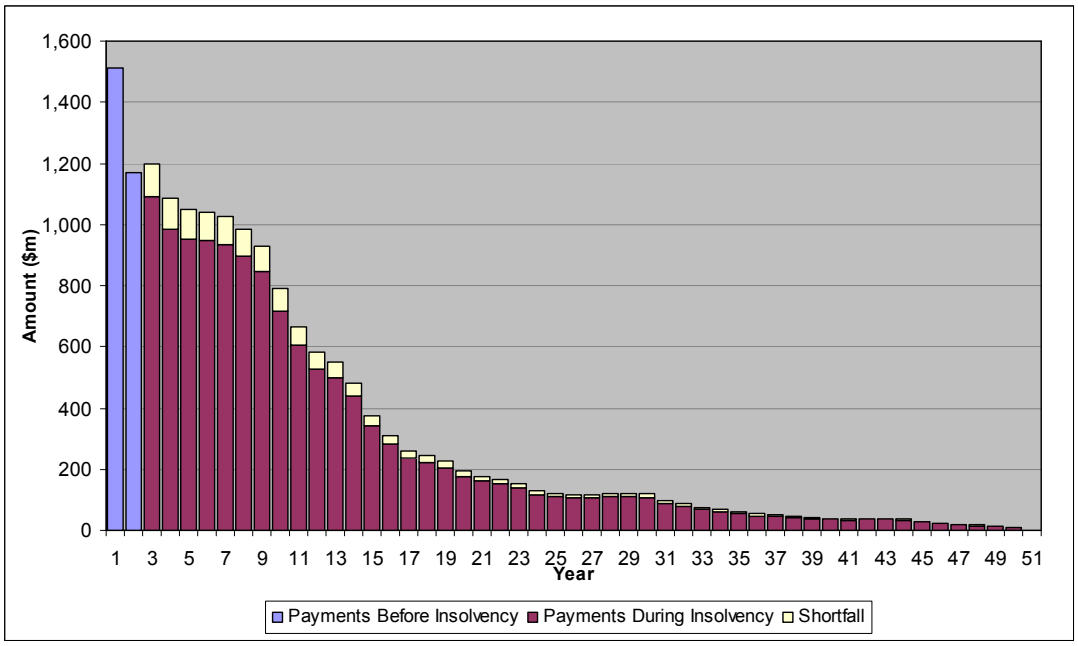


Figure 18-18- Key Statistics – High Variability Assumption

	Post	Pre
Insolvency Year	6	3

All Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	5,334	2,340
(2)	Unpaid at Insolvency	9,938	12,933
(3)	Ultimate Liability	15,272	15,272
(4)	**Insolvency Dividend Rate (%)**	**97.5%**	**92.4%**
(5)	Insolvency Dividend ($)	9,687	11,956
(6)	**Shortfall**	**251**	**977**
(7)	**Break Even Recovery Ratio**	**74.3%**	
(8)	Ultimate Paid	15,021	14,295
(9)	**Ultimate Payout**	**98.4%**	**93.6%**

Reinsurance Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	2,504	1,097
(2)	Unpaid at Insolvency	4,553	5,961
(3)	Ultimate Liability	7,057	7,057
(4)	**insolvency Dividend Rate (%)**	**97.0%**	**92.4%**
(5)	insolvency Dividend ($)	4,416	5,510
(6)	**Shortfall**	**137**	**450**
(7)	**Break Even Recovery Ratio**	**69.5%**	
(8)	Ultimate Paid	6,920	6,607
(9)	**Ultimate Payout**	**98.1%**	**93.6%**

Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	2,830	1,243
(2)	Unpaid at Insolvency	5,385	6,972
(3)	Ultimate Liability	8,215	8,215
(4)	**Insolvency Dividend Rate (%)**	**97.9%**	**92.4%**
(5)	Insolvency Dividend ($)	5,273	6,445
(6)	**Shortfall**	**112**	**527**
(7)	**Break Even Recovery Ratio**	**78.6%**	
(8)	Ultimate Paid	8,102	7,688
(9)	**Ultimate Payout**	**98.6%**	**93.6%**

Long Tail Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	-	-
(2)	Unpaid at Insolvency	7.3	7.3
(3)	Ultimate Liability	7.3	7.3
(4)	**Insolvency Dividend Rate (%)**	**97.9%**	**92.4%**
(5)	Insolvency Dividend ($)	7.2	6.8
(6)	**Shortfall**	**0.2**	**0.6**
(7)	**Break Even Recovery Ratio**	**72.3%**	
(8)	Ultimate Paid	7.2	6.8
(9)	**Ultimate Payout**	**97.9%**	**92.4%**

Figure 18-19 Estimated Ultimate Liability and Total Assets Plus Claims to Date (Scenario)- High Variability Assumption

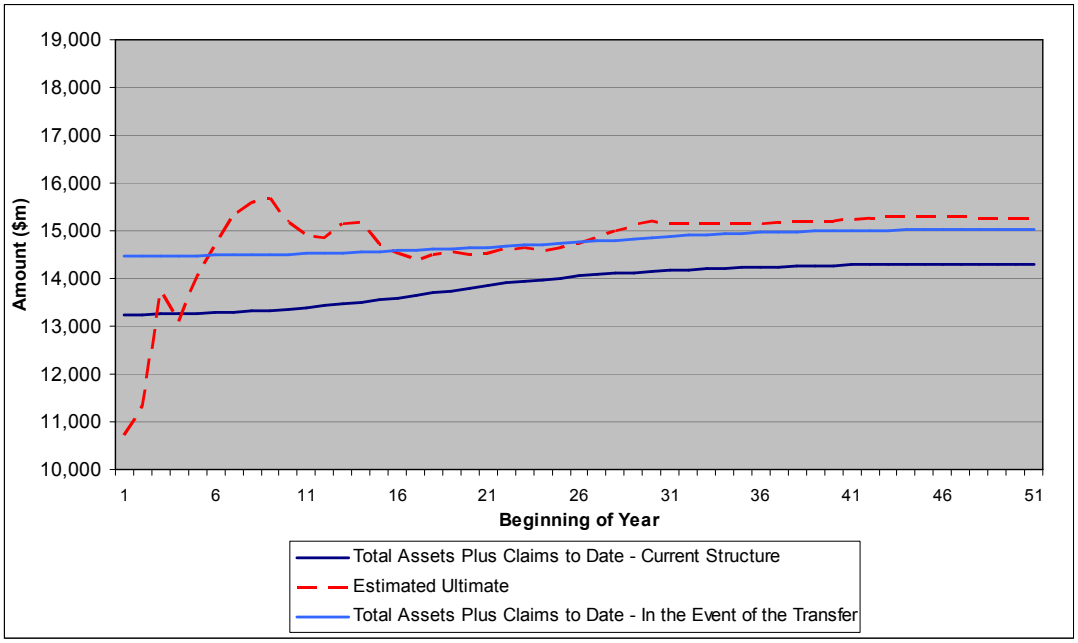


Figure 18-20 Undiscounted Claim Payments and Shortfall (Scenario) High Variability Assumption-Current Structure

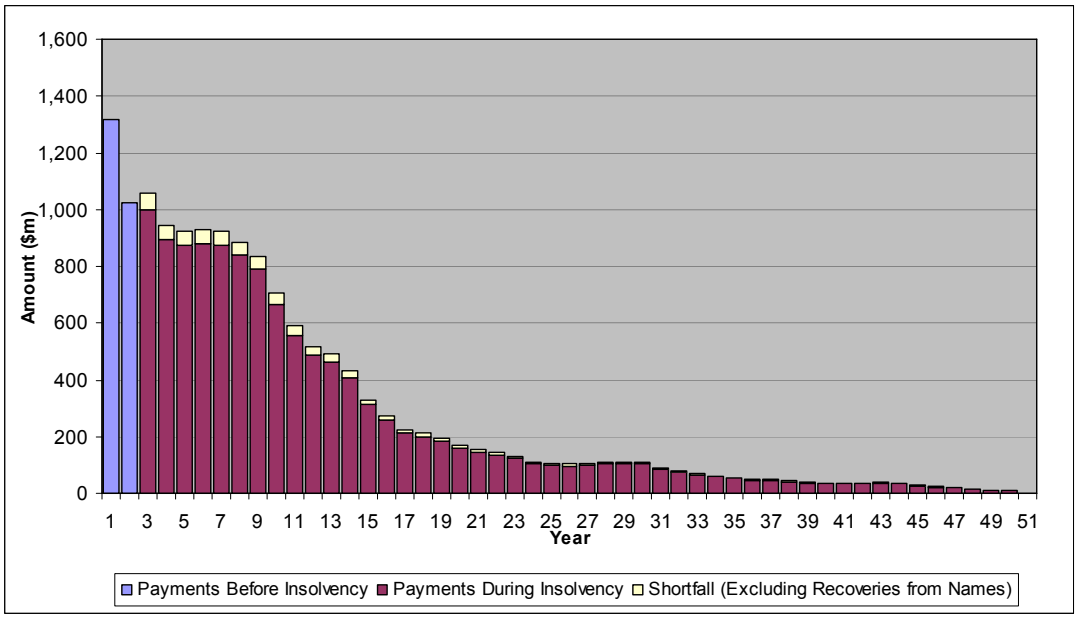


Figure 18-21 - Undiscounted Claim Payments and Shortfall (Scenario) High Variability Assumption-In the Event of the Transfer Structure

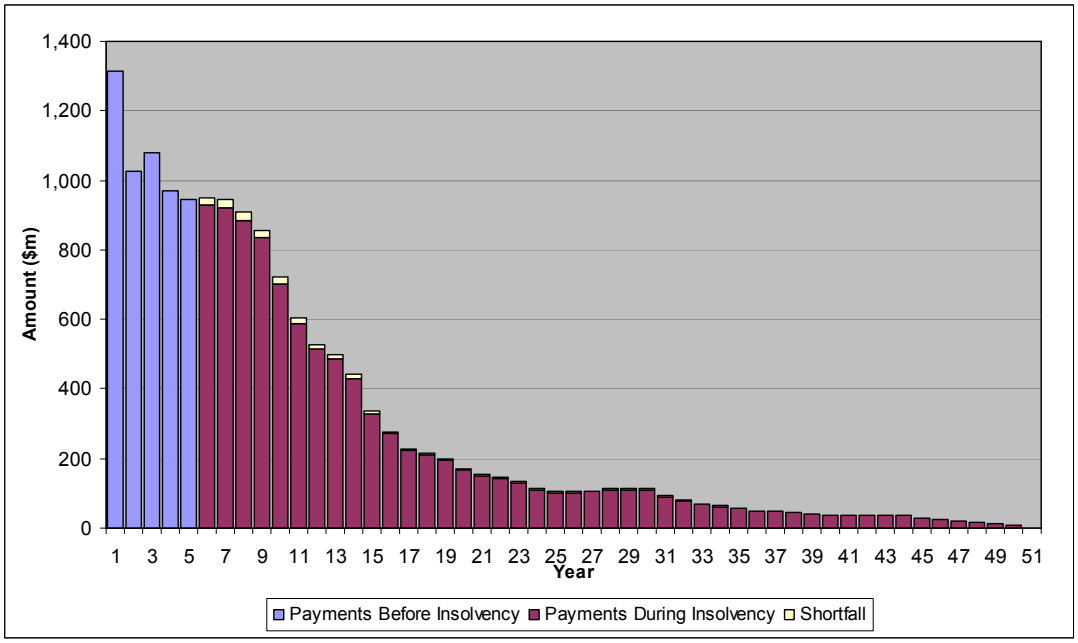


Figure 18-22- Key Statistics - High Mean, High Variability Assumption

	Post	Pre
Insolvency Year	3	2

All Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	2,807	1,577
(2)	Unpaid at Insolvency	15,519	16,749
(3)	Ultimate Liability	18,327	18,327
(4)	**Insolvency Dividend Rate (%)**	**84.3%**	**79.0%**
(5)	Insolvency Dividend ($)	13,076	13,237
(6)	**Shortfall**	**2,443**	**3,513**
(7)	**Break Even Recovery Ratio**	**30.4%**	
(8)	Ultimate Paid	15,883	14,814
(9)	**Ultimate Payout**	**86.7%**	**80.8%**

