

Scheme Report

For the proposed transfer of business from Marine Shipping Mutual Insurance Company Limited (MSMI) to North of England Protecting and Indemnity Association Limited (NOE)

12 June 2015

Prepared for:

The High Court of Justice of England and Wales

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<u>Contents</u>	<u>Page</u>
1 Summary and Conclusions.....	3
1.1 Introduction.....	3
1.2 Appointment.....	3
1.3 Professional experience.....	4
1.4 Independence.....	4
1.5 Scope of work.....	5
1.6 Background and purpose of the Scheme.....	5
1.7 Scheme's impact on transferring policyholders of MSMI.....	7
1.8 Scheme's impact on remaining policyholders and member of MSMI...	9
1.9 Scheme's impact on the current policyholders and members of NOE..	10
1.10 Impact of merger of NOE and SMMI.....	11
1.11 The Parent Company Guarantee given by NOE to SMMI.....	13
1.12 Litigation and other recent developments.....	13
1.13 Conclusions.....	14
1.14 Independent Expert's declaration.....	16
2 Limitations & assumptions.....	18
3 Description of the Scheme, policies and participating insurers.....	20
4 Transferring policyholders of MSMI.....	23
5 Remaining policyholders and member of MSMI.....	26
6 Current policyholders and members of NOE.....	27
7 The capital situation under Solvency I, ICAS and Solvency II.....	29
8 Communication and notification aspects of the Scheme.....	32
Appendix A Engagement letter.....	36
Appendix B Experience of Independent Expert.....	39
Appendix C Company structure charts.....	40
Appendix D Data.....	41
Appendix E Definition of terms and glossary.....	43
Appendix F Balance sheets pre- and post-transfer.....	46
Appendix G External Reinsurance Arrangements of MSMI.....	47

1. Summary and Conclusions

1.1. Introduction

- 1.1.1.** Section 109 of the Financial Services and Markets Act 2000 (the FSMA) requires that a scheme report (Scheme Report) must accompany an application to the High Court of Justice of England and Wales (the Court) to approve an insurance business transfer. The Scheme Report should address the question of whether any policyholders impacted by the insurance business transfer are adversely affected to a material extent. The Scheme Report should be produced by a suitably qualified independent person (the Independent Expert) who has been nominated or approved by the Regulator for this purpose.
- 1.1.2.** In this Scheme Report, “Regulator” means the Financial Services Authority (the FSA) or its successor regulator(s) in the United Kingdom, including the Prudential Regulation Authority (the PRA) and the Financial Conduct Authority (the FCA). On 1 April 2013 the FSA reorganised and became two new regulators, the PRA and the FCA. The North of England Protecting and Indemnity Association Limited (NOE) and the Marine Shipping Mutual Insurance Company Limited (MSMI) were authorised by the FSA to carry out contracts of non-life insurance and reinsurance. With effect from 1 April 2013 insurance companies such as NOE and MSMI are authorised by the PRA and regulated by the PRA and the FCA.
- 1.1.3.** This Summary and Conclusions sets out the key findings, methodology, assumptions and analysis contained in my Scheme Report. Whilst it should not be read as a substitute for reading my full Scheme Report, I believe it contains sufficient information to justify the conclusions set out in section 1.12 below. In this Scheme Report, I have used a number of terms and abbreviations that are defined in Appendix E.

1.2. Appointment

- 1.2.1.** I, Keith Tucker, have been appointed by the Directors of NOE and MSMI to act as the Independent Expert for the proposed scheme to transfer all of the insurance business of MSMI to NOE pursuant to Part VII of the FSMA (the Scheme). The Scheme is intended to be effected on 1 November 2015 (the Effective Date).
- 1.2.2.** My fees incurred in the preparation of this Scheme Report are payable by NOE and MSMI.
- 1.2.3.** An extract of the relevant sections from the Engagement Letter regarding this appointment is contained in Appendix A.
- 1.2.4.** My role is to produce the Scheme Report as described in the PRA’s Insurance Business Transfers Statement of Policy and FCA’s Handbook section SUP 18 and as required by section 109 of the FSMA.
- 1.2.5.** This Scheme Report complies with the applicable rules on expert evidence and with the guidance set out by the Regulators in the PRA’s Insurance Business Transfers Statement of Policy and Chapter 18 of the FCA Supervision Manual (SUP 18), which forms part of the FCA Handbook.
- 1.2.6.** Where appropriate, this Scheme Report complies with the relevant Technical Actuarial Standard (TAS) documents as issued by the Board for Actuarial Standards, a subsection of the Financial Reporting Council. The relevant TAS documents are:
- TAS R: Reporting Actuarial Information
 - Insurance TAS
 - TAS D: Data
 - TAS M: Modelling
 - Transformations TAS

- 1.2.7.** My appointment as Independent Expert for this Scheme has been approved by the Regulator.

1.3. Professional experience

- 1.3.1.** I am a Fellow of the Institute and Faculty of Actuaries in the UK and an Associate of the Society of Actuaries in the USA.
- 1.3.2.** I have skills in all areas of general and life insurance work including reserving, capital, pricing and transfers of business. My recent work has been primarily in the field of general insurance including calculation of capital, loss reserves and other balance sheet items, both on a Solvency I and Solvency II basis, and assisting clients with various aspects of their Solvency II implementation. The clients that I dealt with underwrite similar business to that of the two parties (NOE and MSMI) involved in this Scheme.
- 1.3.3.** At the commencement of this assignment, I was employed as a Director in the Insurance Industry Group practice of Moore Stephens LLP and have more than 30 years' experience as a qualified actuary in the insurance industry. I left the employment of Moore Stephens on 8 February 2013 but continued with this assignment on a consultancy basis to Moore Stephens. A brief summary of my experience is contained in Appendix B.

1.4. Independence

- 1.4.1.** I confirm that I have no direct connections with NOE, MSMI, North Insurance Management Limited (NIML) or Sunderland Marine Mutual Insurance Company Limited (SMMI). In particular, I have never worked on any project involving NOE, MSMI, NIML or SMMI apart from the work carried out in connection with the preparation of this Scheme Report.
- 1.4.2.** The firm of Moore Stephens LLP has carried out a number of projects for NOE and MSMI over the period since the financial year ending 30 April 2009. None of these relate to this Scheme and the fee income generated represents a very small percentage of total Moore Stephens LLP's fee income. For each of the financial years ending 30 April 2009 to 30 April 2013 this amounted to approximately 0.1% to 0.2% of total fee income. For the financial year ending 30 April 2014 this amounted to less than 0.4% of fee income. I have had no involvement in any of this work and do not believe that this affects my independence in acting as the Independent Expert for this Scheme.
- 1.4.3.** David Edison, a Partner at Moore Stephens, has for several years been responsible for making actuarial IBNR (loss reserves) projections for each of NOE and MSMI. David Edison and Simon Gallagher, Managing Partner at Moore Stephens and head of the Moore Stephens Insurance Industry Group, were engaged by NOE for the feasibility study and financial due diligence in connection with the recent merger of NOE and SMMI. This Scheme Report gives further information with regard to this merger in sections 1.6.11, 1.10 and 1.11.
- 1.4.4.** Simon Gallagher is acting as the peer reviewer and is responsible for the oversight of my work carried out in connection with the preparation of this Scheme Report. This oversight responsibility does not extend to influencing the approach I have taken in the preparation of, or the content of, this Scheme Report and does not compromise my independence in acting as the Independent Expert for this Scheme. No other Partners or employees of Moore Stephens are, or have been, involved in any work in connection with the preparation of this Scheme Report.

1.5. Scope of work

1.5.1. My scope is to produce a Scheme Report giving my opinion on the impact of the Scheme from the perspective of all of the policyholders, namely:

- the policyholders transferring from MSMI to NOE;
- the policyholders, if any, remaining in MSMI; and
- the current policyholders of NOE.

These are collectively referred to as the Affected Policyholders in this Scheme Report. The intention of the Scheme is that all policyholders currently in MSMI will be transferred to NOE on the Effective Date.

1.5.2. The Regulator has approved the form of this Scheme Report in the context of the Scheme.

1.6. Background and Purpose of the Scheme

1.6.1. The proposed Scheme is to transfer all of the insurance business of MSMI to NOE pursuant to Part VII of the FSMA. Provided it is sanctioned, the Scheme will become effective on the Effective Date. Under the Scheme, all policies of MSMI will be transferred to NOE together with all the liabilities and assets of MSMI. The intention is that MSMI will subsequently be dissolved. Until MSMI's authorisation is cancelled, it must retain a Minimum Capital Requirement (MCR) and thus the Scheme allows for the value of assets to be transferred to be reduced to the extent necessary to maintain MSMI's MCR, with the remaining balance to be transferred as soon as possible following MSMI's de-authorisation.

1.6.2. MSMI was incorporated under the Companies Acts 1948 to 1967 in England and Wales on 11 August 1972 as a company limited by guarantee and has no share capital. It is authorised under the FSMA to carry out contracts of general insurance of the classes shown in section 3.2.3 of this Scheme Report. Its main business consists of hull and machinery insurance covering risks of loss or damage to the hull and machinery of ships. Some of the policies issued by MSMI can also provide cover in respect of risks arising out of the total loss of a ship and loss of income arising from loss or damage to a ship. As explained in section 1.6.5 below, MSMI is a mutual company owned by its sole member, NOE. MSMI ceased underwriting new business with effect from 30 June 2011 and is in the process of managing the run off of its outstanding liabilities, which comprises direct insurance business only and no inwards reinsurance.

1.6.3. NOE was incorporated under the Companies Act 1948 in England and Wales on 13 March 1952 as a company limited by guarantee and has no share capital. It is authorised under the FSMA to carry out contracts of general insurance of the classes shown in section 3.2.6 of this Scheme Report. Its main business consists of Protecting and Indemnity (liabilities, costs and expenses arising in respect of cargo, seamen and passengers as well as third party liabilities in respect of pollution, property damage, wreck removal, salvage and collision), Freight Demurrage & Defence (legal costs and expenses in relation to a range of disputes) and War Risks (losses caused by war and terrorism or as consequence of a ship being blocked or trapped in an area of conflict). NOE also provides reinsurance to a small number of businesses operating in the marine insurance sector. It is a mutual company owned by its members and is open for new business.

1.6.4. The basic principal of mutuality which underpins the activities of NOE is that the members of the company insure each another against the liabilities, losses, costs and expenses which they or any of them may become liable to pay in respect of any ship entered during the relevant policy year. The rules of NOE contain provisions which provide wide powers to call

upon members to contribute funds for that purpose. More detailed information is shown in sections 3.2.7 to 3.2.9 of this Scheme Report.

- 1.6.5.** NOE made an offer to acquire MSMI which was approved by the members of MSMI at an extraordinary general meeting held on 22 June 2011. The terms of this acquisition were subsequently set out in a Framework Agreement dated 23 August 2011. The transaction contemplated under the terms of the Framework Agreement was subject to the Regulator's approval of NOE as the controller of MSMI pursuant to Part XII FSMA (Change in Control), which was given by the Regulator on 10 August 2011. On 2 November 2011 a transaction was completed which resulted in MSMI becoming a wholly owned subsidiary of NOE with NOE becoming the sole member of MSMI. This transaction was in accordance with the Framework Agreement, resulting in the consequent distribution of a proportion of MSMI's reserves to its former members. All former members of MSMI are now released from any further liability to make contributions to, and from rights to access, the funds of MSMI.
- 1.6.6.** At the same date of 2 November 2011 a reinsurance to close transaction was effected by NOE and MSMI resulting in the Reinsurance Agreement under which NOE reinsures 100% of the risks insured by MSMI net of amounts recovered by or recoverable under other External Reinsurance Arrangements entered into by MSMI.
- 1.6.7.** Subject to the Scheme being approved and there being no excluded policies, all policyholders of MSMI will become policyholders of NOE, the Reinsurance Agreement between MSMI and NOE will cease to exist and all the External Reinsurance Arrangements with External Reinsurance Parties will be transferred from MSMI to NOE.
- 1.6.8.** NOE has a long standing relationship with MSMI having managed its business since it was founded in 1972 either directly or through its wholly owned management company, NIML. The Management Agreement was in effect since November 2003 and terminated on 30 June 2013 in anticipation of the Scheme taking effect. Following this termination, an Interim Management Agreement took effect to provide for NIML to continue to manage the business of MSMI to the same standards of service as under the Management Agreement.
- 1.6.9.** Having MSMI as a separate wholly owned subsidiary still requires MSMI to separately prepare financial statements and to pay separate costs for audit, compliance and management. The new Solvency II regime effective on 1 January 2016 will increase the administrative burden if MSMI remains a separate company. MSMI also needs to maintain a certain level of capital in accordance with the Regulator's requirements. The level of capital will be subject to a minimum level irrespective of the size of the business still in run-off and over time would become a disproportionate amount compared to the size of the liabilities; whereas after the Scheme is effected, as a small part of NOE's overall liabilities, the capital requirement in respect of the former MSMI liabilities would in all likelihood decrease as the liabilities decrease.
- 1.6.10.** **The main purpose of the Scheme, as confirmed in discussions with NOE management, is to achieve a more efficient use of capital and savings in costs by managing one company, NOE, rather than managing two separate companies, NOE and MSMI. I have no reason to doubt that this is likely to be the beneficial outcome of the Scheme given the arguments presented in 1.6.9 above.**
- 1.6.11.** A more recent development, subsequent to the acquisition of MSMI by NOE, was the merger of NOE and SMMI. On 28 February 2014 SMMI became a wholly owned subsidiary of NOE. The transaction involved the SMMI Board and SMMI members appointing NOE as the sole member of SMMI. The principal activity of SMMI is providing insurance against marine and war risks and risks incidental to marine insurance, including protection and indemnity risks, of a variety of vessels including fishing vessels, tugs, barges and short sea cargo vessels. The company also insures risks incidental to aquaculture. SMMI has a number of subsidiaries of which the principal activities are marine insurance and reinsurance and insurance broking. Post-merger, SMMI changed its name from Sunderland