Reinsurance Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	1,316	771
(2)	Unpaid at Insolvency	7,153	7,698
(3)	Ultimate Liability	8,469	8,469
(4)	**Insolvency Dividend Rate (%)**	**84.0%**	**79.0%**
(5)	Insolvency Dividend ($)	6,006	6,084
(6)	**Shortfall**	**1,146**	**1,614**
(7)	**Break Even Recovery Ratio**	**29.0%**	
(8)	Ultimate Paid	7,322	6,854
(9)	**Ultimate Payout**	**86.5%**	**80.9%**

Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	1,491	807
(2)	Unpaid at Insolvency	8,366	9,051
(3)	Ultimate Liability	9,858	9,858
(4)	**Insolvency Dividend Rate (%)**	**84.5%**	**79.0%**
(5)	Insolvency Dividend ($)	7,071	7,153
(6)	**Shortfall**	**1,296**	**1,898**
(7)	**Break Even Recovery Ratio**	**31.7%**	
(8)	Ultimate Paid	8,562	7,960
(9)	**Ultimate Payout**	**86.9%**	**80.7%**

Long Tail Direct Policyholders

Line		Post	Pre
(1)	Paid before Insolvency	-	-
(2)	Unpaid at Insolvency	8.8	8.8
(3)	Ultimate Liability	8.8	8.8
(4)	**Insolvency Dividend Rate (%)**	**84.5%**	**79.0%**
(5)	Insolvency Dividend ($)	7.4	6.9
(6)	**Shortfall**	**1.4**	**1.8**
(7)	**Break Even Recovery Ratio**	**26.2%**	
(8)	Ultimate Paid	7.4	6.9
(9)	**Ultimate Payout**	**84.5%**	**79.0%**

Figure 18-23- Estimated Ultimate Liability and Total Assets Plus Claims to Date (Scenario)- High Mean, High Variability Assumption

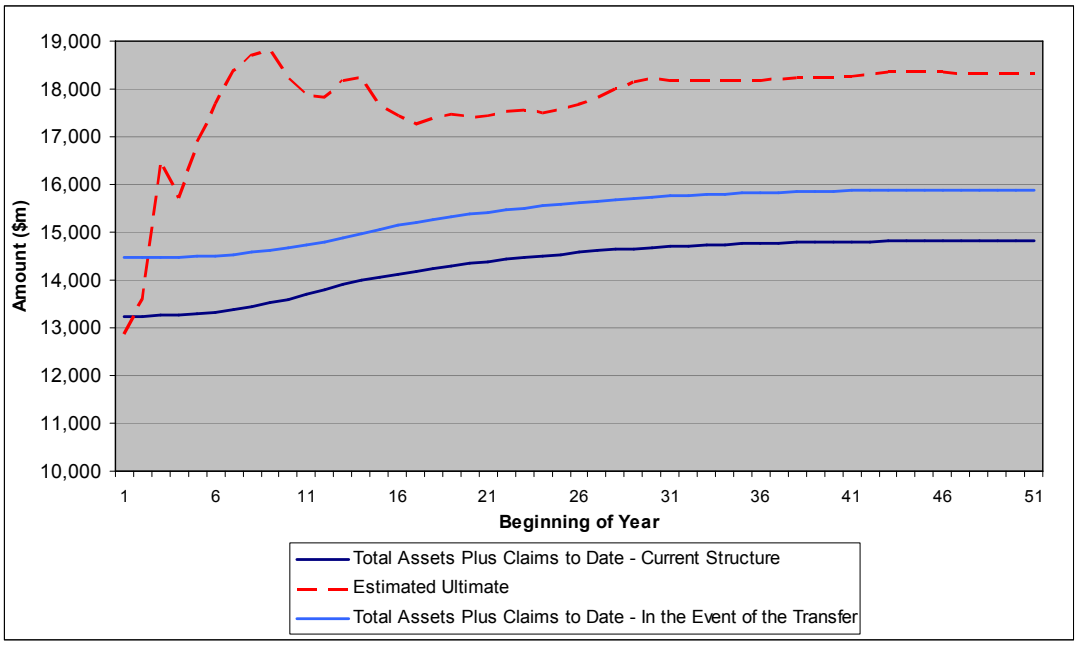


Figure 18-24 - Undiscounted Claim Payments and Shortfall (Scenario) High Mean, High Variability Assumption-Current Structure

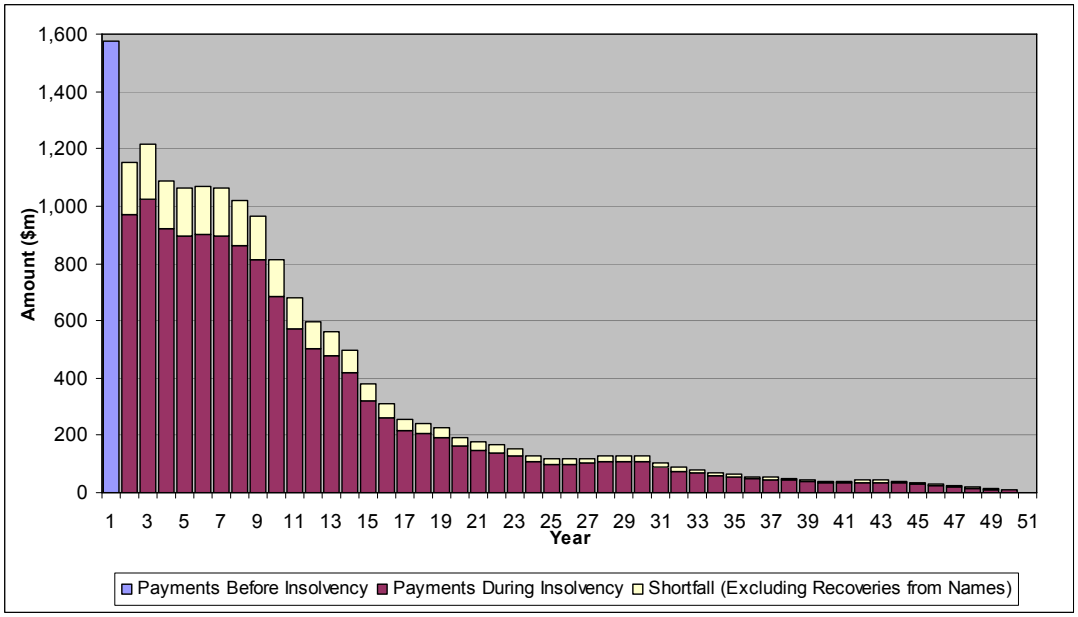
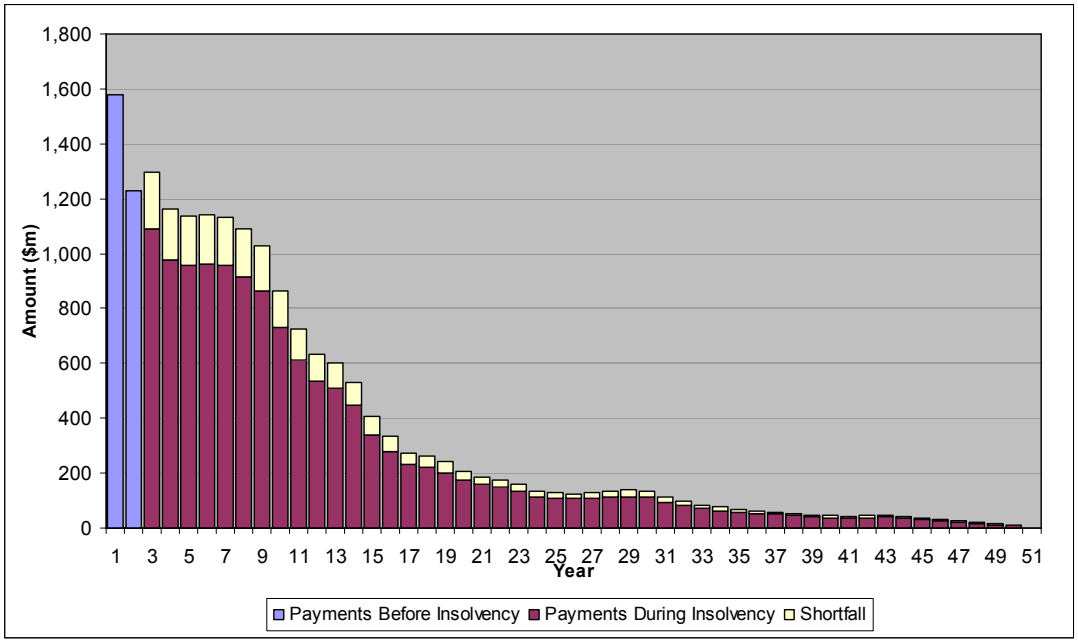


Figure 18-25- Undiscounted Claim Payments and Shortfall (Scenario) High Mean, High Variability Assumption-In the Event of the Transfer Structure



19 APPENDIX IX – COVERAGE MODEL- SHORTFALL HISTOGRAMS

19.1 INSOLVENCY DIVIDEND RATES AND SHORTFALLS

19.1.1 The following histograms show the distribution of shortfalls from the Coverage Model, before any additional recovery from Names. The results are shown for the following four liability assumption sets:

1. Base assumptions;
2. High mean assumption;
3. High variability assumption; and
4. High variability, high mean assumption.

19.1.2 The histograms for each liability assumption set show that:

1. The risk of an Equitas Insolvency of any given level of shortfall is smaller in the event of the Transfer than in the current structure.
2. In the base liability assumptions the risk of an Equitas Insolvency with a shortfall larger than $10bn is approximately 0.2% in the current structure, and 0.1% in the event of the Transfer.