1.7. Scheme’s impact on transferring policyholders of MSMI

- 1.7.1. The intention of the Scheme is that all of the MSMI business will be transferred to NOE. All MSMI policies are of the same class and provide cover for Hull and Machinery. **Table A** below summarises the MSMI business at the financial year end of 20 February 2014 when total technical provisions for gross claims was US\$19,330,000. Note that the numbers of insured vessels and policyholders are in respect of MSMI’s open policy years. *[Note that the table below shows the position as at 20 February 2014 whereas on 6 May 2014 the MSMI Board closed the 2007/08, 2008/09 and 2009/10 policy years and the outstanding claims for those and prior policy years were incorporated into the 2010/11 policy year].*

Table A				
MSMI insured vessels, policyholders and claims technical provisions*				
Open Policy Year	2007/08	2008/09	2009/10	2010/11
Number of insured vessels	371	383	376	425
Number of policyholders#	61	55	51	48
	US \$			
Gross technical provisions for claims	19,330,000			
Reinsured under External Reinsurance Arrangements	13,429,000			
Reinsured under Reinsurance Agreement with NOE	5,901,000			
Net technical provisions for claims	0			
<i>* As at 20 February 2014.</i>				
<i># These are the number of groups of policyholders – each group may have several member companies but from an underwriting and contact perspective, the group level is the most relevant statistic. For the open policy years at 20 February 2014, the actual number of insured vessels, policies and policyholders were 699, 1904 and 414 respectively.</i>				

- 1.7.2. Appendix G shows a summary of the External Reinsurance Arrangements, which are all subject to English Law and the jurisdiction of the English Courts. The External Reinsurance Arrangements are spread over a number of different External Reinsurance Parties. The transfer of the External Reinsurance Arrangements from MSMI to NOE is included within the Scheme and the mechanism for giving notice to the External Reinsurance Parties is described in section 8 of this Scheme Report. The liabilities reinsured post-Effective Date will be exactly the same as the liabilities reinsured pre-Effective Date. **The External Reinsurance Parties will be notified of the Scheme and the External Reinsurance Arrangements will continue with the same financial effects and service standards pre- and post-Effective Date. My conclusion is based on the fact that the reinsured liabilities and the reinsurers will not change as a result of the Scheme.**
- 1.7.3. Prior to the Scheme taking effect, if MSMI suffered a deteriorating claims experience with the need to increase claims payments and claims technical provisions, NOE as part reinsurer of MSMI and the External Reinsurance Parties would be liable to increase their claims payments and claims technical provisions, with the effect being no change in the net

technical provisions of zero for MSMI. For NOE, any such increase would have to come from any surplus assets (free reserves) in NOE or by way of a call to NOE's members. Post-Effective Date, any additional funds to cover such a deterioration in the net (of External Reinsurance Arrangements) claims experience of the former MSMI policies would also have to come from surplus assets of NOE or by way of a call to NOE's members. **Thus, I conclude that the Scheme has no effect on the risks facing MSMI or NOE as a result of such a deteriorating claims experience.**

- 1.7.4.** Prior to the Scheme taking effect, if one or more of the External Reinsurance Parties were to default on their liabilities to MSMI, the additional funds required by MSMI would have to come from any surplus assets (free reserves) in MSMI, which as shown in **Table B** below amounted to US\$5,810,000 or 30.1% of the gross technical provisions for MSMI claims in the balance sheet of 20 February 2014. As NOE is the sole member of MSMI (and MSMI being a wholly owned subsidiary of NOE), any additional funds required by MSMI to replenish such surplus or for any other reason would have to come from any surplus assets in NOE or by way of a call to NOE's members. As can be seen from **Table B**, NOE had surplus assets (as shown in the consolidated balance sheet of 20 February 2014 that included MSMI) of US\$312,274,000 or 32.1% of the gross technical provisions for claims of NOE and MSMI combined. It should also be noted that the gross technical provisions for claims of MSMI amounted to only 2.0% of the gross technical provisions for claims of NOE and MSMI combined. **I conclude that, since the total gross claims of MSMI are relatively minor compared to the consolidated NOE total gross claims and NOE's surplus assets, a reinsurance default by one or more of the External Reinsurance Parties would be unlikely to cause any financial problems due to the fact that NOE would in all likelihood put additional funds as required in MSMI. Moreover, NOE's reputation in the market would suffer if such additional funds were not forthcoming.**

Table B		
MSMI and NOE gross technical provisions and surplus assets (free reserves)*		
US \$	MSMI	NOE #
Gross technical provisions for claims **	19,330,000	973,047,000
Surplus assets (free reserves)	5,810,000	312,274,000
Surplus assets as a percentage of gross technical provisions for claims	30.1%	32.1%
Gross technical provisions for claims of MSMI as a percentage of gross technical provisions for claims of NOE #		2.0%
* As at 20 February 2014.		
# NOE consolidated balance sheet figures including MSMI.		
** Sections 4.1.7 and 4.1.8 of this Scheme Report give further information on the technical provisions for claims.		

- 1.7.5.** The situation with regard to a possible default of one or more of the External Reinsurance Parties post-Effective Date would be that any additional funds would come from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. Pre-Effective Date the MSMI policyholders benefit from the protection of MSMI's surplus assets (as at 20 February 2014 amounting to US\$5,810,000 or 30.1% of MSMI's gross technical provisions for claims) whereas post-Effective Date they will benefit, together with all other policyholders in NOE, from the protection of NOE's surplus assets (as at 20 February 2014 amounting to US\$312,274,000 or 32.1% of NOE's gross technical provisions for claims). **Thus, I conclude that the Scheme will have minimal effect on the protection afforded to MSMI policyholders against a default by one or more of the External Reinsurance Parties.**

- 1.7.6.** All policyholders in MSMI are direct insurance policyholders and prior to the Effective Date all would rank equally in priority in any insolvency situation subject to The Insurers (Reorganisation and Winding Up) Regulations 2004. Post-Effective Date, all direct policyholders in NOE (whether members or non-members) would rank equally in priority in any such insolvency situation.
- 1.7.7.** Both MSMI and NOE were managed by NIML. During 2014 NOE changed its management structure with effect that NIML is no longer involved in the management of NOE and management responsibility was transferred directly to NOE management. NIML still currently manages MSMI under the Interim Management Agreement, but post-Effective Date its business will be managed directly by NOE management. In practical terms there will be no change to the personnel responsible for managing NOE and MSMI business pre- and post-Effective Date. From discussions with NOE management, no changes to the accounting and reserving standards are envisaged post-Effective Date. For both MSMI and NOE, the technical provisions for claims are calculated using cautious bases and it is my opinion, from discussions with NOE management, that this will continue post-Effective Date and that the Scheme will have no impact on the value of the respective liabilities that originated in MSMI or NOE. Further information can be found in section 4 of this Scheme Report (in particular sections 4.1.7 to 4.1.9).
- 1.7.8.** Although the Scheme will not take place until the Effective Date and the financial figures will change over time, I have no reason to believe that the financial strength of NOE immediately post-Effective Date will be different from the situation immediately before the Effective Date. **I conclude from the figures shown in Table B above that the policyholders of MSMI will benefit directly from a greater level of surplus assets (expressed as a percentage of the gross technical provisions for claims) as part of the larger company NOE than if MSMI were a totally separate company.**
- 1.7.9.** I have considered the Solvency I, ICAS and Solvency II capital situation in section 7 of this Scheme Report where **I conclude that NOE has the greater financial strength when compared to MSMI and that post-Effective Date, the transferred MSMI policyholders will benefit from the greater financial strength of NOE.**
- 1.7.10.** NIML manages the MSMI policies now and post-Effective Date, the transferred MSMI policies will continue to be managed by the same personnel in NOE. **Thus, I conclude that the Scheme will have no impact on the standards of service given to MSMI policyholders.**

1.8. Scheme's impact on remaining policyholders and member of MSMI

- 1.8.1.** The intention of the Scheme is that all the policies of MSMI will transfer to NOE at the Effective Date and that there will be no remaining policies in MSMI post-Effective Date. However, the Scheme does allow for the possibility of some policies remaining within MSMI in the event that there is some unforeseen reason why they cannot be transferred to NOE on the Effective Date, these policies being referred to as Residual Policies and would be reinsured from MSMI to NOE under the Residual Policies Reinsurance Contract. The Scheme places an obligation on both MSMI and NOE to enable the later inclusion of Residual Policies. Thus, any such Residual Policies will be subsequently transferred to NOE and the ultimate intention is that all MSMI policies will be transferred to NOE and that MSMI will be dissolved.
- 1.8.2.** **My conclusion is that, in the unlikely event that there are Residual Policies, the situation for any such policies would be substantially the same pre- and post-Effective Date as they are currently reinsured with NOE under the existing Reinsurance Agreement and would be reinsured with NOE under the Residual Policies Reinsurance Contract post-Effective Date.**

- 1.8.3.** There are no proprietary members' rights issues to consider in the unlikely event that there are Residual Policies since NOE is the sole member of MSMI pre-Effective Date and would continue to be the sole member of MSMI post-Effective Date until such time as MSMI is dissolved.

1.9. Scheme's impact on the current policyholders and members of NOE

- 1.9.1.** NOE operates predominantly upon a mutual model of business whereby the persons that enter ships for insurance are automatically appointed as members of NOE. Whilst policyholders are usually members, some risks are underwritten whereby the policyholders do not become members. Sections 3.2.7 to 3.2.9 and 6.1.1 to 6.1.2 of this Scheme Report give further information in this regard. **Table C** below shows the NOE numbers of insured vessels, insured vessels with members' rights, insured vessels without members' rights and policyholders for the open policy years as at the date of this Scheme Report. The Reinsurance Agreement (between NOE and MSMI) does not give the policyholders of insured vessels of MSMI any members' rights in NOE. Post-Effective Date the insured vessels of MSMI will become insured vessels of NOE but with no members' rights for the policyholders in respect of the MSMI policies transferred to NOE.

Table C				
NOE insured vessels, insured vessels with members' rights*, insured vessels without members' rights and policyholders# for Open Policy Years				
Open Policy Year	2012/13	2013/14	2014/15	2015/16
Number of vessels insured	8,551	5176	5245	4653
Number of vessels insured with members' rights*	6,798	3,768	3892	3861
Number of vessels insured without members' rights	1753	1,408	1353	792
Number of policyholders#	437	400	394	334
* <i>Those insured vessels with full mutual membership rights and obligations.</i>				
# <i>These are the number of groups of policyholders – each group may have several member companies but from an underwriting and contact perspective, the group level is the most relevant statistic.</i>				

- 1.9.2.** The outstanding obligations and liabilities of NOE and MSMI predominately relate to entries made in open policy years as described more fully in sections 3.2.7 to 3.2.9 in this Scheme Report.