Figure 19-1 Histogram of Shortfalls ($bn) Base Assumptions

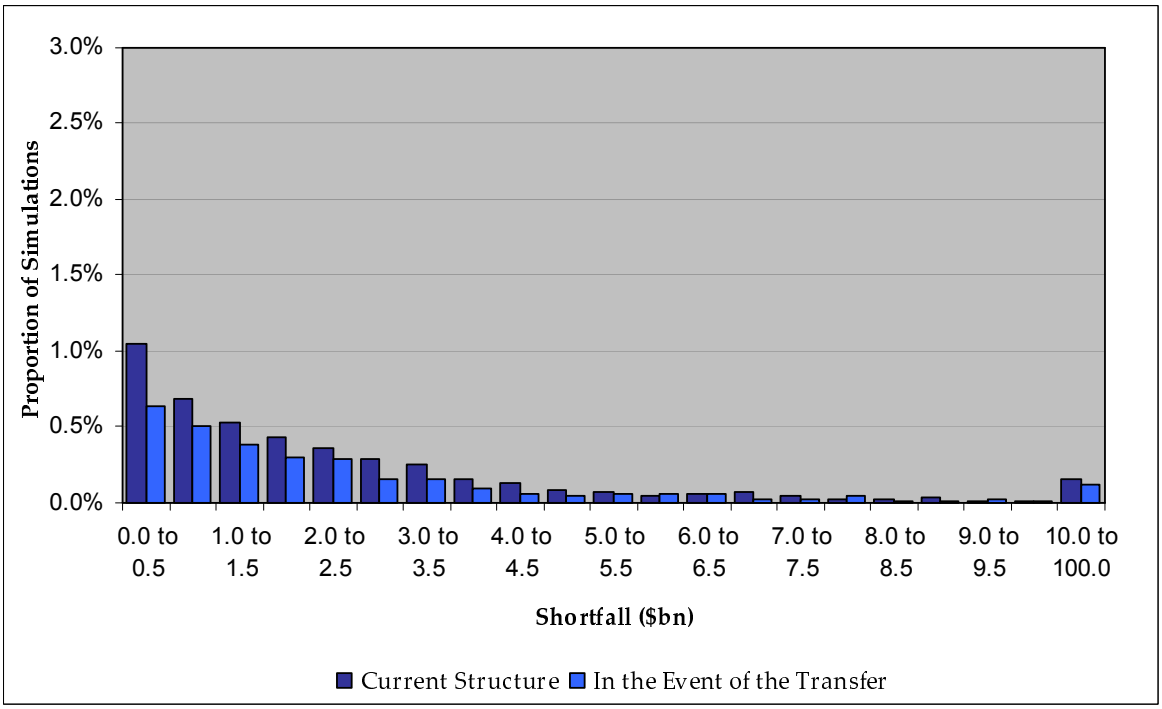


Figure 19-2 Histogram of Shortfalls ($bn) High Mean Assumptions

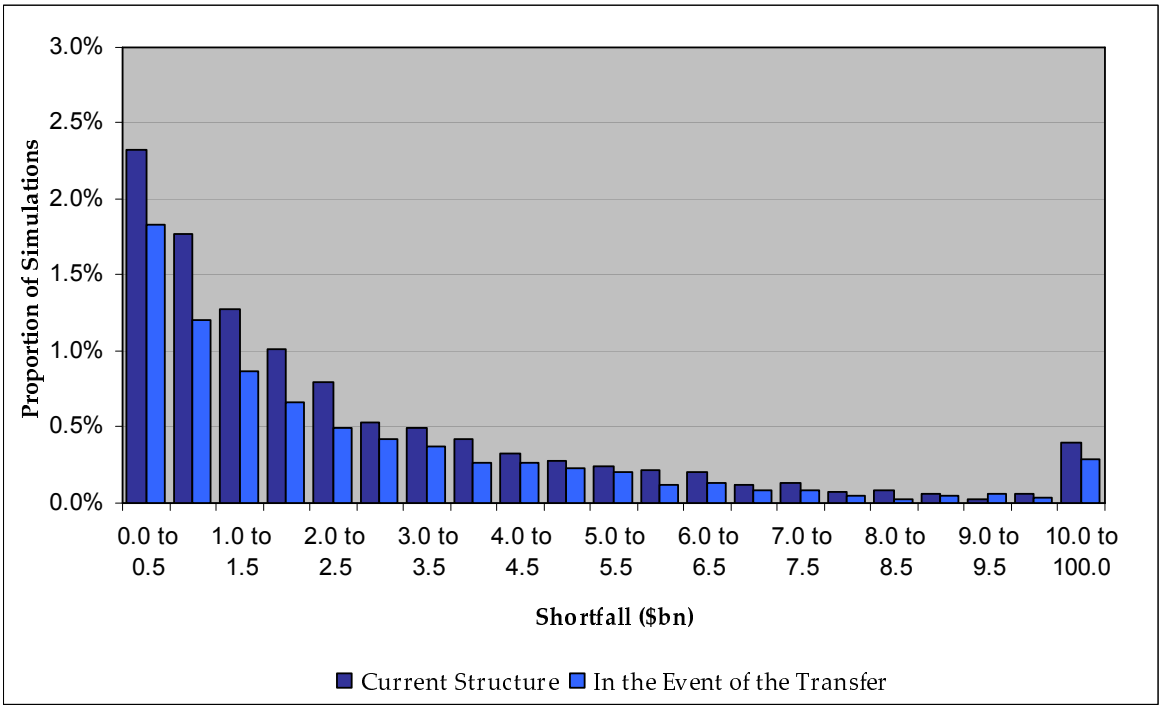


Figure 19-3- Histogram of Shortfalls ($bn) High Variability Assumptions

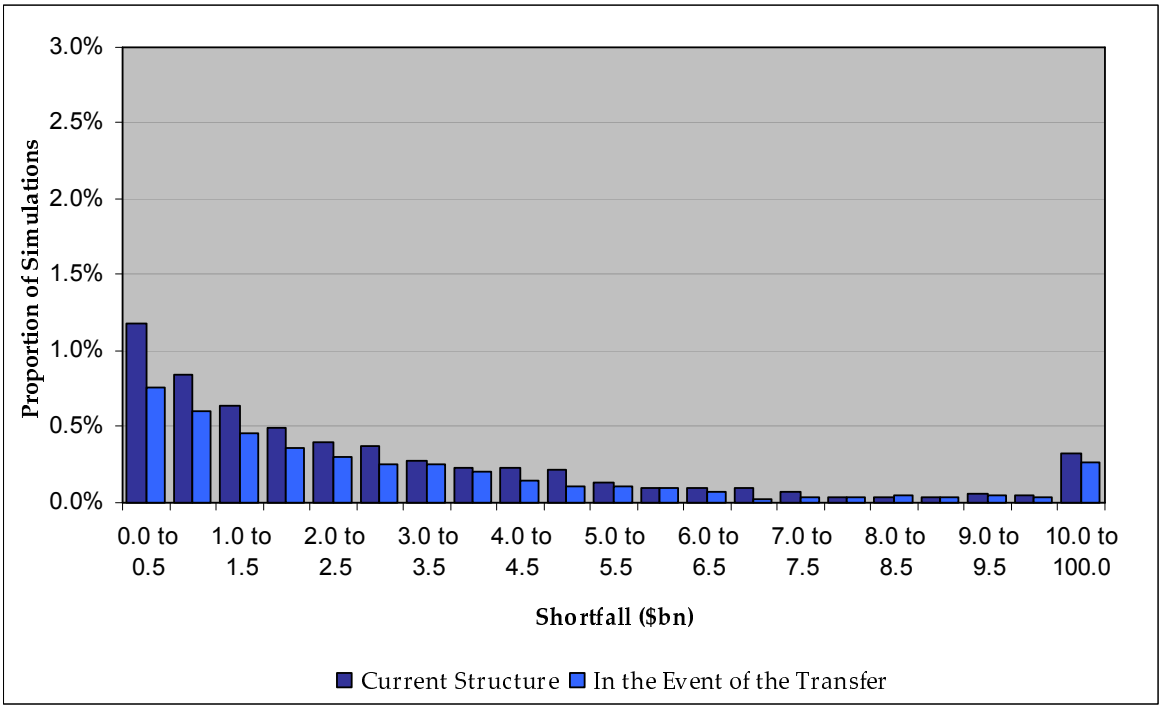
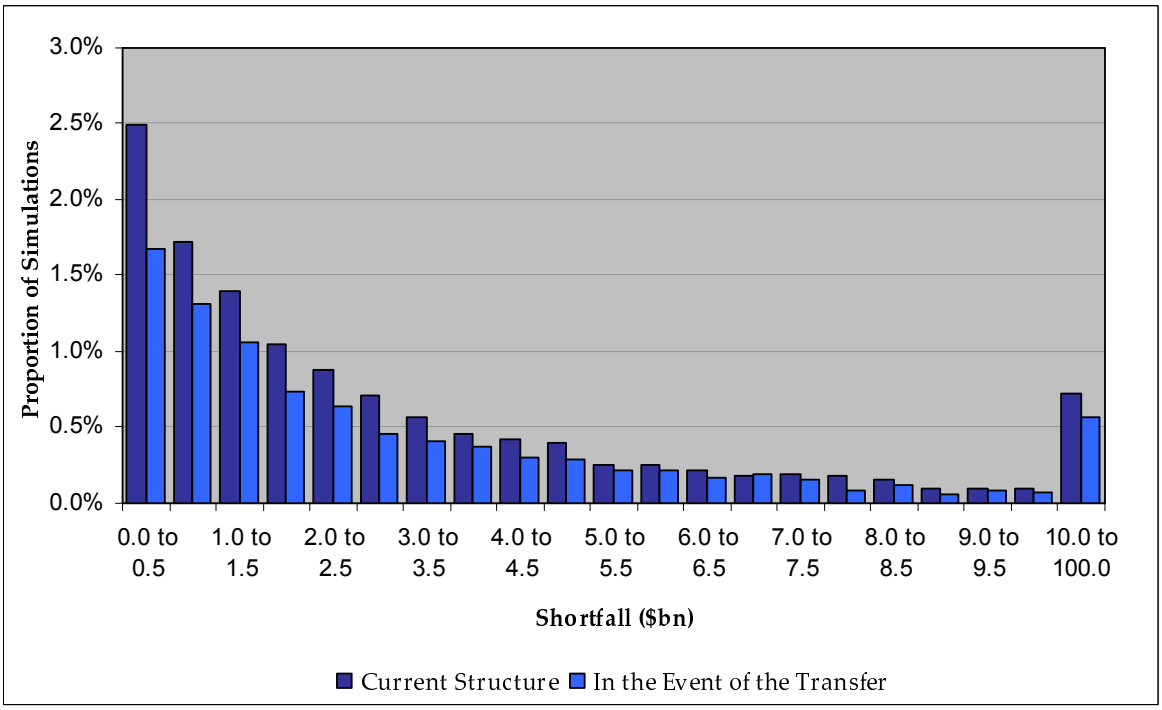


Figure 19-4- Histogram of Shortfalls ($bn) High Mean, High Variability Assumptions



20 APPENDIX X – MORTALITY MODEL – UNDERLYING ASSUMPTIONS AND METHODS

20.1 OVERVIEW OF MORTALITY MODEL

20.1.1 There are three data sources for the Mortality Model:

1. The Office for National Statistics (ONS) life table for England and Wales males, annual data from 1981 to 2006;
2. Anonymised Lloyd's data listing dates of birth and dates of death (when applicable) on of Open Year Names, collected at the time of the 1996 Equitas Reinsurance Contract and updated to the present, dates of birth and dates of death (when applicable); and
3. Historical records containing Lloyd's summary data on all Names membership from 1952 to 1993, by year, showing the number of active members, number of new elections, number of deceased members, and the number of members who have resigned. The model starts with the base Mortality table, overlaid with the estimated age distribution of the Names, and is further adjusted for observed Mortality of Names.

20.1.2 The model starts with the ONS life table, overlaid with the estimated age distribution of the Open Year Names, and adjusted to reflect the observed mortality experience of the Names.

20.1.3 The life table so derived is projected forward and the resulting Survival Rates are calculated. These average Survival Rates for each year in the future are estimated for Open Year Names. Additionally, by making assumptions regarding the change in age profile of Names over the years, estimated Survival Rates were obtained for Closed Year Names and RITC Names. These rates are then weighted against the expected time of insolvency to determine the final Survival Rate.

20.2 DATA LIMITATIONS

20.2.1 Data regarding Names did not include many factors that are often used in analysing Mortality, including:

1. Gender;
2. Socioeconomic class;
3. Geographic class; and
4. Health and lifestyle indicators.

20.2.2 There was incomplete correspondence between the data Lloyd's provided and the data collected by Equitas during, and since, the return premium distribution exercise of 2007:

1. Lloyd's data shows 6,150 deaths of Open Year Names through August 2008; and
2. Equitas data shows a higher number of deaths, 6,806 and we know that Equitas was unable to trace 5,182 Names, a number of whom are likely to have already died.

20.2.3 The methodology dealt with these limitations by calibrating the model based on observed Mortality data.

20.3 ADJUSTMENTS FOR OBSERVED MORTALITY

20.3.1 The Mortality table used was based on the ONS life table for England and Wales, for males from 1981 – 2006. For earlier years, it was assumed that the same Mortality rates as in 1981 would apply. This is prudent as there have been some significant improvements in Mortality during this time period.

20.3.2 It was necessary to make adjustments to the ONS Mortality table, for a number of reasons, including the expectation that Names should have a higher longevity than the average population, given their socioeconomic group. These adjustments include:

1. A scaling factor of 66.7% was applied uniformly to all Mortality rates (past, present and future). This scaling factor was selected by comparing the actual death of Names over the 1992-1996 period to the expected number of deaths in the same period;
2. An additional two year age rating adjustment was introduced, i.e. the Mortality rate corresponding to an individual two years younger was applied to each age. This further improved the fit between actual and expected deaths of Names over the 1992-1996 period.
3. An adjustment was made to the assumed age profile for earlier Years of Account to reflect the large influx of new Names between 1977 and 1993, which is believed to have led to a younger age distribution in the 1977-1992 period;
4. A small adjustment was also made to reflect the fact that 5% of Open Year Names had already died by the end of 1992. Years 1988 – 1991 were also adjusted to account for the likelihood of the effect on those years;

20.3.3 The Mortality Model, after these adjustments have been applied, fits well to the observed Mortality data.

20.3.4 In estimating future Survival Rates, future reductions in Mortality were allowed for by adopting 'medium cohort'[93] improvement rates, subject to a minimum rate of improvement of 1.5% per annum;

20.3.5 It was assumed that the age distribution produced by the calibrated approach is an appropriate starting point going forward.

[93] This is a standard set of Mortality improvement rates used by the UK Actuarial Profession.

20.4 RESULTS AFTER ADJUSTMENTS

20.4.1 After taking adjustments into account, the model estimated 26,207 surviving Names as of 2008, which implies 7,829 deaths of Open Year Names.

20.4.2 Paragraph 20.2.2 shows that this is higher than the number of deaths in the Lloyd's database. However, the Equitas data shows a higher number of deaths than Lloyd's, as well as many Names which were not traceable, and the proportion of deaths amongst the 'untraceable' Names implied by the model is actually lower than the proportion of known deaths for the Names that could be located.

20.4.3 The average age of projected surviving Names as of 2008 is about half a year younger than the average age of Names shown as alive in the Lloyd's dataset.

20.4.4 Before including the effect of future Mortality improvements, the adopted adjustments add over four and a half years to the (period) life expectancy of a 68 years old compared to the original ONS table (from 15.5 years to 20.2 years), and five and a half years to the life expectancy of a 55 years old (from 25.9 years to 31.4 years). Including Mortality improvements, the longevity increases are even higher.

20.4.5 For these reasons, I consider the model to provide a reasonable, if not prudent, estimate of Mortality.

20.5 Assumptions For Year of Account Weights and Calendar Year Weights

20.5.1 After the Survival Rates are determined by Year of Account and for each future year, weights need to be determined to approximate the average effect of Mortality.

Year of Account Weights

20.5.2 The approach used directly gives the weighted result for Open Year Names.

1. Original Year Names – The number of Names by each Year of Account are approximated using the distribution of carried reserves by Year of Account;
2. Any Year of Account in the RITC Chain – These weights were approximated based on the number of effective resignations by Year of Account.

Calendar Year Weights

20.5.3 The risk of an Equitas Insolvency occurring in any future year was taken into account by weighting together the time of insolvency and the amount of insolvency from the Liability Model. This was reviewed for the average Policyholders, as well as the long duration Direct Policyholders. The timing for the long duration direct Policyholders is longer since a later insolvency would significantly affect them more than the average Policyholder.

20.6 MODEL OUTPUT

20.6.1 Projected Survival Rates for the Names on the original Years of Account have been combined with selected reserve weights for the various Years of Account and with the weighted distribution of insolvency years.

20.6.2 Table 20-1 below summarizes the weighted estimates both assuming that Policyholders are only able to claim from Names alive at the time of insolvency and assuming that claims can also be made against estates of Names deceased up to six years before the time of insolvency.

Table 20-1
Weighted Survival Rates Results for Average Policyholder

	Avg Year of Insolvency	Avg Year Less 6 Years
Original Year of Account Names	28.3%	36.4%
Open Years' Names	61.7%	71.5%
Any Year of Account in RITC Chain	67.1%	77.9%
Open Years Names – Long Direct	49.7%	60.0%
Original Year of Account Names – Long Direct	21.0%	28.0%

Note: Average year of insolvency (weighted by shortfall) is the end of 2017 for the average Policyholder

21 APPENDIX XI – RECOVERY RATE ANALYSIS – FRAGMENTATION, POLICYHOLDER EXPENSES, & SETTLEMENT

21.1 DETAILS OF ANALYSIS

21.1.1 This Appendix details my analysis of the costs associated with Fragmentation, Policyholder expenses, and settlements, as it relates to the Policyholder's Recovery Rate in the event of an Equitas Insolvency. As described in section 5.4, this methodology assumes that the effects of these issues will be different for large claims against Names than for small claims against Names.

21.1.2 This section assumes Policyholders work together to pursue claims against Names. Section 21.4 discusses the possibility that a large Policyholder could work on their own.

21.1.3 For the entire analysis outlined below, I have utilized the shortfall scenarios (described in Appendix IX). For each scenario, I have calculated the resulting recovery after effects of Fragmentation, Policyholder expenses and settlements. Then I have used the average amount across all scenarios as my selected Recovery Rate.

Large Claims Against Names

21.1.4 To determine the settlement cost for settling large claims, I first estimated the percentage of claims to Names with liabilities that are larger than £250,000. For each shortfall scenario, I approximated the number of Names that would have claims above £250,000 and also the amount of the total shortfall that those Names represented.[94] I took the average of this shortfall and divided it by the average of the total shortfall for all Names to determine the percentage of claims that are associated with large claims against Names.

21.1.5 I assumed that these claims would settle for 75% of their total amount, resulting in a loss of 25% on settlement.

21.1.6 Under the base assumptions, the results of this calculation are provided in the tables below:

Table 21-1
Average Split Between Large Claims and Small Claims

Item		Amount (£m)
(1)	Large Claims - Amount Above Threshold	334
(2)	Small Claims - Amount Below Threshold	1,096
(3)	Total Average Shortfall = (1) + (2)	1,430

Note: Average Shortfall, at Base Assumptions Equals £1,430m

[94] The Equitas Reinsurance Contract premium for each Name is used as a proxy for the distribution of the expended liabilities of Names.

Table 21-2
Settlement Cost on Large Claims to Names

Item		Value
(1)	Large Claims - Amount Above Threshold, £m	334
(2)	Settlement Cost	25%
(3)	Uncollected Claims - Settlement on Large Claims = (1) * (2), £m	84

21.1.7 I have assumed no effect of Fragmentation on large claims against Names.

Small Claims Against Names

Claims Recoverable after Ten Years Delay

21.1.8 For small claims against Names, I assumed that some would be too small for it to be economical for the Policyholder to pursue a recovery from the Name after the first ten years delay. These would be claims where the expected payment in the first ten years is less than £30,000 (the minimum claim level of £20,000 plus the fixed expenses of £10,000). The amount of these claims is calculated for each scenario, approximating the share of the Names in the same way that was done in paragraph 21.1.4 above.

21.1.9 The result of this analysis is summarized in the table below.

Table 21-3
Effect of Fragmentation over Time for Small Claims to Names - Years 1-10

Item		
(1)	Small Claims - Amount Below Threshold, £m	1,096
(2)	% Due in Years 1-10	46%
(3)	Amount Due in Years 1-10 = (1) * (2), £m	504
(4)	Amount Due in Years 1-10, £m	504
(5)	Uncollected Claims - Amount Below Threshold, £m	218
(6)	Amount Collected in Years 1-10 = (4) - (5), £m	287
(7)	Amount Collected in Years 1-10, £m	287
(8)	Amount Due in Years 1-10, £m	504
(9)	Percentage Collected in Years 1-10 = (7) / (8)	57%

21.1.10 I assume that 46% of claims would be due in the first 10 years, based on the expected insolvency payout pattern. Of these claims, 57% would be collected, after removing claims too small to pursue.

Claims Recoverable 11-45 Years after Insolvency

21.1.11 For the remaining small claims, I assumed that these would settle for an average of:

1. The percent recovered in the first ten years; and
2. The amount that the Policyholders could recover if they billed for claims to Names every five years until no payments were left outstanding.

21.1.12 To determine this Recovery Rate, I performed a similar analysis as that which is described in paragraph 21.1.8, for each five year period. The results of this analysis are shown in Table 21-4 and Table 21-5 below, using the base liability assumptions.