- 1.9.3.** Prior to the Scheme taking effect, the insurance risks of MSMI are 100% reinsured and if it suffered a deteriorating claims experience with the need to increase claims payments and claims technical provisions, NOE as part reinsurer of MSMI and the External Reinsurance Parties would be liable to increase their claims payments and claims technical provisions. For NOE, any such increase would have to come from any surplus assets in NOE or by way of a call to NOE's members. Post-Effective Date, any additional funds to cover such a deterioration in the net (of External Reinsurance Arrangements) claims experience of the former MSMI policies would also have to come from surplus assets of NOE or by way of a call to NOE's members. **Thus, based on the assumption that the External Reinsurance Parties would honour their commitments under the External Reinsurance Arrangements, I conclude that the Scheme has no material effect on the net risks facing NOE as a result of such a deteriorating claims experience.**

- 1.9.4.** The effect on NOE of the situation with regard to a possible default of one or more of the External Reinsurance Parties before the Effective Date has been covered in section 1.7.4 of this Scheme Report. As can be seen from **Table B** in section 1.7.4, NOE had surplus assets that amounted to 32.1% of the gross technical provisions for claims of NOE and MSMI combined and the gross technical provisions for claims of MSMI amounted to only 2.0% of the gross technical provisions for claims of NOE and MSMI combined. Since the total gross claims of MSMI are relatively minor compared to the consolidated NOE total gross claims and NOE's surplus assets, a reinsurance default by one or more of the External Reinsurance Parties would be unlikely to cause any financial problems whereby NOE would not put additional funds as required in MSMI. Moreover, NOE's reputation in the market would suffer if such additional funds were not forthcoming.
- 1.9.5.** The situation with regard to a possible default of one or more of the External Reinsurance Parties post-Effective Date would be that any additional funds would come from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. The Scheme has no effect on the net liabilities of NOE that derive from the MSMI policies, which amounted to US\$5,901,000 as at 20 February 2014 as shown in **Table A** of section 1.7.1 (further information is shown in section 6 of this Scheme Report). **I conclude that, whilst the situation post-Effective Date is different from that pre-Effective Date in that NOE assumes the whole risk of a default by one or more of the External Reinsurance Parties, in a practical sense for the reasons set out in section 1.9.4 above, the risks facing NOE and its members are little changed by the Scheme.**
- 1.9.6.** Prior to the Effective Date all direct insurance policyholders in NOE (whether members or non-members) would rank equally in priority in any insolvency situation subject to The Insurers (Reorganisation and Winding Up) Regulations 2004. In any such situation, inwards reinsurance business (such as provided under the Reinsurance Agreement) would rank below direct insurance policyholders. Post-Effective Date, all direct policyholders in NOE (including those transferred from MSMI) would rank equally in priority in any such insolvency situation and thus, would rank above any NOE inwards reinsurance business. However, the total net technical provisions for claims of NOE are unchanged by the transfer of the MSMI policies and the total gross technical provisions for claims of the transferring MSMI policies amount to only 2.0% of the total gross technical provisions for claims of MSMI and NOE combined.
- 1.9.7.** **Thus, I conclude that the Scheme has no material financial impact on the policyholders who are also members of NOE and no material impact on the proprietary interests of the members of NOE.** The only other consideration is that of policyholders of NOE who are not members. Again, there is no material financial impact since MSMI is already owned by NOE and all liabilities of MSMI (net of the liabilities reinsured under the External Reinsurance Arrangements) are reinsured with NOE under the Reinsurance Agreement. Moreover, the total gross technical provisions for claims of the transferring MSMI policies amount to only 2.0% of the total gross technical provisions for claims of MSMI and NOE combined and thus have a minimal impact on the risk profile of NOE. **Thus, I conclude that the Scheme will not have a material effect on NOE's risk profile and policyholders whether as a going concern business or in an insolvency situation.** Further information in this regard can be found in section 6 of this Scheme Report.

1.10. Impact of merger of NOE and SMMI

- 1.10.1.** As mentioned in sections 1.4.3 and 1.6.11 of this Scheme Report, on 28 February 2014 SMMI became a wholly owned subsidiary of NOE with NOE being the sole member of SMMI. Post-merger, SMMI changed its name to SMI.
- 1.10.2.** Founded in 1882, SMI is an insurer of hull and machinery, protection and indemnity, personal accident and aquaculture risks, serving circa 29,000 policyholders in over 50 countries. SMI has expanded to become a worldwide specialist insurer. SMI's focus is on

maintaining an exemplary level of service to its policyholders whilst also providing them with financial security. Its head office is based in the North East of England with Group operations also spanning across 13 other offices in Australia, Canada, the Netherlands, New Zealand, South Africa and the USA, employing around 120 people across the Group.

- 1.10.3.** SMI has a 'BBB+' financial strength rating and stable outlook from Standard & Poor's and 'A-' ratings from Fitch and AM Best. For the year ending 31 December 2012, SMI reached gross premium income of £95.3 million (US\$156.3M), total assets and liabilities were £169.8 million (US\$278.3M) and £134.5 million (US\$220.5) respectively, with the surplus assets reaching £35.3 million (US\$57.8M). These ratings were recently reaffirmed via the various agencies, which all reacted positively when the news of the proposed merger was announced. For the year ending 31 December 2013, the equivalent figures in sterling were gross premium income £92.5M, total assets £165.6M, total liabilities £130.9M and surplus assets £34.7M.
- 1.10.4.** As at the date of acquisition of 28 February 2014, the balance sheet of SMI in US\$ showed total assets of US\$271.4M, total liabilities of US\$223.8M and surplus assets of US\$47.6M. **Table D** below shows the financial situation of **Table B** (section 1.7.4) with the consolidation of SMI in the NOE figures. It should be noted that that the SMI figures are at a slightly different date of 28 February 2014 whereas the other figures relate to 20 February 2014.

Table D			
MSMI, SMI and NOE gross technical provisions and surplus assets (free reserves)*			
US \$	MSMI	SMI	NOE @@
Gross technical provisions for claims	19,330,000	176,613,000	1,115,177,000
Surplus assets (free reserves)	5,810,000	47,587,000	359,861,000
Surplus assets as a percentage of gross technical provisions for claims	30.1%	26.9%	32.3%
Gross technical provisions for claims of MSMI as a percentage of gross technical provisions for claims of NOE @@			1.7%
<i>* As at 28 February 2014 for SMI figures and 20 February 2014 for other figures.</i>			
@@ NOE consolidated balance sheet figures including MSMI and SMI.			

- 1.10.5.** A comparison of **Tables B and D** shows that the recent merger of NOE and SMI had minimal financial impact on MSMI. Based on February 2014 figures, MSMI benefits from surplus assets amounting to 30.1% of gross technical provisions as a stand-alone company and 32.1% (**Table B**) as part of the much larger company NOE. When the SMI figures are consolidated, the surplus assets amount to 32.3% (**Table D**) of the gross technical provisions. The gross technical provisions of MSMI as a percentage of the combined NOE and MSMI gross technical provisions are only 2% (**Table B**) and amount to only 1.7% (**Table D**) in the consolidated balance sheet that includes SMI.
- 1.10.6.** **Table E** below shows the impact of the Scheme from the perspective of SMI now that it is a wholly owned subsidiary of NOE. As a stand-alone company (but wholly owned by NOE) SMI has surplus assets amounting to 26.9% of its gross technical provisions. With SMI consolidated with NOE but excluding MSMI (apart from the reinsurance from MSMI to NOE), the surplus assets amount to 32.1% of the gross technical provisions of NOE and SMI combined. With SMI consolidated with NOE including MSMI, the surplus assets amount to 32.3% of the gross technical provisions of NOE, SMI and MSMI combined. The gross technical provisions of SMI are 16.0% of the combined gross technical provisions of NOE and SMI, and 15.8% of the combined technical provisions of NOE, SMI and MSMI. **Thus, I conclude that the Scheme will not have a material impact on the financial situation of SMI, which will be little changed pre- and post-Effective Date.**

Table E			
SMI and NOE gross technical provisions and surplus assets (free reserves)*			
US \$	SMI	NOE @	NOE @@
Gross technical provisions for claims	176,613,000	1,101,748,000	1,115,177,000
Surplus assets (free reserves)	47,587,000	354,051,000	359,861,000
Surplus assets as a percentage of gross technical provisions for claims	26.9%	32.1%	32.3%
Gross technical provisions for claims of SMI as a percentage of gross technical provisions for claims of NOE @ and NOE @@		16.0%	15.8%
<i>* As at 28 February 2014 for SMI figures and 20 February 2014 for other figures.</i>			
<i>@ NOE consolidated balance sheet figures including SMI but excluding MSMI (apart from the reinsurance from MSMI to NOE).</i>			
<i>@@ NOE consolidated balance sheet figures including MSMI and SMI</i>			

1.11. The Parent Company Guarantee given by NOE to SMI

- 1.11.1.** Under the Parent Company Guarantee dated 28 February 2014 NOE is ultimately responsible for SMI's liabilities comprising primarily of claims under the insurance contracts and the liabilities arising from the SMI defined benefit pension scheme, which is closed to new members. This is my understanding of the situation having read a copy of the Parent Company Guarantee supplied by NOE.
- 1.11.2.** As shown in **Table E** (section 1.10.6) SMI has substantial surplus assets and the overall financial position of NOE is little changed by the inclusion of SMI's assets and liabilities in the consolidated figures of NOE. The surplus assets of 32.3% of the total gross technical provisions for claims is comparable to that of 32.1% shown in **Table B** (section 1.7.4). As shown in **Table G** (section 7.1.4) SMI has substantial capital resources in excess of the capital resources requirement (CRR) and the ratio of its capital resources to the CRR at 347.5% is not too dissimilar to that of NOE (389.4%) as shown in **Table F** (section 7.1.3).
- 1.11.3.** The pension scheme deficit of SMI in the balance sheet of 28 February 2014 amounted to US\$1.361million (the difference between the pension scheme assets of US\$49.190million and liabilities of US\$50.551million). NOE already has a similar defined benefit pension scheme that is also closed to new members. The pension scheme deficit of NOE in its balance sheet of 20 February 2014 amounted to US\$26.303million (the difference between the pension scheme assets of US\$75.048million and liabilities of US\$101.351million). Thus, the SMI pension scheme deficit represented less than 5% of the combined pension scheme deficits of NOE and SMI.
- 1.11.4.** Thus, I conclude that the Parent Company Guarantee given by NOE to SMI has minimal impact on the financial security of MSMI policyholders both pre- and post-Effective Date.

1.12. Litigation and other recent developments

- 1.12.1.** MSMI and NOE are both currently party to proceedings concerning an appeal to the relevant tax authority in Germany concerning the quantum of insurance premium taxes (IPT) levied, in respect of various insurance policies issued by MSMI and NOE in connection with German registered vessels forming part of a fleet managed by a member company, also based in Germany. It is my understanding that NOE and MSMI have a contractual right to indemnification from the member company in respect of the costs of the proceedings and the related IPT liability. Any potentially material developments with regard to these German

tax proceedings will be addressed in a supplementary report to be produced prior to the final Court hearing.

- 1.12.2.** In early February 2015 NOE provided SMI with capital support of £10million under the Parent Company Guarantee. This was due to a projected fall in SMI's Individual Capital Guidance (ICG) coverage at 20 February 2015. The principal reason for the projected fall was an estimated increase in the deficit of SMI's defined benefit pension scheme from £0.817million (the US\$1.361million mentioned in section 1.11.3 above) to over £7million due to movement in corporate bond yields. The actual deficit in the SMI defined benefit pension scheme as at 20 February 2015 was not as high as projected and was £3.4million (US\$5.3million), the difference between pension scheme assets of £29.8million (US\$46.0million) and liabilities of £33.2million (US\$51.3million). By comparison the NOE defined benefit pension scheme deficit as at 20 February 2015 had increased to £29.4million (US\$45.4million), the difference between pension scheme assets of £50.5million (US\$78.0million) and liabilities of £79.9million (US\$123.4million).
- 1.12.3.** I believe these two recent developments do not have any material impact on the Scheme and have minimal impact on the level of financial security available for NOE and MSMI policyholders.

1.13. Conclusions

- 1.13.1.** The main purpose of the Scheme, as confirmed in discussions with NOE management, is to achieve a more efficient use of capital and savings in costs by managing one company, NOE, rather than managing two separate companies, NOE and MSMI. **I have no reason to doubt that this is likely to be the beneficial outcome of the Scheme** (see sections 1.6 and 3 of this Scheme Report for more information).
- 1.13.2.** The transfer of the External Reinsurance Arrangements from MSMI to NOE is included within the Scheme and the mechanism for giving notice to the External Reinsurance Parties is described in section 8 of this Scheme Report. The liabilities reinsured post-Effective Date will be exactly the same as the liabilities reinsured pre-Effective Date. **The External Reinsurance Parties will be notified of the Scheme and the External Reinsurance Arrangements will continue with the same financial effects and service standards pre- and post-Effective Date. My conclusion is based on the fact that the reinsured liabilities and the reinsurers will not change as a result of the Scheme** (see sections 1.7 and 4 of this Scheme Report for more information).
- 1.13.3.** A deteriorating claims experience on the MSMI policies pre- or post-Transfer with the consequent need to increase claims payments and claims technical provisions, would require NOE and the External Reinsurance Parties to increase their claims payments and claims technical provisions, with the effect being no change in the net technical provisions of zero for the MSMI policies. For NOE, any such increase would have to come from any surplus assets (free reserves) in NOE or by way of a call to NOE's members. **Thus, based on the assumption that the External Reinsurance Parties would honour their commitments under the External Reinsurance Arrangements, I conclude that the Scheme has no material effect on the net risks facing MSMI or NOE as a result of such a deteriorating claims experience** (see sections 1.7, 1.9, 4 and 6 of this Scheme Report for more information).
- 1.13.4.** Prior to the Scheme taking effect, if one or more of the External Reinsurance Parties were to default on their liabilities to MSMI, the additional funds required by MSMI would have to come from any surplus assets (free reserves) in MSMI, which amounted to US\$5,810,000 or 30.1% of the gross technical provisions for MSMI claims in the balance sheet of 20 February 2014. As NOE is the sole member of MSMI (and MSMI being a wholly owned subsidiary of NOE), any additional funds required by MSMI to replenish such surplus or for any other reason would have to come from any surplus assets in NOE or by way of a call to NOE's members. NOE had surplus assets (as shown in the consolidated balance sheet of 20

February 2014 that included MSMI) of US\$312,274,000 or 32.1% of the gross technical provisions for claims of NOE and MSMI combined. It should also be noted that the gross technical provisions for claims of NOE and MSMI amounted to only 2.0% of the gross technical provisions for claims of NOE and MSMI combined. **I conclude that, since the total gross claims of MSMI are relatively minor compared to the consolidated NOE total gross claims and NOE's surplus assets, a reinsurance default by one or more of the External Reinsurance Parties would be unlikely to cause any financial problems due to the fact that NOE would in all likelihood put additional funds as required in MSMI. Moreover, NOE's reputation in the market would suffer if such additional funds were not forthcoming** (see sections 1.7, 1.9, 4 and 6 of this Scheme Report for more information).