Table 21-4
Effect of Fragmentation Over Time for Small Claims to Names

Years	Payout Pattern	Total for Small Claims (£m)	Uncollected (£m)	Amount Collected (£m)	Collected, as % of Small
1 - 10	46.0%	504	218	287	57%
11 - 15	16.0%	175	155	20	11%
16 - 20	12.0%	132	132	-	0%
21 - 25	9.0%	99	99	-	0%
26 - 30	7.0%	77	77	-	0%
31 - 35	5.5%	60	60	-	0%
36 - 40	4.0%	44	44	-	0%
41 - 45	0.5%	5	5	-	0%
Subtotal, Years 11 - 45	54.0%	592	572	20	3%
Total	100.0%	1,096	790	307	28%

Table 21-5
Recoveries after Effect of Settlement & Fragmentation on Small Claims to Names, Years 11-45

Item	Description	Value
(1)	Total Due on Small Claims, Years 11 - 45	£592m
(2)	Percentage Collected in Years 11 - 45	3%
(3)	Total Collected in Years 11 - 45	£20m
(4)	Total Due on Small Claims, Years 11 - 45	£592m
(5)	Percentage Collected in First 10 Years	57%
(6)	Years 11 - 45, Assuming Same Collectible % in First 10 Years	£337m
(7)	Recoveries on Claims Years 11 - 45	£178m

Notes

(1),(2),(4),(5) are from Table 21-3

(3) = (1) * (2)

(6) = (4) * (5)

(7) = Average of (3) & (6)

Total Recovery for Small Claims to Names

21.1.13 The total recoverable for small claims to Names is summarized in the table below.

Table 21-6
Effect of Fragmentation & Settlement for Small Claims to Names

Item		Amount
(1)	Total Collected in First 10 Years	£287m
(2)	Total Collected in Years 11 - 45	£178m
(3)	Total Collected, All Years = (1) + (2)	£465m
(4)	Total Small Claims to Names	£1,096m
(5)	Total Collected on Small Claims to Names	£465m
(6)	Total Uncollected on Small Claims to Names = (4) - (5)	£631m

Amount of Fixed Policyholder Expenses

21.1.14 I assumed a fixed Policyholder expense equal to £10,000 for each of the Names that are pursued. After the first 10 years, all claims are assumed to be settled, as described earlier in this section. I estimated the number of Names that are not too small to pursue (above £30,000 recovery in the first 10 years) using the same methodology described in paragraph 21.1.4. This number includes both large and small claims against Names. This figure is then multiplied by £10,000 to

determine the total fixed Policyholder expenses. The result of this analysis is shown in the table below:

Table 21-7
Fixed Policyholder Expenses

Item		Amount
(1)	Number of Names Pursued	6,078
(2)	Expense per Name	£10,000
(3)	Total Expenses = (1) * (2)	£61m

Overall Results

21.1.15 The summary of these results is shown below.

Table 21-8
Results of Fragmentation Analysis

Collection	Amount (£m)	Percentage of Total
Uncollected Portion of Large Claims- Settlement Cost	84	6%
Uncollected Portion of Small Claims- Settlement/Fragmentation Cost	631	44%
Fixed Policyholder Expenses	61	4%
Total Uncollected Due to Settlement, Fragmentation, and Policyholder Expenses.	776	54%

21.2 SENSITIVITY ANALYSIS

21.2.1 The results of the analysis described in section 21.1 are sensitive to the assumptions that I have selected. I have tested the sensitivities of these results in the following ways:

1. Fixed Policyholder Expense – This is the cost to the Policyholder associated with pursuing each Name. I assumed that this would be £10,000 over 10 years, and have also tested the assumption that this would be £5,000 over 10 years and £5,000 over 5 years;
2. Minimum Claim Level Pursued – This is the minimum recovery amount where it would be considered worthwhile to pursue a claim to a Name. I assumed that this would be £20,000, and have tested changing this assumption to £10,000 and £30,000;
3. Time Delay After Insolvency – I assumed that there would be a ten year delay from the time of Insolvency before the first payments are made to Policyholders. I have also tested the assumption that there would only be a five year delay;
4. Liability Assumptions – The calculations shown in section 21.1 assumes the base liability assumptions. I have also tested the calculation assuming the high mean, high variability, and high mean/high variability liability assumptions; and
5. Large Claim Threshold – This is the level that I consider large enough where the claim would be treated differently from others, and would likely end in settlement. I assumed that this would be £250,000.For the purpose of sensitive analysis, I have also tested my analysis assuming that a large claim would be £150,000.

21.2.2 The results of this sensitivity analysis are summarized in Table 21-9 and below, which show the total cost from Fragmentation, Policyholder expenses, and settlement cost.

Table 21-9
Total Cost - Fragmentation, Sensitivity Test Policyholder Expense & Settlement Cost

A. £5,000 Fixed Expense, 5 Year Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	47%	60%	69%
High Mean	45%	58%	68%
High Variability	42%	54%	63%
High/High	40%	53%	61%

B. £10,000 Fixed Expense, 10 Year Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	46%	54%	60%
High Mean	45%	53%	58%
High Variability	42%	49%	54%
High/High	41%	48%	53%

C. £5,000 Fixed Expense, 10 Year Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	38%	48%	56%
High Mean	37%	46%	54%
High Variability	34%	43%	50%
High/High	33%	42%	49%

Table 21-10
Sensitivity Test of Large Claim Threshold Total Cost – Fragmentation, Policyholder Expense & Settlement Delay
£20,000 Threshold, £10,000 Fixed Expense, 10 Years

Liability Assumption	£150,000	£250,000
Base	55%	54%
High Mean	53%	53%
High Variability	49%	49%
High/High	48%	48%

21.2.3 Table 21-9 and Table 21-10 results show that this calculation is especially sensitive to the minimum claim threshold chosen, and somewhat sensitive to the expense assumptions and liability assumptions. The final result is not very sensitive to the threshold for large claims. This is due to the fact that small

claims will have a much higher settlement cost when the threshold is lower, which is almost entirely offset by the fact that the number of large claims which would have a lower settlement cost increases.

21.2.4 The cost for Fragmentation, Policyholder expense, and settlements differ for the high variability/high mean assumption sets for a number of reasons:

1. Fewer claims are below the minimum claim threshold. This decreases the cost from Fragmentation;
2. Since fewer claims are below the minimum claim threshold, more Names are pursued. This increases the fixed Policyholder expenses; and
3. A larger proportion of claims are large claims. Large claims have a lower cost associated with Fragmentation and settlement, which decreases the total costs.

21.3 FIXED POLICYHOLDER EXPENSES

21.3.1 In order to assess the reasonableness of my assumptions on fixed Policyholder expenses, I have estimated fixed expenses in total for all Names. Under my assumptions detailed in paragraph 5.4.51, this results in total Policyholder expenses of £61m. I consider this amount to be a reasonable, if not prudent selection. I have also sensitivity tested this assumption, using the same sensitivity tests performed in section 21.2. The results of this analysis are shown in the Table 21-11 below.

Table 21-11
Total Policyholder Expense, £m

A. £5,000 Fixed Expense, 5 Year Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	35	19	12
High Mean	37	21	13
High Variability	42	25	17
High/High	44	27	18

B. £10,000 Fixed Expense, 10 Years Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	90	61	44
High Mean	94	65	47
High Variability	107	76	57
High/High	109	79	60

C. £5,000 Fixed Expense, 10 Years Delay

	Threshold		
Liability Assumption	£10,000	£20,000	£30,000
Base	56	37	26
High Mean	58	39	28
High Variability	65	45	33
High/High	66	46	34

21.4 LARGE POLICYHOLDER ANALYSIS

21.4.1 In sections 21.1-21.3, I discussed the situation if all Policyholders coordinate their efforts to pursue claims against Names. In this section I have considered the potential Recovery Rates for large Policyholders if they were to make claims against the Names individually.

21.4.2 I have kept the following assumptions the same for this scenario as I had made for the scenario where all Policyholders coordinate together:

3. *Policyholder Expense* – I assumed that there would be £10,000 fixed expenses;
4. *Time Delay After an Equitas Insolvency* – I assumed that there would be a ten year delay from the time of an Equitas Insolvency before the first payments made to Policyholders; and
5. *Settlement Cost to Large Claims* – This is the percentage that would be unrecoverable from large claims, due to settlement negotiations. I assumed this to be 25%.

21.4.3 I have made alternate assumptions for the following:

1. *Minimum Claim Level Pursued* – This is the level where it would be considered worthwhile to pursue a claim to a Name. I have assumed that this would be £5,000. This is lower than the amount for all Policyholders of £20,000 because it is not spread across multiple Policyholders;
3. *Large Claim Against a Name* – This is the level that I consider to be a claim large enough that it would be treated differently than others, and likely would result in settlement. I assumed that this would be £50,000. This is a smaller threshold, considering that this would only be one Policyholder, among many others, thus both parties would be eager to settle these large claims at a smaller threshold;
4. *Size of a Large Policyholder* – I have assumed that a large Policyholder would represent 5% of total liabilities. This has been selected by reviewing the Policyholders with the largest amount outstanding as of 31 August 2008. The 3 largest Policyholders each represented about 5% of the total liabilities; and
5. *Number of Names* – Only a certain percentage of the Names would be responsible for the claims of any one Policyholder. I assume a large Policyholder to have claims against 15% of the Names, or about 5,100 Names. I believe it would be larger than 5% (their share of the liabilities), because the largest Policyholders have numerous types of outstanding claims over a long period of time. Also as a reasonableness check, I know that the Dresser Policy buy-back settlement involved about 209 Syndicates, which under my assumption would be about 24 (5,100 divided by 209) Names per Syndicate. Considering that many Syndicates have hundreds of Names, this selection is prudent.

21.4.4 The results of this analysis are summarised below in Table 21-12, along with the results assuming all Policyholders coordinate together, for comparison.

Table 21-12
Results of Fragmentation Analysis

Collection	Cost for Large Policyholder	Cost for All Policyholders
Uncollected Portion of Large Claims- Settlement Cost	10%	6%
Uncollected Portion of Small Claims- Settlement/Fragmentation Cost	50%	44%
Fixed Policyholder Expenses	8%	4%
Total Uncollected Due to Settlement, Fragmentation, and Policyholder Expenses.	68%	54%

21.4.5 Table 21-12 above shows that a large Policyholder would recover more if it coordinated with other Policyholders.

21.5 RESULTS FOR TOTAL RECOVERY RATE

21.5.1 Table 21-13 and Table 21-14 show the results of this analysis on the total Recovery Rate, incorporating all of the collection issues detailed in section 5.

Table 21-13
Summary of Assumptions for Various Recovery Components

A. Collected Claims after Fragmentation ,Settlement and Fixed Policyholder Expenses

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	46%	46%	46%	34%	34%
High Variability	51%	51%	51%	38%	38%
High Mean	47%	47%	47%	36%	36%
High/High	52%	52%	52%	39%	39%

B. Death of Names

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	67%	32%	67%	55%	25%
High Variability	68%	33%	68%	57%	26%
High Mean	71%	36%	71%	63%	30%
High/High	72%	37%	72%	62%	30%

C. Delay

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	98%	98%	98%	98%	98%
High Variability	98%	98%	98%	98%	98%
High Mean	98%	98%	98%	98%	98%
High/High	98%	98%	98%	98%	98%

D. Bankruptcy/past and future

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	98%	98%	97%	98%	98%
High Variability	98%	98%	97%	98%	98%
High Mean	98%	98%	97%	98%	98%
High/High	98%	98%	97%	98%	98%

E. Locating Names

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	95%	95%	95%	95%	95%
High Variability	95%	95%	95%	95%	95%
High Mean	95%	95%	95%	95%	95%
High/High	95%	95%	95%	95%	95%

F. Variable Policyholder Costs

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	90%	90%	85%	90%	90%
High Variability	90%	90%	85%	90%	90%
High Mean	90%	90%	85%	90%	90%
High/High	90%	90%	85%	90%	90%

G. Recovery Rate from Names (Total)

	Type of Names				
Liability Assumption	Open	Original	RITC Chain	Open Long DIR	Original Long DIR
Base	25%	12%	23%	15%	7%
High Variability	29%	14%	27%	18%	8%
High Mean	28%	14%	26%	18%	9%
High/High	31%	16%	29%	20%	10%

21.5.2 The Recovery Rate, as it relates to Fragmentation, Policyholder expense and settlement issues, for long duration direct Policyholders differs when compared with all Policyholders on average. This is due to a number of reasons:

1. There would be fewer Names associated with the long duration Policyholders. This would increase the Recovery Rate;
2. These claims would be smaller, which would increase the effect of Fragmentation, and thus decrease the Recovery Rate; and
3. There are fewer Policyholders to spread across the cost of pursuing these Names. This would decrease the Recovery Rate.

21.5.3 For these reasons, I have selected the Recovery Rate to be 75% lower for long duration direct Policyholders than for all Policyholders on average

21.5.4 I have also calculated the total Recovery Rate results for each of the sensitivity tests described in Section 21.2. These results are shown in Table 21-14 below.

Table 21-14
Total Recovery Rate

A. £5,000 Fixed Expense, 5 Year Delay

	Threshold		
Liability Assumption	**£10,000**	**£20,000**	**£30,000**
Base	29%	22%	17%
High Mean	32%	24%	19%
High Variability	33%	26%	21%
High/High	35%	28%	23%

B. £10,000 Fixed Expense, 10 Year Delay

	Threshold		
Liability Assumption	**£10,000**	**£20,000**	**£30,000**
Base	29%	25%	22%
High Mean	32%	28%	24%
High Variability	32%	29%	25%
High/High	35%	31%	28%

C. £5,000 Fixed Expense, 10 Year Delay

	Threshold		
Liability Assumption	**£10,000**	**£20,000**	**£30,000**
Base	34%	28%	24%
High Mean	37%	31%	27%
High Variability	37%	32%	28%
High/High	39%	34%	30%

22 APPENDIX XII– TRUST FUND EXAMPLES (EATF)

22.1.1 This Appendix demonstrates the operation of the EATF, and examines the effect of the operation of this Trust Fund on Policyholders that are not covered by the EATF.

22.1.2 I discuss the two circumstances when the EATF becomes significant for the analysis of the Transfer. These are in the case of an Equitas Insolvency or a NICO Insolvency.

22.1.3 These examples discuss the EATF based on current EATF rules.

22.2 EATF EXAMPLES IN THE EVENT OF AN EQUITAS INSOLVENCY

22.2.1 Given the relative size of the USD exposure, an insolvency will likely be caused by an increase of USD claims, or an increase of all claims. An increase in non-USD claims alone would have to be extreme to cause an insolvency. Table 22-1 and Table 22-2, below, give example scenarios for the level of protection provided by the EATF for various levels of USD and non-USD liabilities.

22.2.2 The example in Table 22-1 shows the situation if the adverse development in liabilities is entirely due to an increase in USD liabilities.

22.2.3 The example in Table 22-2 shows the situation if the adverse development in non-USD liabilities is proportional to the adverse development in the USD liabilities

22.2.4 For simplicity, the examples assume that the ultimate liabilities are known, and insolvency, where there is one, is recognized immediately.

22.2.5 All figures in this section are net of reinsurance unless otherwise stated.

22.2.6 Table 22-1 and Table 22-2 have the following rows:

USD Liability excluding Lioncover - Row (1)

22.2.7 The EATF covers all Policies with premium or limits in USD, other than Lioncover. In Scenario A, the USD Liability excluding Lioncover is $5.8bn.

Lioncover - Row (2)

22.2.8 Lioncover liabilities are 8% of total liabilities. In Scenario A, these make up $0.6bn of the liabilities. They are assumed to be entirely USD dominated, however they are not covered by the EATF.

Non-USD Liability - Row (3)

22.2.9 In the example given in Table 22-1, non-USD liabilities are equal to $1.4bn in each scenario.

22.2.10 Table 22-2, non-USD liabilities are a fixed proportion of the Total Liabilities.

Total Liability - Row (4)

22.2.11 The total liability is the sum of the USD and non-USD liabilities. In Scenario A, I assume that the total liability is $7.8bn.

Available Limit - Row (5)

22.2.12 The available limit is the remaining NICO cover available at December 2008 ($13.1bn), plus the increased limit associated with the Transfer ($1.3bn). Equitas and Speyford Assets are ignored in this example.

Shortfall - Row (6)

22.2.13 The shortfall is the excess of the liabilities over the available limit.

EATF Assets as of December 2008 - Row (7)

22.2.14 The value of the EATF assets as of December 2008 is $2.8bn, including $0.2bn of reinsurance recoverable on paid claims.

Future value of EATF Assets - Row (8)

22.2.15 The future value of the EATF is $4.5bn, which includes investment income up to the point that claims are paid. This uses a future value factor of 1.6 times the current value.

Ceded RI on USD Claims - Row 9)

22.2.16 The ceded RI on USD claims is the amount of claims ceded by Equitas to reinsurers. Approximately 11% of liabilities are ceded on USD claims.

Gross EATF Share-Row (10)

22.2.17 The gross EATF share is the proportion of gross claims covered by the EATF that can be paid out of the EATF.

22.2.18 The gross EATF share is calculated as the future value of EATF assets, plus ceded RI on USD claims (the total amount available to meet EATF claims) divided by the USD Liability excluding Lioncover plus ceded RI on USD claims (the gross claims covered by EATF) ([(8) + (9)]/[(1) + (9)]).

Net EATF Share Row (11)

22.2.19 The Net EATF Share is the proportion of claims that can be paid by the EATF out of assets other than amounts received from reinsurance recoverables.

22.2.20 The Net EATF Share calculated using the following formula 1 – [1 – (10)]*(1 + Reinsurance percentage (11% of gross claims in this example))

22.2.21 This is the minimum dividend payment, in the event of an Equitas insolvency, for USD Policyholders.

Approximate Dividend Rate - Row (12)

22.2.22 The approximate dividend rate is an average insolvency dividend rate taken from the Coverage Model. This average is calculated over all insolvency scenarios that have a shortfall within £0.5bn of the shortfall in row (6). For example in Scenario C the Approximate Dividend Rate is equal to the average dividend rate for insolvency scenarios in the Coverage Model with a shortfall of between £0.5bn and £1.0bn.

22.2.23 If the insolvency dividend rate is greater than the net EATF share, then the dividend rate for USD Policyholders is equal to the dividend rate for all Policyholders.

Probability of Dividend Rate < Net EATF Share - Row (13)

22.2.24 This shows the probability, calculated using the Coverage Model, that the insolvency dividend rate is less than the net EATF share in row (11), given a shortfall less than or equal to the shortfall in row (6). In each scenario in these

examples the probability is less than 0.1%. For example in Scenario C this represents the probability that the dividend rate will be less than 32%, given a shortfall less than $1.0bn.

Table 22-1
EATF Example
Equitas Insolvency Due to USD Liability Deterioration ($bn)

Item		Scenario				
		A	B	C	D	E
(1)	USD Liability excluding Lioncover	$5.8	$13.0	$14.0	$18.0	$23.0
(2)	Lioncover	$0.6	$1.2	$1.2	$1.6	$2.0
(3)	Non-USD Liability	$1.4	$1.4	$1.4	$1.4	$1.4
(4)	Total Liability	$7.8	$14.4	$15.4	$19.4	$24.4
(5)	Available Limit	$14.4	$14.4	$14.4	$14.4	$14.4
(6)	Total Shortfall			$1.0	$5.0	$10.0
(7)	EATF Assets as of December 2008	$2.8	$2.8	$2.8	$2.8	$2.8
(8)	Future value of EATF Assets	$4.5	$4.5	$4.5	$4.5	$4.5
(9)	Ceded RI on USD claims	$0.6	$1.4	$1.6	$2.0	$2.6
(10)	Gross EATF Share	80%	41%	39%	32%	28%
(11)	Net EATF Share	78%	34%	32%	25%	19%
(12)	Approximate Dividend Rate	n/a	n/a	88%	67%	52%
(13)	Probability of Dividend Rate < Net EATF Share	n/a	n/a	0%	0%	0%

Table 22-2
EATF Example
Equitas Insolvency Due to USD and Non USD Liability Deterioration ($bn)

Item		Scenario				
		A	B	C	D	E
(1)	USD Liability excluding Lioncover	$5.8	$10.7	$11.4	$14.4	$18.1
(2)	Lioncover	$0.6	$1.2	$1.2	$1.6	$2.0
(3)	Non-USD Liability	$1.4	$2.6	$2.8	$3.5	$4.4
(4)	Total Liability	$7.8	$14.4	$15.4	$19.4	$24.4
(5)	Available Limit	$14.4	$14.4	$14.4	$14.4	$14.4
(6)	Total Shortfall			$1.0	$5.0	$10.0
(7)	EATF Assets as of December 2008	$2.8	$2.8	$2.8	$2.8	$2.8
(8)	Future value of EATF Assets	$4.5	$4.5	$4.5	$4.5	$4.5
(9)	Ceded RI on USD claims	$0.6	$1.2	$1.3	$1.6	$2.0
(10)	Gross EATF Share	80%	48%	45%	38%	32%
(11)	Net EATF Share	78%	42%	39%	31%	25%
(12)	Approximate Dividend Rate	n/a	n/a	89%	70%	57%
(13)	Probability of Dividend Rate < Net EATF Share	n/a	n/a	0%	0%	0%

22.2.25 In the examples above, the net EATF shares in the insolvency scenarios is under 45% of USD liabilities and generally under 35%. Those ratios are less than the insolvency dividend ratios to 'all Policies' in even the most extreme insolvencies.

22.2.26 In the base liability assumptions the risk of an Equitas Insolvency with a shortfall larger than $10bn (Scenario E) is approximately 0.2% in the current structure, and 0.1% in the event of a Transfer.