- 1.13.5.** The situation with regard to a possible default of one or more of the External Reinsurance Parties post-Effective Date would be that any additional funds would come from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. Pre-Effective Date the MSMI policyholders benefit from the protection of MSMI's surplus assets (as at 20 February 2014 amounting to US\$5,810,000 or 30.1% of MSMI's gross technical provisions for claims) whereas post-Effective Date they will benefit, together with all other policyholders in NOE, from the protection of NOE's surplus assets (as at 20 February 2014 amounting to US\$312,274,000 or 32.1% of NOE's gross technical provisions for claims). **Thus, I conclude that the Scheme will have minimal effect on the protection afforded to MSMI policyholders against a default by one or more of the External Reinsurance Parties** (see sections 1.7 and 4 of this Scheme Report for more information).
- 1.13.6.** Whilst the Scheme has no effect on the net liabilities of NOE that derive from the MSMI policies (which amounted to US\$5,901,000 as at 20 February 2014), a possible default of one or more of the External Reinsurance Parties post-Effective Date would require additional funds from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. **I conclude that, whilst the situation post-Effective Date is different from that pre-Effective Date in that NOE assumes the whole risk of a default by one or more of the External Reinsurance Parties, in a practical sense for the reasons set out in section 1.13.4 above, the risks facing NOE and its members are little changed by the Scheme** (see sections 1.9 and 6 of this Scheme Report for more information).
- 1.13.7.** Although the Scheme will not take place until the Effective Date and the financial figures will change over time, I have no reason to believe that the financial strength of NOE immediately post-Effective Date will be different from the situation immediately before the Effective Date. **I conclude from the figures shown in Table B (in section 1.7.4 of this Scheme Report) that the policyholders of MSMI will benefit directly from a greater level of surplus assets (expressed as a percentage of the gross technical provisions for claims) as part of the larger company NOE than if MSMI were a totally separate company** (see sections 1.7, and 4 of this Scheme Report for more information).
- 1.13.8.** I have also considered the Solvency I, ICAS and Solvency II capital situation in section 7 of this Scheme Report where **I conclude that NOE has the greater financial strength when compared to MSMI and that post-Effective Date, the transferred MSMI policyholders will benefit directly from the greater financial strength of NOE.**
- 1.13.9.** NIML manages the MSMI policies now and Post-Effective Date, the transferred MSMI policies will continue to be managed by the same personnel in NOE. **Thus, I conclude that the Scheme will have no impact on the standards of service given to MSMI policyholders** (see sections 1.7 and 4 of this Scheme Report for more information).
- 1.13.10.** **My conclusion is that, in the unlikely event that there are Residual Policies, the situation for any such policies would be substantially the same pre- and post-Effective Date as they are currently reinsured with NOE under the existing Reinsurance Agreement and would be reinsured with NOE under the Residual**

Policies Reinsurance Contract post-Effective Date (see sections 1.8 and 5 of this Scheme Report for more information).

1.13.11. Table E in section 1.10.6 of this Scheme Report shows the impact of the Scheme from the perspective of SMI policyholders. This table clearly shows the trivial impact of the MSMI liabilities and assets being transferred to NOE under the Scheme. **Thus, I conclude that the financial impact of the Scheme on SMI policyholders will be minimal.**

1.13.12. I have considered the effect on MSMI policyholders of the Parent Company Guarantee given by NOE to SMI and have **concluded that it has minimal impact on the financial security of MSMI policyholders both pre- and post-Effective Date.**

1.13.13. I am satisfied that the proposed approach to communication with policyholders (as described in section 8 of this Scheme Report) is both proportionate and reasonable.

1.13.14. As per SUP 18.2.36(4)(c) of the FCA Handbook and section 2.33(4)(c) of the PRA's Insurance Business Transfers Statement of Policy, I am satisfied that the costs and tax effects of the Scheme do not affect the security of any the of the policyholders contractual rights in MSMI, NOE and SMI. No costs relating to the Scheme will be borne by the policyholders. In reaching these conclusions, I have relied on information supplied by Chris Owen, Corporate Counsel & Company Secretary of NOE.

1.13.15. My overall conclusions are:

- **The Scheme has a beneficial effect on NOE in terms of future administration costs and future capital requirements.**
- **MSMI policyholders will benefit directly from the greater financial strength of NOE post-Effective Date.**
- **The Scheme has no material financial impact on NOE's risk profile and policyholders whether as a going concern business or in an insolvency situation.**
- **The Scheme has no material impact on the proprietary interests of the members of NOE.**
- **The Scheme has no impact on the service standards for all policyholders in NOE and MSMI.**
- **The Scheme has minimal impact for SMI policyholders.**

1.13.16. My conclusions are based on information available at the date of this Scheme Report and financial information for both MSMI and NOE as at 20 February 2014. SMI financial information is either based on the financial year end of 31 December 2013 or at 28 February 2014, the date of acquisition of SMI by NOE.

1.14. Independent Expert's declaration

1.14.1. I confirm that I understand my duty to the Court and have complied and will continue to comply with it. I understand that I must help the Court on matters within my expertise. I confirm that I understand this duty overrides any obligation to the persons from which I have received instructions or from whom I have been paid.

1.14.2. I have exercised reasonable care and skill in order to be accurate and complete in preparing this Scheme Report. I have not, without forming an independent view, included or excluded

anything which has been suggested to me by others. I will notify those instructing me immediately and confirm in writing if, for any reason, my existing Scheme Report requires any correction or qualification.

1.14.3. I confirm that I am aware of the requirements of the Civil Procedure Rules Part 35, Practice Direction Part 35 and the Protocol for the Instruction of Experts to give Evidence in Civil Claims.

1.14.4. I confirm that I have made clear which facts and matters referred to in this Scheme Report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.

A handwritten signature in black ink, appearing to read "Keith Tucker", with a long horizontal flourish extending to the right.

Keith Tucker FIA, ASA

12 June 2015

2. Limitations and Assumptions

2.1. Introduction

2.1.1. In preparing this Scheme Report, I have obtained and reviewed the data and other information set out in Appendix D. Whilst most of this data and information has been audited, I have relied on some additional data and information provided by staff employed by NOE and NIML both in writing and orally in meetings. I am satisfied with the reasonableness of this data and information from my own experience in the insurance industry. However, my opinions depend on the substantial accuracy of this data and information. The user of this Scheme Report is relying on NOE, NIML and MSMI, not me or Moore Stephens, for data quality and it should be noted that any misrepresentation in the data could affect the conclusions I have drawn in this Scheme Report.

2.1.2. My role is to consider the relative position of the Affected Policyholders before and after the Effective Date. From examination of the financial data available, I have concluded that the level of capital for each insurer (MSMI and NOE) before the Effective Date is appropriate. I have necessarily used historical information, as at 20 February 2014 (the financial year end date for both NOE and MSMI), for this Scheme Report. I have relied on NOE's and MSMI's published assessments of their financial positions.

2.1.3. This Scheme Report considers only the Scheme and does not consider any alternative schemes.

2.1.4. My conclusions are based on:

- The fact that there will be no change in management following the Effective Date;
- the absence of any material change in the relationship with reinsurers after the Effective Date;
- no material change in the financial risks facing Affected Policyholders after the Effective Date;
- the preservation of capital adequacy mechanisms following the Effective Date; and
- no material change in the proprietary rights of members of NOE following the Effective Date.

2.1.5. I am relying on NOE and MSMI to inform me, the Regulator and the Court of anything that may affect the conclusions contained within this Scheme Report that may occur between the date of this Scheme Report and the Effective Date. Examples of such changes include, but are not restricted to:

- any modifications or additions to the Scheme;
- any modifications to the business plans of any company involved in the Scheme;
- any changes in reserving strategy and methodology;
- any events that NOE or MSMI would consider likely to give rise to a material adjustment to the reserves; and
- any material change in the value and make-up of the assets and liabilities being transferred or remaining as part of the Scheme.

- 2.1.6.** There is a possibility that I may need to revisit these items prior to the final Court hearing at which the Scheme will be considered. In any event, the financial data and information in this Scheme Report relates primarily to the financial year ending 20 February 2014 and at the time of preparation of this Scheme Report, I did not have access to any financial reports and accounts for the financial year ending 20 February 2015. In the light of this, a supplementary report will be produced prior to the final Court hearing. The supplementary report will include audited figures for the year ending 20 February 2015 and will confirm whether or not there are any significant changes to the conclusions contained in this Scheme Report.
- 2.1.7.** In this Scheme Report I have also considered the impact of the recent merger of NOE and SMMI. On 28 February 2014 SMMI became a wholly owned subsidiary of NOE with NOE being the sole member of SMMI. Post-merger, SMMI changed its name to SMI.

2.2. Use of this Scheme Report

- 2.2.1.** This Scheme Report has been prepared to inform the Court of the likely effect of the Scheme upon Affected Policyholders and members of MSMI and NOE. It has been prepared solely for the purposes of the FSMA requirements for insurance business transfer schemes and solely in respect of the Scheme.
- 2.2.2.** A copy of this Scheme Report will be made available to the Regulator and the Court. A copy of this Scheme Report and a statement setting out the terms of the Scheme (and containing a summary of the Scheme Report) will be given free of charge to any person who requests them.
- 2.2.3.** I assume no responsibility whatsoever in respect of, arising out of, or in connection with the contents of this Scheme Report to parties other than those mentioned above. If other parties choose to rely in any way on the contents of this Scheme Report then they do so entirely at their own risk.
- 2.2.4.** Draft versions of this Scheme Report and any other interim working papers must not be relied on by any person for any purpose.

2.3. Uncertainty

There is always an element of uncertainty surrounding the calculation of liabilities associated with general insurance transactions, including transfers of insurance policies. I have taken into account this uncertainty in reaching my conclusions in this Scheme Report.

3. Description of the Scheme, policies and participating insurers

3.1. The Scheme

The proposed Scheme is to transfer all of the insurance business of MSMI to NOE pursuant to Part VII of the FSMA. Provided it is sanctioned, the Scheme will become effective on the Effective Date. Under the Scheme, all policies of MSMI will be transferred to NOE together with all the liabilities and assets of MSMI. The intention is that MSMI will subsequently be dissolved. Until MSMI's authorisation is cancelled, it must retain a Minimum Capital Requirement (MCR) and thus the Scheme allows for the value of assets to be transferred to be reduced to the extent necessary to maintain MSMI's MCR, with the remaining balance to be transferred as soon as possible following MSMI's de-authorisation.

3.2. Background and Purpose of the Scheme

- 3.2.1.** MSMI was incorporated under the Companies Acts 1948 to 1967 in England and Wales on 11 August 1972 as a company limited by guarantee and has no share capital. It was a mutual company originally owned by its members (but see sections 3.2.2, 3.2.11 and 3.2.12 below). The objects of MSMI are to insure its members' ships upon the mutual principle against every description of marine and transit risks that may be lawfully undertaken. It is authorised under the FSMA to carry out contracts of general insurance of various classes and its main business consists of hull and machinery insurance covering risks of loss or damage to the hull and machinery of ships. Some of the policies issued by MSMI can also provide cover in respect of risks arising out of the total loss of a ship and loss of income arising from loss or damage to a ship.
- 3.2.2.** MSMI is now a wholly owned subsidiary of NOE as shown in Appendix C and has ceased underwriting new business. NOE is now the only member of MSMI as explained in more detail below in sections 3.2.11 and 3.2.12.
- 3.2.3.** MSMI is a "UK authorised person" as defined in Section 191G of the FSMA, with permission to carry out contracts of general insurance in the UK under classes of business 1, 4, 5, 6, 7, 11, 12 and 15 set out in Part I of Schedule 1 to the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (S.I. 2001/544). Prior to cessation of underwriting, MSMI's permission to carry on regulated activities under Part IV of the FSMA also included effecting contracts of insurance in EEA states other than the United Kingdom.
- 3.2.4.** NOE was incorporated under the Companies Act 1948 in England and Wales on 13 March 1952 as a company limited by guarantee and has no share capital. It is a mutual company owned by its members. The objects of NOE are to carry on marine and transit insurance business. It is authorised under the FSMA to carry out contracts of general insurance of various classes and its main business consists of Protecting and Indemnity (liabilities, costs and expenses arising in respect of cargo, seamen and passengers as well as third party liabilities in respect of pollution, property damage, wreck removal, salvage and collision), Freight Demurrage & Defence (legal costs and expenses in relation to a range of disputes) and War Risks (losses caused by war and terrorism or as consequence of a ship being blocked or trapped in an area of conflict).
- 3.2.5.** NOE is open to the writing of new business and also provides reinsurance to a small number of businesses operating in the marine insurance sector.
- 3.2.6.** NOE is a "UK authorised person" as defined in Section 191G of the FSMA, with permission to effect and carry out contracts of general insurance in the UK under classes of business 1, 4, 5, 6, 7, 11, 12, 15 and 17 set out in Part 1 of Schedule 1 to the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (S.I. 2001/544). NOE's permission to carry on regulated activities under Part IV of the FSMA also includes effecting contracts of insurance in EEA states other than the United Kingdom.

- 3.2.7.** The basic principal of mutuality which underpins the activities of NOE is that the members of the company for each class of business (P&I, FD&D and War Risks separately) and for each policy year insure each another against the liabilities, losses, costs and expenses which they or any of them may become liable to pay in respect of any ship entered during the relevant policy year. The rules of NOE contain provisions which provide wide powers to call upon members to contribute funds for that purpose.
- 3.2.8.** The liability of a member of NOE to make contributions in respect of a policy year will ordinarily continue for so long as that policy year remains “open” or a “Release Call” is paid in order to release the member from any further liability to make contributions. Policy years usually remain open until such time as the directors of the company are satisfied that the claims, expenses and outgoings arising in respect of that policy year have largely been satisfied and no further contributions are required from the members of that policy year; at which time the directors will ordinarily declare the relevant policy year closed and the members of that policy year will normally have no further liability to make further contributions in respect of that policy year. However, the rules do provide for the directors to take action if, at any time or times after a policy year has been closed, it appears that the claims, expenses and outgoings arising in respect of that policy year exceed or are likely to exceed the totality of the contributions and other receipts in respect of such policy year. This action can include:
- transferring funds from the reserves of NOE;
 - transferring funds standing to the credit of any different closed policy year;
 - making an Additional Call (contributions from members) in respect of an open policy year with the intention of applying a part thereof to meet any such deficiency.
- 3.2.9.** To the extent that any claims, expenses and outgoings for a policy year remain outstanding at the time of closure it is usual for such claims, expenses and outgoings to be amalgamated with those of the remaining open policy years. As at the date of this Scheme Report, NOE had four open policy years (namely: 2012/2013, 2013/2014, 2014/15 & 2015/16) and as at 20 February 2014, MSMI had four open policy years (namely: 2007/2008, 2008/2009, 2009/2010 & 2010/2011). On 6 May 2014, the MSMI Board closed the 2007/08, 2008/09 and 2009/10 policy years and the outstanding claims for those and prior policy years were incorporated into the 2010/11 policy year. The outstanding obligations and liabilities of NOE and MSMI therefore predominantly relate to entries made in these open policy years.
- 3.2.10.** During the course of 2010 the directors of MSMI undertook a review of its future strategy and concluded that, although MSMI was financially sound and well reserved, its relatively small scale business model was unlikely to be viable in the foreseeable economic climate. MSMI ceased underwriting new business with effect from 30 June 2011 and is in the process of managing the run off of its outstanding liabilities, which comprises direct insurance business only and no inwards reinsurance.
- 3.2.11.** The directors of MSMI then gave consideration to the options available to MSMI in respect of the handling and run off of its outstanding liabilities. As a result of this process NOE made an offer to acquire MSMI which was approved by the members of MSMI at an extraordinary general meeting held on 22 June 2011. The terms of this acquisition were subsequently set out in a Framework Agreement dated 23 August 2011. The transaction contemplated under the terms of the Framework Agreement was subject to the Regulator’s approval of NOE as the controller of MSMI pursuant to Part XII FSMA (Change in Control), which was given by the Regulator on 10 August 2011.
- 3.2.12.** On 2 November 2011 a transaction was completed which resulted in MSMI becoming a wholly owned subsidiary of NOE with NOE becoming the sole member of MSMI. From this date NOE allocated US\$7.2 million of capital to MSMI by way of an inter-company debtor/creditor transaction to cover the Regulator solvency capital requirements under

Solvency I. This transaction was in accordance with the Framework Agreement, resulting in the consequent distribution of a proportion of MSMI's reserves to its former members. The period for claiming a distribution payment expired on 2 November 2012 and there is no further liability to former MSMI members for the distribution payments. All former members of MSMI are now released from any further liability to make contributions to, and from rights to access, the funds of MSMI.

- 3.2.13.** At the same date of 2 November 2011 a reinsurance to close transaction was effected by NOE and MSMI resulting in the Reinsurance Agreement under which NOE reinsures 100% of the risks insured by MSMI net of amounts recovered from or recoverable under other External Reinsurance Arrangements entered into by MSMI. The reinsurance premium payable by MSMI to NOE was equal to the net assets of MSMI as at 2 November 2011. Thus, the liabilities of MSMI (net of the liabilities reinsured under the External Reinsurance Arrangements) are currently the liabilities of NOE.
- 3.2.14.** Following completion of the aforementioned transactions MSMI issued a circular to its brokers, directors and former members to confirm completion and provide notice of its intention to undertake a Part VII Transfer. Under the Part VII Transfer, referred to as the Scheme in this Scheme Report, former members of MSMI who are all now policyholders of MSMI (without members' rights) will become policyholders of NOE without members' rights.
- 3.2.15.** Subject to the Scheme being approved and there being no excluded policies, all policyholders of MSMI will become policyholders of NOE, the Reinsurance Agreement between MSMI and NOE will cease to exist and all the External Reinsurance Arrangements with External Reinsurance Parties will be transferred from MSMI to NOE.
- 3.2.16.** NOE has a long standing relationship with MSMI having managed its business since it was founded in 1972 either directly or, as has been the case since December 2000, through its wholly owned management company, North Insurance Management Limited (NIML). The Management Agreement was in effect since November 2003 and terminated on 30 June 2013 in anticipation of the Scheme taking effect, the required notice of termination of two years having been given by MSMI to NOE and NIML in a letter dated 20 June 2011. Following this termination, an Interim Management Agreement took effect to provide for NIML to continue to manage the business of MSMI to the same standards of service as under the Management Agreement. Under the terms of the Framework Agreement NOE gave an undertaking to MSMI to the effect that policyholder claims of MSMI would continue to be handled in substantially the same manner as they were handled prior to the acquisition of MSMI by NOE.
- 3.2.17.** Having MSMI as a separate wholly owned subsidiary still requires MSMI to separately prepare financial statements and to pay separate costs for audit, compliance and management. Such administrative burdens and costs are likely to increase with the forthcoming Solvency II regime effective from 1 January 2016. As a separate company, MSMI also needs to maintain a certain level of capital under the requirements of the current Solvency I and FSA Individual Capital Adequacy Standards (ICAS regime), and under the forthcoming Solvency II regime. The level of capital will be subject to a minimum level irrespective of the size of the business still in run-off and over time would become a disproportionate amount compared to the size of the liabilities; whereas after the Scheme is effected, as a small part of NOE's overall liabilities, the capital requirement in respect of the former MSMI liabilities would in all likelihood decrease as the liabilities decrease.
- 3.2.18.** **The main purpose of the Scheme, as confirmed in discussions with NOE management, is to achieve a more efficient use of capital and savings in costs by managing one company, NOE, rather than managing two separate companies, NOE and MSMI. I have no reason to doubt that this is likely to be the beneficial outcome of the Scheme given the arguments presented in 3.2.17 above.**

4. Transferring policyholders of MSMI

4.1. The financial and non-financial impacts

4.1.1. MSMI closed to new business on 30 June 2011 and is in run off. As at the 20 February 2014 financial year end, the insurance liabilities of MSMI primarily comprised the claims outstanding (both reported and those yet to be reported) relating to the four open policy years of 2007/2008, 2008/2009, 2009/2010 and 2010/2011. On 6 May 2014 the MSMI Board closed the 2007/08, 2008/09 and 2009/10 policy years and the outstanding claims for those and prior policy years were incorporated into the 2010/11 policy year. At the financial year end of 20 February 2014, the total technical provisions for gross claims outstanding as shown in the balance sheet of the “Strategic Report, Directors Report and Financial Statements for the year ended 20 February 2014” (an extract is shown in Appendix F) was US\$19,330,000. These gross liabilities were 100% reinsured as follows:

- US\$13,429,000 under External Reinsurance Arrangements with External Reinsurance Parties, and
- US\$5,901,000 under the Reinsurance Agreement with the parent company NOE.

4.1.2. All MSMI policies are of the same class and provide cover for Hull and Machinery. In respect of the open policy years (mentioned in 4.1.1. above) as at the financial year end of 20 February 2014 the insurance business of MSMI comprised 699 vessels, 1904 policies and 414 policyholders. The figures shown in 4.1.1 and 4.1.2 are summarised in **Table A** shown in section 1.7.1 of this Scheme Report.

4.1.3. The Scheme provides for all the External Reinsurance Arrangements to be transferred from MSMI to NOE such that no change is envisaged pre- and post-Effective Date. Appendix G shows a summary of the External Reinsurance Arrangements, which are all subject to English Law and the jurisdiction of the English Courts. The External Reinsurance Arrangements are spread over a number of different External Reinsurance Parties. The External Reinsurance Parties were informed of the 2 November 2011 change of control of MSMI (pursuant to Part XII of the FSMA), which resulted in MSMI becoming a wholly owned subsidiary of NOE and such External Reinsurance Arrangements continued without change. **The External Reinsurance Parties will be notified of the Scheme and the External Reinsurance Arrangements will continue with the same financial effects and service standards pre- and post-Effective Date. My conclusion is based on the fact that the reinsured liabilities and the reinsurers will not change as a result of the Scheme.**

4.1.4. Prior to the Scheme taking effect, if MSMI suffered a deteriorating claims experience with the need to increase claims payments and claims technical provisions, NOE as part reinsurer of MSMI and the External Reinsurance Parties would be liable to increase their claims payments and claims technical provisions, with the effect being no change in the net technical provisions of zero for MSMI. For NOE, any such increase would have to come from any surplus assets (free reserves) in NOE or by way of a call to NOE’s members. Post-Effective Date, any additional funds to cover such a deterioration in the net (of External Reinsurance Arrangements) claims experience of the former MSMI policies would also have to come from surplus assets of NOE or by way of a call to NOE’s members. **Thus, I conclude that the Scheme has no effect on the risks facing MSMI or NOE as a result of such a deteriorating claims experience.**

4.1.5. Prior to the Scheme taking effect, if one or more of the External Reinsurance Parties were to default on their liabilities to MSMI, the additional funds required by MSMI would have to come from any surplus assets (free reserves) in MSMI, which as shown in **Table B** (in section 1.7.4 of this Scheme Report) amounted to some 30.1% of the gross technical provisions for MSMI claims in the balance sheet of 20 February 2014. As NOE is the sole member of MSMI (and MSMI being a wholly owned subsidiary of NOE), any additional funds required by MSMI to replenish such surplus or for any other reason would have to come

from any surplus assets in NOE or by way of a call to NOE's members. As can be seen from **Table B**, NOE had surplus assets (as shown in the consolidated balance sheet of 20 February 2014 that included MSMI) that amounted to 32.1% of the gross technical provisions for claims of NOE and MSMI combined and the gross technical provisions for claims of MSMI amounted to only 2.0% of the gross technical provisions for claims of NOE and MSMI combined. **I conclude that, since the total gross claims of MSMI are relatively minor compared to the consolidated NOE total gross claims and NOE's surplus assets, a reinsurance default by one or more of the External Reinsurance Parties would be unlikely to cause any financial problems due to the fact that NOE would in all likelihood put additional funds as required in MSMI. Moreover, NOE's reputation in the market would suffer if such additional funds were not forthcoming.**

- 4.1.6.** The situation with regard to a possible default of one or more of the External Reinsurance Parties post-Effective Date would be that any additional funds would come from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. Whilst pre-Effective Date the MSMI policyholders benefit from the dedicated protection of US\$5,810,000 of free assets, this protection amounts to 30.1% of the MSMI gross technical provisions for claims; whereas post-Effective Date they will benefit (along with all other policyholders in NOE) from the protection of US\$312,274,000 of free assets amounting to 32.1% of the gross technical provisions for claims. **Thus, I conclude that the Scheme will have minimal effect on the protection afforded to MSMI policyholders against a default by one or more of the External Reinsurance Parties.**
- 4.1.7.** The estimation of technical provisions for claims for insurance business is an inherently uncertain exercise. The claims distribution of potential losses for MSMI is positively skewed in that claims cannot be less than zero but can be many times larger than the average loss (alternatively, this can be viewed as a distribution of potential losses having a higher frequency of lower value losses, and a lower frequency of higher value losses, e.g. observed losses of: 1, 2, 3, 4, 100). As the claims distribution is positively skewed, a best estimate or most likely outcome for claims outstanding would represent a level above the 50th percentile level of confidence. I have examined the basis for establishing the MSMI technical provisions for claims outstanding, which I believe is actuarially sound and cautious representing an approximate 90th percentile level of confidence (90% probability of being sufficient to meet all the claims and 10% probability of not being sufficient to meet all the claims). **Table B** (in section 1.7.4 of this Scheme Report) shows the gross (before reinsurance) technical provisions for claims outstanding of the insurance business of MSMI and the surplus assets (free reserves) in excess of the liabilities available in the balance sheet of 20 February 2014. The gross technical provisions for claims outstanding amounted to US\$19,330,000 and the surplus assets amounted to US\$5,810,000 or 30.1% of the gross technical provisions for claims outstanding.
- 4.1.8.** The claims distribution of potential losses for NOE is also positively skewed with a best estimate or most likely outcome for claims outstanding representing a level above the 50th percentile level of confidence. I have examined the basis for establishing the NOE technical provisions for claims outstanding, which I believe is actuarially sound and cautious representing an approximate 95th percentile level of confidence. As MSMI is a wholly owned subsidiary of NOE, the NOE balance sheet of 20 February 2014 consolidated both the NOE and MSMI balance sheet figures. **Table B** shows the NOE consolidated gross technical provisions for claims outstanding for insurance business of US\$973,047,000. The surplus assets (free reserves) available in the consolidated balance sheet amounted to US\$312,274,000 or 32.1% of the gross technical provisions for claims outstanding. As the net (of External Reinsurance Arrangements) technical provisions for claims outstanding of MSMI are already reinsured with NOE under the Reinsurance Agreement, the MSMI policyholders already benefit to a certain extent from the greater financial strength shown by the combined balance sheet.
- 4.1.9.** Both MSMI and NOE were managed by NIML. During 2014 NOE changed its management structure with effect that NIML is no longer involved in the management of NOE and management responsibility was transferred directly to NOE management. NIML still

currently manages MSMI under the Interim Management Agreement, but post-Effective Date its business will be managed directly by NOE management. In practical terms there will be no change to the personnel responsible for managing NOE and MSMI business pre- and post-Effective Date. From discussions with NOE management, no changes to the accounting and reserving standards are envisaged post-Effective Date. For both MSMI and NOE, the loss reserves or technical provisions are calculated using cautious bases (to the 90th and 95th percentiles respectively) and it is my opinion, from discussions with NOE management, that this will continue post-Effective Date and that the Scheme will have no impact on the value of the respective liabilities that originated in MSMI or NOE. The fact that MSMI aims for a 90th percentile and NOE aims for a 95th percentile are purely for historical reasons and the type of business insured by MSMI is different from the business insured by NOE.