22.2.27 Thus, in the scenarios tested, the USD Policyholders are not in a better position than non-USD Policyholders due to the EATF, in respect of its operation in the event of an Equitas Insolvency.

22.3 EATF EXAMPLES IN THE EVENT OF A NICO INSOLVENCY

22.3.1 If NICO becomes insolvent, and NICO was unable to put a LOC in place, NICO will pay a dividend based on their liabilities to Equitas.

22.3.2 The following scenarios may then occur:

1. If the net EATF share is less than the 'all Policyholder' insolvency dividend rate, then all Policyholders are paid the 'all Policyholder' insolvency dividend rate;
2. If the future value of the EATF assets is less than the USD liabilities, but the net EATF share is greater than the 'all Policyholder' insolvency dividend rate, then USD Policyholders will receive a dividend rate, which is higher than the dividend rate for non-USD Policyholders; and
3. If the EATF assets are greater than the USD liabilities, the excess is paid to EL and is available to pay non-USD claims.

22.3.3 The examples in Table 22-3 and Table 22-4 assume that the adverse development in non-USD liabilities is proportional to the adverse development in the USD liabilities.

22.3.4 The example in Table 22-3 shows the situation if the NICO dividend rate is 50%.

22.3.5 The example in Table 22-4 shows the situation if the NICO dividend rate is 25%.

22.3.6 Table 22-3 and Table 22-4 have the following rows that are not in Table 22-1and Table 22-2:

NICO Dividend - Row (11)

22.3.7 The NICO dividend in Table 22-3 is equal to 50% of the NICO limit, or 50% of the total liabilities if they are less than the NICO limit.

22.3.8 In Table 21-4 the NICO dividend rate is 25%.

Dividend - all Policies - Row (12)

22.3.9 This row is the insolvency dividend rate that all Policyholders receive if the EATF share is less than the 'all Policyholder' dividend rate.

22.3.10 This dividend rate is equal to the NICO dividend plus the future value of EATF assets plus ceded RI on total claims (the total assets available to pay claims), divided by the total liability plus ceded RI on total claims (the total gross claims).

Dividend - USD Policies, EATF Alone - Row (13)

22.3.11 This row is equal to the insolvency dividend rate that USD Policyholders receive from the EATF, which is, equal to the net EATF share in row (10).

Table 22-3
EATF Example
NICO Insolvency with 50% NICO Dividend ($bn)

Item		Scenario				
		A	B	C	D	E
(1)	USD Liability excluding Lioncover	$5.8	$10.7	$11.4	$14.4	$18.1
(2)	Lioncover	$0.6	$1.2	$1.2	$1.6	$2.0
(3)	Non-USD Liability	$1.4	$2.6	$2.8	$3.5	$4.4
(4)	Total Liability	$7.8	$14.4	$15.4	$19.4	$24.4
(5)	Available Limit	$14.4	$14.4	$14.4	$14.4	$14.4
(6)	Total Shortfall			$1.0	$5.0	$10.0
(7)	EATF Assets as of December 2008	$2.8	$2.8	$2.8	$2.8	$2.8
(8)	Future value of EATF Assets	$4.5	$4.5	$4.5	$4.5	$4.5
(9)	Ceded RI on USD claims	$0.6	$1.2	$1.3	$1.6	$2.0
(10)	Net EATF Share	80%	48%	45%	38%	32%
(11)	NICO Dividend (at 50%)	$3.9	$7.2	$7.2	$7.2	$7.2
(12)	Dividend - all Policies	100%	81%	76%	60%	48%
(13)	Dividend - USD Policies, EATF alone	80%	48%	45%	38%	32%

Table 22-4
EATF Example
NICO Insolvency with 25% NICO dividend ($bn)

Item		Scenario				
		A	B	C	D	E
(1)	USD Liability excluding Lioncover	$5.8	$10.7	$11.4	$14.4	$18.1
(2)	Lioncover	$0.6	$1.2	$1.2	$1.6	$2.0
(3)	Non-USD Liability	$1.4	$2.6	$2.8	$3.5	$4.4
(4)	Total Liability	$7.8	$14.4	$15.4	$19.4	$24.4
(5)	Available Limit	$14.4	$14.4	$14.4	$14.4	$14.4
(6)	Total Shortfall			$1.0	$5.0	$10.0
(7)	EATF Assets as of December 2008	$2.8	$2.8	$2.8	$2.8	$2.8
(8)	Future value of EATF Assets	$4.5	$4.5	$4.5	$4.5	$4.5
(9)	Ceded RI on USD claims	$0.6	$1.2	$1.3	$1.6	$2.0
(10)	Net EATF Share	80%	48%	45%	38%	32%
(11)	NICO Dividend (at 25%)	$2.0	$3.6	$3.6	$3.6	$3.6
(12)	Dividend - all policies	82%	56%	52%	42%	33%
(13)	Dividend - USD policies, EATF alone	80%	48%	45%	38%	32%

22.3.12 The 'all Policyholder' insolvency dividend rate exceeds the EATF share in all of the examples shown above.

Conclusion

22.3.13 The operation of the EATF arrangements does not appear to materially disadvantage Policyholders that are not covered by the EATF in respect to its operation in the event of a NICO Insolvency, even if NICO has not purchased a LOC.

23 APPENDIX XIII– GLOSSARY OF TERMS

Table 23-1

Administration	A procedure under Part II of the Insolvency Act 1982 of England, Scotland, and Wales pursuant to which an administrator (an insolvency practitioner) is appointed to manage the business operations and affairs of a company.
Accepting Names	The Open Year Names who accepted the Lloyd's 1996 Settlement Offer under R&R (the vast majority of Open Year Names)
AM Best	Worldwide insurance rating and information agency.
APRA	Australia Prudential Regulation Authority.
Asbestos	Mineral that naturally occurs in the environment that can be separated into thin, durable threads that are resistant to heat, fire and chemicals and do not conduct electricity. Insurance liability usually arises from bodily injury caused by exposure to the fibres.
Assisted Names	Names with the benefit of a Lloyd's undertaking arising from a Hardship Agreement or similar Agreement.
Assisted Names Undertakings	Lloyd's undertakings to Assisted Names
Balance of Account	Claims that are not Asbestos, Pollution, Health Hazard or Catastrophe claims.
bn	Billion.
Catastrophe	Event that causes $25m or more in insured property losses and affects a significant number of property and casualty Policyholders.
Centrewrite	Centrewrite Limited, a company incorporated in England and Wales, a subsidiary of Lloyd's that reinsures the Warrilow Syndicate and various other Names with respect to 1992 and Prior Business.
Cedent	A Reinsurance Policyholder
Centrewrite Reinsurance Contract	The reinsurance contract whereby certain liabilities of Centrewrite are retroceded to ERL.
Closed Year Names	Names participating in a Closed Year Syndicate in their capacity as such.
Closed Year Policies	Policies underwritten by Syndicates for whom that particular Year of Account was subject to RITC.
Closed Year Syndicate	Any Syndicate which has been reinsured to close into another Syndicate, Centrewrite or Lioncover.
Connected Persons	Immediate family members and in respect of a company being a director of that company
Continuing Name	Name on the 1992 and Prior Business who continued as Lloyd's Name on 1993 and any subsequent Years of Account.
Contract Exchange Rate	The rate used in the NICO Retrocession Agreement to determine the level of coverage (£1 = $1.7372).
Coverage Model	An Actuarial Model used to estimate claims coverage generated by the Liability Model.

Compensation Act 2006	An act to specify certain factors that may be taken into account by a court determining a claim in negligence or breach of statutory duty; to make provision about damages for Mesothelioma etc.
Credit for Reinsurance	Insurers and reinsurers in the USA and certain other countries that are Lloyd's Policyholders, can record the full value o their estimates reinsurance recoveries for solvency reporting purposes because of, in part, regulatory arrangements supported by Trust Funds.
EATF	Equitas American Trust Fund (EATF) is a US trust fund available to protect direct and reinsurance polices reinsured under the Equitas Reinsurance Contract, with premium and limits in US dollars. Sometimes called the NICO American Trust Fund or NATF since the completion of the NICO Retrocession Agreement.
EL	Equitas Limited, a company registered in England and Wales, facilitating the Transfer on behalf of the Names. EL reinsures ERL. EL acts on behalf of the Transfer.
EHL	Equitas Holdings Limited, a company registered in England and Wales, which acts as the holding company to ERL, EL and EPTL.
EMSL	Equitas Management Services Limited, until 30 March 2007 a subsidiary of EHL. Sold to the Berkshire Hathaway group and renamed Resolute Management Services Limited (RMSL) in March 2007. Now acts as a run-off agent for the Names for the Equitas reinsured business.
EPD	The Expected Policyholder Deficit, average claim amount not paid (if any) as a percent of the total liability amount, assuming there is a shortfall.
EPP	Estate Protection Plan, a Policy written originally by Lloyd's Syndicates and, from 1993, by Centrewrite which covers cash calls on a Name's Open Years of Account in the event of a Name's death.
EPTL	Equitas Policyholders Trustee Limited, a company registered in England and Wales, part of the Equitas Group that would act as a channel through which funds would flow in the event of an Equitas Insolvency.
Equitas	When cited as a source of information means provided by EL staff or RMSL staff acting on behalf of EL.
Equitas Group	Equitas Limited, Equitas Reinsurance Limited, Equitas Holdings Limited and Equitas Policyholders Trustee Limited, formed in 1996 as part of Lloyd's Reconstruction and Renewal plan to reinsure the 1992 and Prior Business.
an Equitas Insolvency	The insolvency of any of the companies in the Equitas Group (including Speyford) having the effect that valid claims from Policyholders are not paid in full by funds from NICO, EL, ERL, EHL and Speyford.

Equitas Reinsurance Contract	The reinsurance contract entered into by ERL on 3 September 1996 (as subsequently amended) in which ERL agreed to reinsure and indemnify the Names in respect of the 1992 and Prior Business and was appointed by the Names to assume responsibility for the run-off of the 1992 and Prior Business.
Equitas Retrocession Agreement	The retrocession contract entered into by EL on 3 September 1996 (as subsequently amended) in which ERL retroceded to EL its liabilities under the Equitas Reinsurance Contract and Lioncover Reinsurance Contract and delegated to EL responsibility for the run-off of the business reinsured.
External Outwards Reinsurance	Reinsurance on 1992 and Prior Business to reinsurers other than Names, Lioncover, Centrewrite, ERL, EL or NICO.
ERL	Equitas Reinsurance Limited, a company registered in England and Wales.
EU Winding-Up Directive	Directive 2001/17/EC on reorganisation and winding up of insurance undertakings.
Fragmentation	The effect whereby claims are too small to be collected on an economical basis.
FSA	Financial Services Authority, the UK regulatory body in respect of financial institutions which regulates RMSL, EL, ERL, Lioncover and Centrewrite.
FSCS	Financial Services Compensation Scheme. The body that administers eligible claims made when an insurer is insolvent and unable to pay claims in full.
FSMA or "the Act"	Financial Services and Markets Act 2000;
Hardship Agreement	An agreement under the Lloyd's Hardship Scheme between Lloyd's and a Name who demonstrated that he was unable to meet his Lloyd's losses under which, inter alia, Lloyd's agreed to meet cash calls made on the Name in respect of syndicates in which he participated.
Health Hazard(s)	Various exposures that are hazardous to the health and well-being of individuals, giving rise to bodily injury insurance claims. Includes items such as: fumes from welding rods, tainted blood, pharmaceuticals and breast implants.
High Court	The High Court of Justice of England and Wales
Illinois Trust Fund	The Trust Fund established by ERL in Illinois to collateralise the reinsurance provided by ERL to Names licensed in Illinois in respect of the amount of their risk retentions on Illinois 1992 and Prior Business.
Independent Expert	The individual appointed and approved by the FSA to produce the Report on the terms of a Part VII business transfer.
Insurers (Reorganisation and Winding Up) Regulations 2004	Statutory Instrument No. 353 of 2004 on reorganisation and winding up of insurance undertakings.
ISR	Inter-Syndicate Reinsurance – Reinsurance contracts between Syndicates, including but not limited to RITC contracts.