- 4.1.10.** All policyholders in MSMI are direct insurance policyholders and prior to the Effective Date all would rank equally in priority in any insolvency situation subject to The Insurers (Reorganisation and Winding Up) Regulations 2004. Post-Effective Date, all direct policyholders in NOE (whether members or non-members) would rank equally in priority in any such insolvency situation.
- 4.1.11.** Although the Scheme will not take place until the Effective Date and the financial figures will change over time, I have no reason to believe that the financial strength of NOE immediately post-Effective Date will be different from the situation immediately before the Effective Date. **I conclude from the figures shown in Table B that the policyholders of MSMI will benefit directly from a greater level of surplus assets (expressed as a percentage of the gross technical provisions for claims) as part of the larger company NOE than if MSMI were a totally separate company.**
- 4.1.12.** I have considered the Solvency I, ICAS and Solvency II capital situation in section 7 of this Scheme Report where **I conclude that NOE has the greater financial strength when compared to MSMI and that post-Effective Date, the transferred MSMI policyholders will benefit from the greater financial strength of NOE.**
- 4.1.13.** Under the terms of the Framework Agreement NOE gave an undertaking to MSMI to the effect that policyholder claims of MSMI would continue to be handled in substantially the same manner as they were handled prior to the acquisition of MSMI by NOE. NIML manages the MSMI policies now and Post-Effective Date, the transferred MSMI policies will continue to be managed by the same personnel in NOE. **Thus, I conclude that the Scheme will have no impact on the standards of service given to MSMI policyholders.**

5. Remaining policyholders and member of MSMI

5.1. The financial and non-financial impacts

- 5.1.1.** The intention of the Scheme is that all the policies of MSMI will transfer to NOE at the Effective Date and that there will be no remaining policies in MSMI post-Effective Date. NOE management are of the opinion that there are no individual policies or groups of policies insured by MSMI that are expected to be problematic in this regard and their expectation is that all policies in MSMI will transfer to NOE on the Effective Date. I concur with this expectation.
- 5.1.2.** Although the intention is for all the policies to transfer to NOE, the Scheme does allow for the possibility of some policies remaining within MSMI post-Effective Date in the event that there is some unforeseen reason why they cannot be transferred to NOE on the Effective Date, these policies being referred to as Residual Policies. The Scheme allows for any such Residual Policies to be reinsured from MSMI to NOE under a reinsurance contract, referred to as the Residual Policies Reinsurance Contract (the terms and conditions of which are based on the Reinsurance Agreement). In this event, MSMI would need to remain operational but only until such time as the Residual Policies are transferred to NOE by other means. The Scheme places an obligation on both MSMI and NOE to enable the later inclusion of Residual Policies. Thus, any such Residual Policies will be subsequently transferred to NOE and the ultimate intention is that all MSMI policies will be transferred to NOE and that MSMI will be dissolved.
- 5.1.3.** **My conclusion is that, in the unlikely event that there are Residual Policies, the situation for any such policies would be substantially the same pre- and post-Effective Date as they are currently reinsured with NOE under the existing Reinsurance Agreement pre-Effective Date and would be reinsured with NOE under the Residual Policies Reinsurance Contract post-Effective Date.**
- 5.1.4.** There are no proprietary members' rights issues to consider in the unlikely event that there are Residual Policies since NOE is the sole member of MSMI pre-Effective Date and would continue to be the sole member of MSMI post-Effective Date until such time as MSMI is dissolved.

6. Current policyholders and members of NOE

6.1. The financial and non-financial impacts

- 6.1.1.** NOE operates predominantly upon a mutual model of business whereby the persons that enter ships for insurance are automatically appointed as members of NOE until such time as the entry ceases or is terminated. The relationship that exists between NOE and policyholders is based upon the provisions of the NOE Articles of Association with regards to membership. Whilst policyholders are usually members, the NOE Articles of Association do allow for some risks to be underwritten whereby the policyholders do not become members in the sense of having full mutual membership rights and obligations. **Table C** in section 1.9.1 shows the NOE numbers of insured vessels, insured vessels with members' rights, insured vessels without members' rights and policyholders for the currently open policy years. The Reinsurance Agreement (between NOE and MSMI) does not give the policyholders of MSMI any members' rights in NOE. Post-Effective Date the policyholders of MSMI will become policyholders of NOE but with no members' rights in respect of the MSMI policies transferred to NOE.
- 6.1.2.** As at the date of this Scheme Report, NOE had four open policy years (namely: 2012/2013, 2013/2014, 2014/2015 & 2015/16) and as at the financial year ending 20 February 2014 MSMI had four open policy years (namely: 2007/2008, 2008/2009, 2009/2010 & 2010/2011). On 6 May 2014 the MSMI Board closed the 2007/08, 2008/09 and 2009/10 policy years and the outstanding claims for those and prior policy years were incorporated into the 2010/11 policy year. The outstanding obligations and liabilities of NOE and MSMI therefore predominantly relate to entries made in these open policy years.
- 6.1.3.** The outstanding obligations and liabilities of MSMI are relevant in that pre-Effective Date, all insurance risks of MSMI (net of the risks reinsured under the External Reinsurance Arrangements with External Reinsurance Parties) are reinsured with NOE under the Reinsurance Agreement and, in accordance with Clause 2.3 of the Reinsurance Agreement, form part of the P&I class of business within NOE. The P&I class of business is by far the largest part of the insurance liabilities of NOE and represents over 96% of the insurance liabilities (as at 20 February 2014). If the Scheme is sanctioned, on the Effective Date all assets and liabilities of MSMI will be transferred to NOE.
- 6.1.4.** Prior to the Scheme taking effect, the insurance risks of MSMI are 100% reinsured and if it suffered a deteriorating claims experience with the need to increase claims payments and claims technical provisions, NOE as part reinsurer of MSMI and the External Reinsurance Parties would be liable to increase their claims payments and claims technical provisions. For NOE, any such increase would have to come from any surplus assets in NOE or by way of a call to NOE's members. Post-Effective Date, any additional funds to cover such a deterioration in the net (of External Reinsurance Arrangements) claims experience of the former MSMI policies would also have to come from surplus assets of NOE or by way of a call to NOE's members. **Thus, based on the assumption that the External Reinsurance Parties would honour their commitments under the External Reinsurance Arrangements, I conclude that the Scheme has no material effect on the net risks facing NOE as a result of such a deteriorating claims experience.**
- 6.1.5.** Prior to the Scheme taking effect, if one or more of the External Reinsurance Parties were to default on their liabilities to MSMI, the additional funds required by MSMI would have to come from any surplus assets in MSMI, which as shown in **Table B** in section 1.7.4 of this Scheme Report amounted to some 30.1% of the gross technical provisions for MSMI claims in the balance sheet of 20 February 2014. As NOE is the sole member of MSMI (and MSMI being a wholly owned subsidiary of NOE), any additional funds required by MSMI to replenish such surplus or for any other reason would have to come from any surplus assets in NOE or by way of a call to NOE's members. As can be seen from **Table B**, NOE had surplus assets (as shown in the consolidated balance sheet of 20 February 2014 that included MSMI) that amounted to 32.1% of the gross technical provisions for claims of NOE

and MSMI combined and the gross technical provisions for claims of MSMI amounted to only 2.0% of the gross technical provisions for claims of NOE and MSMI combined. Since the total gross claims of MSMI are relatively minor compared to the consolidated NOE total gross claims and NOE's surplus assets, a reinsurance default by one or more of the External Reinsurance Parties would be unlikely to cause any financial problems whereby NOE would not put additional funds as required in MSMI. Moreover, NOE's reputation in the market would suffer if such additional funds were not forthcoming.

- 6.1.6.** The situation with regard to a possible default of one or more of the External Reinsurance Parties post-Effective Date would be that any additional funds would come from the surplus assets in NOE and, if any further funds were required, this would come from a call on NOE's members. As can be seen from **Table A** in section 1.7.1 of this Scheme Report (and based on figures at 20 February 2014), the situation pre-Effective Date is that NOE directly reinsures US\$5,901,000 of the total gross technical provisions for claims of MSMI, with the External Reinsurance Parties reinsuring the balance of US\$13,429,000. Post-Effective Date, NOE will directly insure the total US\$19,330,000 of MSMI gross technical provisions for claims, with US\$13,429,000 being reinsured with the External Reinsurance Parties, leaving NOE a net of reinsurance liability of US\$5,901,000. Thus, the Scheme has no effect on the net liabilities of NOE that derive from the MSMI policies. **I conclude that, whilst the situation post-Effective Date is different from that pre-Effective Date in that NOE assumes the whole risk of a default by one or more of the External Reinsurance Parties, in a practical sense for the reasons set out in section 6.1.5 above, the risks facing NOE and its members are little changed by the Scheme.**
- 6.1.7.** Prior to the Effective Date all direct insurance policyholders in NOE (whether members or non-members) would rank equally in priority in any insolvency situation subject to The Insurers (Reorganisation and Winding Up) Regulations 2004. In any such situation, inwards reinsurance business would rank below direct insurance policyholders. In any such insolvency situation post-Effective Date, policyholders with policies transferred to NOE from MSMI would rank equally in priority to all other direct insurance policyholders in NOE and thus, would rank above any NOE inwards reinsurance business. However, the total net technical provisions for claims of NOE are unchanged by the transfer of the MSMI policies and the total gross technical provisions for claims of the transferring MSMI policies amount to only 2.0% of the total gross technical provisions for claims of MSMI and NOE combined.
- 6.1.8.** **Thus, I conclude that the Scheme has no material financial impact on the policyholders who are also members of NOE and no material impact on the proprietary interests of the members of NOE.** The only other consideration is that of policyholders of NOE who are not members. Again, there is no material financial impact since MSMI is already owned by NOE and all liabilities of MSMI (net of the liabilities reinsured under the External Reinsurance Arrangements) are reinsured with NOE under the Reinsurance Agreement. Moreover, the total gross technical provisions for claims of the transferring MSMI policies amount to only 2.0% of the total gross technical provisions for claims of MSMI and NOE combined and thus have a minimal impact on the risk profile of NOE. Even if all the External Reinsurance Parties defaulted (a most unlikely scenario), the extra liabilities falling to NOE would amount to US\$13,429,000 (as shown in **Table A**), which represents only 4.3% of the excess assets (free reserves) of US\$312,274,000 of MSMI and NOE combined. **Thus, I conclude that the Scheme will not have a material effect on NOE's risk profile and policyholders whether as a going concern business or in an insolvency situation.**

7. The capital situation under Solvency I, ICAS and Solvency II

7.1. Consideration of the Solvency I capital position

7.1.1. Form 1 of the MSMI PRA Return for financial year ended 20 February 2014 gives the published "Statement of solvency" for MSMI. This shows capital resources (the excess of admissible assets over the liabilities) of US\$7,628,000 for MSMI as at 20 February 2014 and a Solvency I Capital Resources Requirement (CRR) of US\$3,667,000. Thus, as at 20 February 2014, there was a surplus of US\$3,961,000 in the available capital resources to cover the CRR. To put it another way, the **capital resources expressed as a percentage of the CRR was 208.0% for MSMI.**

7.1.2. Form 1 of the NOE PRA Return for financial year ended 20 February 2014 gives the published "Statement of solvency" for NOE. As MSMI is a wholly owned subsidiary of NOE, this is a combined PRA Return incorporating the MSMI assets and liabilities. This shows capital resources (the excess of admissible assets over the liabilities) of US\$348,811,000 as at 20 February 2014 and a Solvency I Capital Resources Requirement (CRR) of US\$89,580,000. Thus, as at 20 February 2014, the excess of available capital resources to cover the CRR was US\$259,231,000. To put it another way, the **capital resources expressed as a percentage of the CRR was 389.4% for NOE (combined with MSMI).**

7.1.3. The Solvency I capital situation is summarised in **Table F** below:

Table F		
MSMI and NOE Solvency I capital resources* and CRR **		
US \$	MSMI	NOE #
Available capital resources*	7,628,000	348,811,000
Solvency I CRR **	3,667,000	89,580,000
Capital resources * expressed as a percentage of the CRR **	208.0%	389.4%
* The excess of Solvency I admissible assets over liabilities <i>at 20 February 2014</i>		
** Solvency I Capital Resources Requirement <i>at 20 February 2014</i>		
# NOE shows figures from the combined FSA Returns that includes MSMI		

7.1.4. The available figures for SMI are from the PRA Return for financial year ended 31 December 2013 and are expressed in £ sterling as shown below in **Table G**. This shows capital resources (the excess of admissible assets over the liabilities) of £32,562,000 for SMI as at 31 December 2013 and a Solvency I Capital Resources Requirement (CRR) of £9,370,000. Thus, as at 31 December 2013, there was a surplus of £23,192,000 in the available capital resources to cover the CRR. To put it another way, the **capital resources expressed as a percentage of the CRR was 347.5% for SMI.**

Table G	
SMI Solvency I capital resources # and CRR ##	
UK £	SMI
Available capital resources #	32,562,000
Solvency I CRR ##	9,370,000
Capital resources # expressed as a percentage of the CRR ##	347.5%
# The excess of Solvency I admissible assets over liabilities <i>at 31 December 2013</i>	
## Solvency I Capital Resources Requirement <i>at 31 December 2013</i>	

- 7.1.5.** A further measure of the Solvency I capital is given by the Enhanced Capital Requirement (ECR). As at 20 February 2014, although not a publicly disclosed figure, NOE (including the assets and liabilities of MSMI) had available capital resources in excess of the ECR. As at 31 December 2013 SMI also had available capital resources in excess of the ECR.
- 7.1.6.** Although the Scheme will not take place until the Effective Date and the financial figures will change over time, I have no reason to believe that the Solvency I strength (as indicated by the capital resources compared to the CRR, ECR and to the gross technical provisions) of NOE immediately post-Effective Date will be different from the situation immediately before the Effective Date.
- 7.1.7. The figures in Table F above show that NOE has the greater Solvency I financial strength when compared to MSMI.** As the net (of External Reinsurance Arrangements) liabilities of MSMI are already reinsured with NOE under the Reinsurance Agreement, the MSMI policyholders already benefit to a certain extent from the greater financial strength shown by the combined FSA Return. The figures shown in Table G above indicate that MSMI has a Solvency I financial strength not too dissimilar from NOE. **My conclusion is that Post-Effective Date, the transferred MSMI policyholders will benefit from the greater Solvency I financial strength of NOE as shown by the combined FSA Return of NOE.**

7.2. Consideration of the ICAS and Solvency II capital position

- 7.2.1.** Solvency II is the new insurance regulatory regime with an implementation date of 1 January 2016. This will impose new rules for the calculation of liabilities, assets and capital requirements. In simplistic terms, the liabilities and assets will be calculated on a more realistic basis (essentially market values) and the capital requirements will more realistically reflect the risks being undertaken by the insurance company. The amount of the required capital under Solvency II will be in the public domain as part of the disclosed financial statements.
- 7.2.2.** At the current time in the UK, all insurance companies have to carry out additional calculations of capital in accordance with the Individual Capital Adequacy Standards (ICAS) resulting in an Individual Capital Assessment (ICA), which more realistically reflects the risks being undertaken by the insurance company. This measure of the required capital is not in the public domain but is a Regulator requirement. Whilst there are some fundamental differences between the proposed Solvency II capital requirements and the ICA, they are both methodologies that reflect more accurately (than the current Solvency I requirements) the risks being undertaken by individual insurance companies and groups. Some insurance companies do base their ICA calculations on the proposed Solvency II methodology.
- 7.2.3.** NOE's calculation of the ICA for 20 February 2014 was based on the proposed Solvency II methodology that was tested on an industry-wide basis within Europe (including the UK) and is commonly referred to as QIS5 (Quantitative Impact Study 5).
- 7.2.4.** Although not a publicly disclosed figure, the ICA methodology (based on the Solvency II methodology) for NOE as at 20 February 2014 showed that NOE had capital resources in excess of the ICA capital requirement. The calculation of the NOE ICA for 20 February 2014 included the liabilities and assets of MSMI, as it is a wholly owned subsidiary of NOE. **In my opinion, this excess capital represented a healthy surplus of capital in terms of the financial security for policyholders.**
- 7.2.5.** The 31 December 2013 calculations for SMI also showed capital resources in excess of the ICA and Solvency II capital requirements.

- 7.2.6.** Whilst the Scheme will not take place until the Effective Date and the financial figures will change over time, I have no reason to believe that the ICA (and Solvency II) strength (as indicated by the capital resources compared to the ICA capital requirement) of NOE immediately post-Effective Date will be different from the situation immediately before the Effective Date.
- 7.2.7.** As the net (of External Reinsurance Arrangements) liabilities of MSMI are already reinsured with NOE under the Reinsurance Agreement, the MSMI policyholders already benefit to a certain extent from the greater financial strength of NOE. **My conclusion is that Post-Effective Date, the transferred MSMI policyholders will benefit from the greater financial strength of NOE.**
- 7.2.8.** With regard to the preparedness of the NOE Group of companies for Solvency II; the transition to Solvency II is being overseen by NOE's Global Director (Finance), Jeff O'Neill, and my understanding is that NOE has a Solvency II implementation plan for the Group to ensure readiness for 1 January 2016. As MSMI, SMI and NOE are part of the same Group and NOE is preparing for Solvency II on a group basis, I do not expect that the Scheme will make any difference to MSMI from a Solvency II readiness and compliance point of view. The NOE Group will use the Standard Formula approach rather than an Internal Model for Solvency II purposes.

8. Communication and notification aspects of the Scheme

8.1. Objectives of the communication

8.1.1. The companies (NOE and MSMI) involved in the Scheme have set out the approach they intend to take in communicating information about the proposed transfer of business to the affected policyholders and other parties.

8.1.2. The main objectives of the communications are:

- Give policyholders the information they need to understand the proposed changes;
- Inform affected policyholders about the implications for them of the proposed changes;
- Give affected policyholders access to further information;
- Let affected policyholders know how to object to the proposed changes;
- Maintain customers' confidence in MSMI and NOE to continue to meet their obligations under transferring and non-transferring policies; and
- Meet legal and regulatory requirements.

8.1.3. Regulations made under the FSMA require a communication regarding the proposed transfer to be sent to every policyholder of the parties to the Scheme unless the Court waives this requirement. However, consideration may be given to the practicality and costs of sending notices against the likely benefits for policyholders of receiving such communications. In order to comply with FCA Handbook section SUP 18.2.46G and PRA's Insurance Business Transfers Statement of Policy section 2.53, the companies would be expected to notify the policyholders, or interested persons, at least six weeks before the date of the Court hearing at which the application to sanction the Scheme will be heard. The companies intend to comply with this guidance in the manner outlined below.

8.2. Publications in Newspapers

8.2.1. Pursuant to regulation 3(2)(a)(i) of the Financial Services and Markets Act 2000 (Control of Business Transfers) (Requirements on Applicants) Regulations 2001 ("the Transfer Regulations"), a notice will be published once each in the London Gazette, the Edinburgh Gazette and the Belfast Gazette.

8.2.2. The Transfer Regulations also contain requirements for notice of the Part VII application to be published in two national newspapers in the UK and two national newspapers in any EEA State where the risk is "situated", in relation to any policy included in the transfer (other than a policy which evidences a contract of reinsurance). Dispensation is being sought from these requirements and it is proposed that a notice will instead be published in the following publications:

- The Financial Times (International Edition)
- Tradewinds, a leading weekly international shipping newspaper
- Lloyd's List, a leading daily newspaper for the maritime industry

8.2.3. The managers of NOE and MSMI have stated that the rationale for seeking dispensation from the requirements mentioned in 8.2.2 above are:

- MSMI and NOE policyholders are exclusively comprised of international shipping businesses whose activities transcend traditional national and regional territorial boundaries. A publication such as the Financial Times (International Edition), which is widely circulated and read amongst the international business community, will be a more effective means of targeting the notice at MSMI policyholders than national newspapers.
- MSMI and NOE policyholders belong to a common community of interest, namely shipping & marine insurance. Tradewinds and Lloyds List are both widely circulated and read within the shipping and marine insurance industries, and they will also be a more effective means of notifying the Part VII application to MSMI policyholders than national newspapers.

8.3. Notification of policyholders

8.3.1. Regulation 3 (2) (b) of the Transfer Regulations requires that a notice stating that the Part VII application has been made must be sent to every "policyholder" of MSMI and NOE. The definition of "policyholder", as set out in the Financial Services and Markets Act 2000 (Meaning of "Policy" and "policyholder") Order 2001, is extremely broad and the managers of NOE and MSMI believe that it is appropriate in the circumstances to seek a dispensation from the strict requirements of Regulation 3 (2) (b) of the Transfer Regulations.

8.3.2. The managers of NOE and MSMI normally communicate with members and policyholders in the following ways:

- Brokers - many members and policyholders employ the services of brokers and in such circumstances it is normal for communications to be conducted through the broker on behalf of the member or policyholder. The rules of NOE and MSMI expressly provide for communications in such circumstances and expressly permit notices to be served via the brokers.
- Managing Agents - it is common for the day to day activities of a ship, including the placement of insurance for the vessel, to be managed by a managing agent acting on behalf of the member or policyholder. The rules of NOE and MSMI expressly provide for communications in such circumstances and expressly permit notices to be served via the managing agents.
- Joint members - in some cases a ship will be entered for insurance in the name of multiple parties as joint members (or joint policyholders). In such circumstances it is usual for one of these joint members to be designated as the "senior member" in relation to that ship and with whom communications are conducted on behalf of all of the joint members. The rules of NOE and MSMI expressly provide for communications in such circumstances and expressly permit notices to be served upon all joint members via service upon one of their number.
- Fleet entries - in some cases the entry of more than one ship by one or more members is treated together as a fleet by NOE or MSMI for underwriting purposes. In such circumstances NOE and MSMI are permitted under their Rules to act as if all of the ships forming a fleet entry were entered by the same members. In practice therefore it is normal for a member to be designated as the central point of contact in relation to all matters concerning policies relating to the relevant fleet entry.
- Co-assured - in some cases NOE accepts entries from a member on the basis that another person or persons will become co-assured. In such circumstances the member who has made the entry is deemed irrevocably to have full power and authority to act in the name of and/or on behalf of the co-assured. Notices and communications in respect of such policies are therefore normally sent to the relevant member on behalf of all parties insured under the relevant policy.

8.3.3. It is proposed that notice of the Part VII Transfer application will be given in the manner contemplated in section 8.3.4 below to the following persons (“the Relevant Policyholders”) as shown on the operational computer records of NOE and MSMI:

- All members/policyholders and reinsurers of MSMI's open policy years. In addition all members/policyholders of MSMI's closed policy years 2007/08, 2008/09 and 2009/10.
- All members/policyholders of NOE's open policy years.
- All members/policyholders of NOE and MSMI's closed policy years with outstanding claims.
- All reinsurers of MSMI's closed policy years against whom MSMI has an outstanding claim.
- Any persons to whom NOE has provided reinsurance during NOE's open policy years.

8.3.4. The notice will be sent via the method of communication shown in section 8.3.5 below. The manner in which it is proposed that notice will be given to the Relevant Policyholders is as follows:

- Where it is usual practice for NOE/MSMI to communicate with the Relevant Policyholder through a broker, notice will be sent to the relevant broker.
- Where it is usual practice for NOE/MSMI to communicate with the Relevant Policyholder through an agent, notice will be sent to the relevant agent or the broker of that agent (where applicable).
- Where the Relevant Policyholder is a joint member in relation to any transferring policy, notice will be sent to the senior member with whom communications are ordinarily sent in relation to that policy or to the broker or agent of that senior member (where applicable).
- Where the Relevant Policyholder is a reinsurer of MSMI or NOE participating in a reinsurance programme in conjunction with one or more other reinsurers, notice will be sent to the lead reinsurer or to the broker of the lead reinsurer (where applicable).
- To the extent that none of the above are applicable, notice will be sent directly to the Relevant Policyholder.

8.3.5. The Rules of NOE and MSMI both contain provisions which permit notices to be served upon members by post or electronic communications. Notice will be sent via the following methods of communication:

- Where email is the usual method of communication with the Relevant Policyholder or (as applicable) their broker or agent, notice will be sent by email to the last known contact email address notified to MSMI/NOE by the Relevant Policyholder.
- If the above is not applicable, notice will be sent by courier or post to the last known contact address notified to MSMI/NOE by the Relevant Policyholder or (as applicable) their broker or agent.