JATF	Lloyd's Joint Asset Trust Fund, supports business transferred in this transaction and non-transferred business written by underwriting members of Lloyd's.
Joint Liability / Jointly Liable	Each party is liable up to the full amount of the relevant obligation. One or all parties can be sued for the full amount, but judgement against or release of one of them discharges all others who can, however, be sued for contribution by the one making payment so far as his payment exceeds his share.
Joint and Several Liability	Any party is liable up to the full amount of the relevant obligation. All or any of them can be sued for the entire amount and judgement against one does not discharge the others. It is up to that party making payment to pursue contribution from the other obligated parties for the amount paid by him that exceeds his share.
Joint Survival Rate	Probability of surviving Names from a group of Names who underwrote a RITC contract.
LATF	The Lloyd's American Trust Fund, the fund of premiums and other sums receivable in respect of 1992 and prior US dollar denominated business. There is a separate LATF for each underwriting member of Lloyd's.
Liability Model	An actuarial model used to simulate scenarios of the size and timing of Equitas claims liability.
Lioncover	Lioncover Insurance Company Limited, a company incorporated in England and Wales, a subsidiary of Lloyd's that reinsures liabilities of the PCW Names
Long-DIR	Long duration direct Policyholder
Lioncover Reinsurance Contract	The reinsurance contract whereby liabilities of Lioncover are retroceded to ERL .
Lloyd's	The Society incorporated by Lloyd's Act 1871 by the Name of Lloyd's of One Lime Street, London EC3M 7HA.
LMRO	Lloyd's Market Reorganization Order under the Insurers (Reorganisation and Winding Up) (Lloyd's) Regulations 2005.
LOC	Letter of Credit.
MCR	Minimum Capital Requirement.
Mesothelioma Claims	Claims arising from a rare cancer that is linked to exposure to Asbestos.
Mortality	Death rate among the Names.
Mortality Model	An Actuarial model used to estimate the Survival Rate of Names.
NAIC	National Association of Insurance Commissioners.
Names	Individuals who participated as underwriting members of Lloyd's through groupings known as Syndicates and acted as underwriters under rules specified by Lloyd's and who were reinsured directly or indirectly into ERL under R&R.
NATF	NICO American Trust Fund. See EATF
NICO	National Indemnity Company, a company incorporated in the State of Nebraska, USA (subsidiary of Berkshire Hathaway).

NICO Retrocession Agreement	The retrocession contract (as amended) entered into by NICO, EL, EHL and RMSL in which EL retroceded to NICO its liabilities under the Equitas Retrocession Agreement and delegated to RMSL responsibility for the conduct of the run-off of such business as sub-delegate of the Names.
Navigant	Navigant Consulting (Europe) Ltd and/or Navigant Consulting Inc.
Non-Transferring Policyholders	Policyholders of Names who underwrote 1992 and Prior Business and continued as Names in 1993 and subsequent years with respect to 1993 and subsequent years of business.
Open Year Names	Names participating in Open Year Syndicates in their capacity as such.
Open Year Policy	A Policy underwritten by Syndicates for whom that particular Year of Account was not subject to RITC (other than the reinsurance to close constituted by the Equitas Reinsurance Contract).
Open Year Syndicates	Syndicates that were unable to purchase reinsurance (RITC) in the ordinary course on a certain account year and remained 'open' beyond the normal 3 year period.
Original Year Names	Names in the Syndicate and Year of Account who originally underwrote the insurance.
Overseas Trust Fund	Trust funds in USA, Canada, Australia and/or South Africa.
OSFI	The Office of the Superintendent of Financial Institutions (Canada).
PCW EPTL Trust	PCW trust formed in the event of the Transfer
PCW Names	The underwriting members of Lloyd's comprising the PCW Syndicates in their capacity as such; this expression also includes WMD Names covered by the PCW Reinsurance Contract.
PCW Reinsurance Contract	The reinsurance contract in which Lioncover agreed to reinsure and indemnify the PCW Names in relation to all liabilities under Policies underwritten at Lloyd's through the PCW Syndicates.
PCW Syndicates	Each of the Syndicate Years of Account listed in schedule 3 to the Lioncover Reinsurance Contract.
Policy	A contract of insurance, describing the term, coverage, premiums and deductibles.
Policyholder	See Transferring Policyholder.
Pollution	Environmental contaminants often requiring environmental clean-up. These clean up costs are often covered under US insurance Policies.
PSL	Personal Stop Loss Policies, covers potential cash calls which might be made on Names in respect of Syndicates in which they participate.
Recovery Rate	Percent of otherwise uncollected claims paid by Names in the event of an Equitas Insolvency.

Reconstruction & Renewal (R&R)	The arrangements which led to the establishment of the Equitas Group and under which, amongst other things, ERL provided reinsurance to close with respect of the 1992 and prior years non-life obligations of the Names.
Regulated Activities Order	The FSMA (Regulated Activities) Order 2001 (Statutory Instrument Number 544/2001) relating to the regulation of financial services in the UK.
Report	This document is a Scheme Report as defined in section 109 of FSMA in respect of the Transfer.
RITC	Reinsurance to Close a particular Syndicate Year of Account. Typically, Syndicates reinsured to close after three years.
RITC Chain	The RITC from one Year of Account to another would include the reinsurance of RITC contracts from earlier years. This creates a chain of RITC contracts from Original Year Syndicates to Open Year Syndicates.
RITC Names	Those Names providing reinsurance under RITC contracts.
RMSL	Resolute Management Services Limited (formerly EMSL), a company registered in England and Wales, and is the entity that manages the run-off of the liabilities reinsured by ERL. Prior to March 2007 RMSL was EMSL.
S&P	Standard and Poor's, worldwide provider of independent credit ratings, indices, risk evaluation, investment research and data.
Scheme of Arrangement	A Scheme of Arrangement is a court-approved agreement between a company and its shareholders or creditors The relevant provisions for effecting a Scheme of Arrangement are found in the UK Companies Act 2006, Part 26 (ss.895-901) and Part 27.
Set-Off	The ability to net off debit and credit balances where there is a mutuality of dealings between two parties and one of the parties is in default with respect to meeting the obligations to the other party.
Several Liability	Parties are only liable for their respective share of an obligation.
Speyford	Speyford Ltd., obligations of the Names are being transferred to this new entity.
Solvency II	Solvency II is the proposed updated set of regulatory requirements for insurance firms that operate in the European Union.
Supplemental Report	An additional Report covering specific issues in relation to the proposed Transfer..
Survival Rate	Proportion of Names surviving to a specified date.
Syndicate	A group of underwriting members of Lloyd's (Names), with each member having a 'Several Liability' share of Policies underwritten.
Syndicate Year	Also Year of Account, one year venture of a Syndicates operation.

Transfer	The Transfer is the insurance business transfer scheme between EL acting on behalf of Names and Speyford as defined in section 105 of Part VII of the Financial Services and Markets Act 2000 (FSMA).
Transferee	Speyford Limited.
Transferor(s)	The Names are the Transferor(s)
Transferring Policies	All Policies written by or on behalf of any of the Names as insurer, reinsurer or retrocessionaire (including all supplement, endorsements and riders thereto and all ancillary agreements in connection therewith) comprised in the 1992 and Prior Business.
Trust Deeds	A formal document creating a trust, stating its objects, naming trustees and defining their powers and duties.
UK	The United Kingdom of Great Britain and Northern Ireland.
USD	United States Dollar
USD Policy	Policy covered by the EATF
Warrilow Names	The underwriting members of Lloyd's comprising Syndicate 553 as constituted for the 1985 or 1987 Years of Account in their capacity as such.
Warrilow Reinsurance Contract	The reinsurance contract entered into between Centrewrite and CJW (Underwriting Agencies) Ltd in which Centrewrite agreed to reinsure and indemnify the Warrilow Names in relation to liabilities under Policies underwritten by them.
Warrilow Syndicates	Syndicate 553 as constituted for each of the 1985 and 1987 Years of Account.
Warrilow EPTL Trust	Warrilow Trust, formed in the event of the Transfer.
Year of Account	One year venture of a Syndicate's operation. Also Syndicate Year.
ZAR	South African Rand.
$ or USD	US dollars unless otherwise stated (e.g. AUD or CAD).
The 1930 Act	Third Party (Rights Against Insurers) Act 1930
1992 and Prior Business	All liabilities under Policies underwritten at Lloyd's (other than life business) and originally allocated to the 1992 Year of Account or any earlier Year of Account including any such liabilities reinsured to close into the 1993 Year of Account or any later year of account, but excluding any liabilities re-signed, or re-allocated pursuant to a premium transfer, into the 1993 Year of Account or any later year of account.

24 APPENDIX XIV - FURTHER INFORMATION REQUIRED

24.1.1 There are areas where documentation at the date of this Report does not allow me to confirm certain aspects of my analysis. I have been asked to assume that the documentation will be provided in time to consider before the Court hearing and that the information will be consistent with my analysis and conclusions. To the extent that it is considered necessary I will address this documentation and any impact on the analysis in one or more supplemental reports

24.1.2 This documentation is as follows:

Speyford Authorisation and Equitas Group Capital Structure

1. Documentation for authorisation of Speyford (including the scope of its authorisation);
2. The manner in which capital is allocated among the Speyford, EL and EHL, and any undertakings to provide capital support among the companies;

Trust Funds

3. Reports on discussions, if any, with US regulators regarding the Credit for Reinsurance with respect to the Transferring Policies;
4. Reports on discussions, if any, with Australian or Canadian regulators regarding the Credit for Reinsurance with respect to the Transferring Policies;

Lloyd's

5. Lloyd's undertaking and bonds (including provisions that are enforceable by Policyholders);
6. Confirmation of data attributed to Lloyd's in the Report; and
7. Lloyd's other confirmations described in section 3.3.28.