8.3.6. The notice will comprise a letter accompanied with a copy of the Scheme Report and Scheme Document setting out the full terms and conditions of the Scheme. The letter will be headed “Transfer of the Insurance Business of Marine Shipping Mutual Company Limited to

North of England Protecting & Indemnity Association Limited” and giving the following information:

- Full names and addresses of NOE and MSMI.
- A brief statement of the background and rationale for the Scheme.
- A statement describing briefly the proposed transfer, the intended date of the Court hearing and the proposed Effective Date.
- The name of the Independent Expert; that he has been appointed as such with the approval of the Regulator.
- A statement that the Regulator has been consulted in relation to the proposed Scheme and will continue to consider it in the light of information it receives including issues raised by affected parties or any other representations or information it receives prior to the sanction hearing and, should it have any significant concerns, these will be drawn to the attention of the Court.
- A statement that certain documents can be viewed on a named website and that further copies of documents (including the Scheme Report and Scheme Document) can be requested free of charge by contacting a named person at a given mail address, email address or telephone number.
- A statement that the documents can also be viewed at normal office hours at a given address in Newcastle Upon Tyne.
- A statement to the effect that any person who considers that he would be adversely affected by the carrying out of the transfer has the right under FSMA to make written representations and/or to be heard by the Court (the Court address and application hearing date is given).
- A statement inviting a person with any objections to write or email to a named person at NOE giving reasons for any such objections (the address and email address are given).

8.3.7. I am satisfied that the proposed approach to communication with policyholders is both proportionate and reasonable.

Appendix A Engagement Letter

The following is an extract from our engagement letter. The abbreviations have been changed to be consistent with the abbreviations used in this Scheme Report.

19/09/2012

The Directors
North of England P&I Association Ltd and
Marine Shipping Mutual Insurance Company Ltd
c/o North Insurance Management Limited
The Quayside
Newcastle Upon Tyne
NE1 3DU

Dear Sirs

North of England P&I Association Limited (“NOE”), and Marine Shipping Mutual Insurance Company Limited (“MSMI”) - appointment of Keith Tucker, FIA, as Independent Expert for proposed Part VII Transfer of all business from MSMI to NOE.

1. We are writing to confirm our understanding of the services you wish us to provide for you. This engagement letter, together with the attached Terms and Conditions, sets out the terms upon which we offer to act in connection with the provision of professional services. Our role will be to provide the professional services detailed below. The duties and responsibilities of Moore Stephens LLP shall be limited to the matters expressly referred to herein.
2. This engagement is undertaken by Moore Stephens LLP, a body corporate with members and its own legal personality separate from the members. Our members will generally be referred to by the traditional term of “partner”, and therefore all references in this letter, and in all dealings between us, to “partners” are to members of Moore Stephens LLP. The members are not in partnership with each other or with Moore Stephens LLP, and they have limited liability.

Services

3. You have asked us to provide an Independent Expert to report on the proposed insurance business transfer scheme to transfer business from MSMI to NOE (“the Scheme”). The Independent Expert’s report will be prepared in accordance with and for the purpose set out in Part VII of the Financial Services and Markets Act 2000 (“FSMA”) and for no other purpose.
4. The Independent Expert analysis and formal report will follow the relevant FSMA requirements and associated supplemental guidance including FCA Handbook Section SUP 18 and PRA’s Insurance Business Transfers Statement of Policy. The Independent Expert will consider the scheme as a whole and its effects on the policyholders of MSMI and NOE. In particular it will include, but not be limited to, an opinion on:
 - the impact of the scheme on the security of the different groups of policyholders affected by the scheme, namely
 - transferring policyholders
 - policyholders of the transferee
 - any policyholders of the transferor whose contracts will not be transferred (although we understand that the scheme is designed to effect the transfer of all contracts from MSMI to NOE)
 - the adequacy of any safeguards in the scheme that are intended to protect the interests of the affected policyholders

- the fairness of any mechanisms implemented at the same time as the scheme, but not included in the scheme, intended to improve the security of any policyholders affected by the scheme
 - any other information required to be included in the FSMA and any guidance issued by the FSA
5. The above list is not intended to be exhaustive and other aspects of the transfer may come to light during the assignment which are considered to be material. Any changes to the scope of the assignment should be by mutual agreement and confirmed in writing.

Data reliance and limitations

6. The Independent Expert will rely upon data and information provided by you, other third party experts, such as auditors and actuaries, and industry sources of data. He will not audit or verify this data and information. If the underlying data or information is incomplete or inaccurate, the results of his analysis may likewise be incomplete or inaccurate. However, the Independent Expert will endeavour to verify the accuracy and completeness of the data and information and may carry out his own independent calculations and projections based on the data and information supplied.
7. The Independent Expert's ability to carry out this assignment will depend on a number of key factors, including:
- that the relevant and appropriate information is readily available, specifically
 - financial data including projections
 - actuarial and audit reports
 - detailed information on reinsurances
 - detailed information on any guarantees
 - access to any relevant modelling and sensitivity analysis tools
 - access to appropriate personnel of MSMI and NOE for the purpose of interview and discussion
 - access to the authors of any third party reports
 - agreement of third parties to his reliance on their reports for the purpose of forming his independent expert opinion.

Duty to the Court

8. The Independent Expert will carry out the duties and requirements regarding experts as set out in Part 35 of the Civil Procedure Rules. The Independent Expert's report will be addressed to the Court and will include, inter-alia, the following matters:
- an express statement that our expert understands his duty to the Court and he has complied and will continue to comply with that duty
 - a summary of the matters dealt with in the report together with the reasons for those opinions
 - a statement setting out the substance of all material facts and instructions that our expert has received (whether written or oral), which are material to the opinions expressed in his report or upon which his opinions are based
 - whether any questions or issues specifically fall outside his expertise, and how he has dealt with those questions or issues
 - any other matters required under FSMA and SUP 18 of the FCA Handbook and PRA's Insurance Business Transfers Statement of Policy

Our Team

9. Keith Tucker, the proposed Independent Expert, will be involved throughout all stages of this assignment, making his own independent projections, reviewing the proposed scheme, and

preparing a report of his findings for submission to the Court, as well as attending Court as required and appropriate.

10. The Moore Stephens Partner responsible for the oversight of this assignment will be Simon Gallagher, head of Moore Stephens Insurance Industry Group.

Fees

11. We understand you wish us to invoice The North of England Protection & Indemnity Association Limited for this amount.
12. Our fee estimate is based on the assumption that we do not encounter any unexpected issues and that we are provided at the commencement of our assignment with the information we request. Should any unexpected issues arise, including the identification of the existence of, or potential for, latent claims, we will notify you as early as possible, so that we can agree how they should be dealt with.

Limitation of liability

13. The Limit of Liability referred to in paragraph 17 of the Terms and Conditions shall be the lower of:
 - ten times the fees charged pursuant to this engagement letter for the period or periods during which the work giving rise to the claim was carried out (but excluding fees for any work in respect of which liability cannot lawfully be limited or excluded); or
 - £5 million.

Service

14. If at any time you would like to discuss with us how our service to you could be improved or if you are dissatisfied with the service you are receiving please let us know by contacting Simon Gallagher. If you are still not satisfied, you should contact our Senior Partner, Richard Moore. In the event of your not being satisfied by our response, you may also wish to bring the matter to the attention of the Institute of Chartered Accountants in England and Wales.
15. We undertake to look at any complaint carefully and promptly and to do all we can to explain the position to you.

Agreement of terms

16. We shall be grateful if you will kindly acknowledge receipt of this letter and the attached Terms and Conditions by signing the enclosed copy of this letter where indicated and returning it to us. If the contents are not in accordance with your understanding of our terms of appointment, please let us know.
17. Once it has been agreed, this letter and the Terms and Conditions will remain effective, from one appointment to another, until replaced, or revised by mutual agreement or we cease to act on your behalf.

Yours faithfully

Simon Gallagher

Appendix B Experience of Independent Expert

Keith Tucker FIA, ASA

Fellow of the Institute of Actuaries, 1980.
Associate of the Society of Actuaries, 1988.
Affiliate member of the Institute of Risk Management.

I am currently acting in a consultancy role to Moore Stephens specifically for this assignment. Until 8 February 2013, I was employed as a Director in the Insurance Industry Group department of Moore Stephens LLP, which undertakes a variety of assignments with its insurance industry clients that include insurance companies (including P&I clubs and marine mutuals), underwriting agencies, firms at Lloyd's, managing agencies, composites and companies that support the insurance industry such as claims handlers and loss adjusters. My recent work was primarily in the field of general insurance including calculation of capital, loss reserves and other balance sheet items, both on a Solvency I and Solvency II basis, and assisting clients with various aspects of their Solvency II implementation. The clients that I dealt with underwrite similar business to that of the two parties (NOE and MSMI) involved in this proposed Scheme.

I was previously Actuarial Manager in the UK subsidiary (Omnilife Insurance) of the Mediterranean & Gulf Reinsurance & Insurance Company Group ("Medgulf Group") for the period 2008 to 2011. I was the appointed Signing Actuary for Medgulf Group's largest insurance company in Saudi Arabia (with annual written premiums in the region of £500 million) as well as Bahrain. My position in the Medgulf Group was that of regional actuary to the Middle East (which also included Lebanon and Jordan) and to the UK. Medgulf Group underwrites a full range of insurance including Health (medical expenses), Motor, Property, Engineering, Marine Cargo, Marine Hull, Aviation, Liability, Accident and Life. My general insurance work included reserving, regulatory reporting and pricing investigations for all the above lines of business. I was also responsible for the UK actuarial work and Solvency II implementation. I was a non-executive director of Omnilife Insurance for several years before joining the Medgulf Group as a permanent full time employee in 2008.

For the period 2006 to 2008 I was the Finance Actuary in the Finance Department of Reinsurance Group of America UK ("RGA UK"). I was primarily responsible for the production of the required valuation output for UK Regulatory, Companies Act, ICA and Solvency II reporting, including the necessary actuarial analyses and preparation of draft reports for the board and regulators.

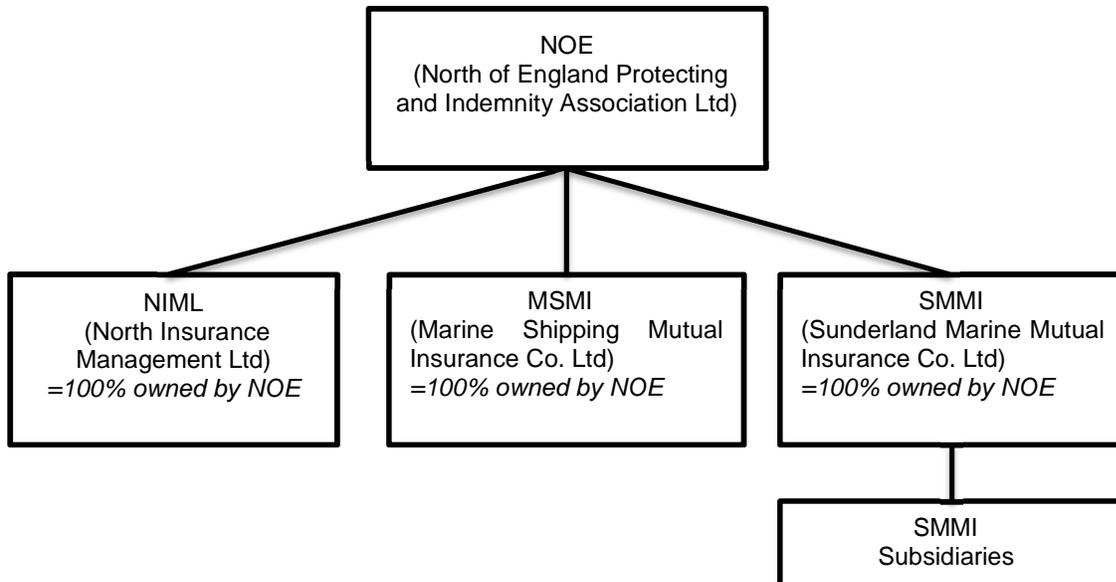
For the period 2004 to 2006 I was Actuary, Life Statutory Reporting at Co-operative Insurance Society. I managed a team primarily concerned with peak 2 (realistic valuation) periodic work and with bonus & related asset share work. Prior to this I was responsible for the team that developed the realistic balance sheet and ICA modelling work.

For the period 1990 to 2004 I was a consulting actuary, primarily as a Salaried Partner in Hymans Robertson's Insurance Division (now part of Milliman UK) but for the last three years as a self-employed consultant. During this period I dealt with a variety of work for UK and overseas insurance companies (life and general) and with some overseas pension funds. This included being a UK Appointed Actuary to a life insurer that transacted two inwards transfers of insurance business under Schedule 2C of the Insurance Companies Act 1982 (the regime in place prior to the current Part VII transfer regime). I also assisted in the work carried out by one of the partners in Hymans Robertson when he was appointed to act as the Independent Expert in other Schedule 2C transfers.

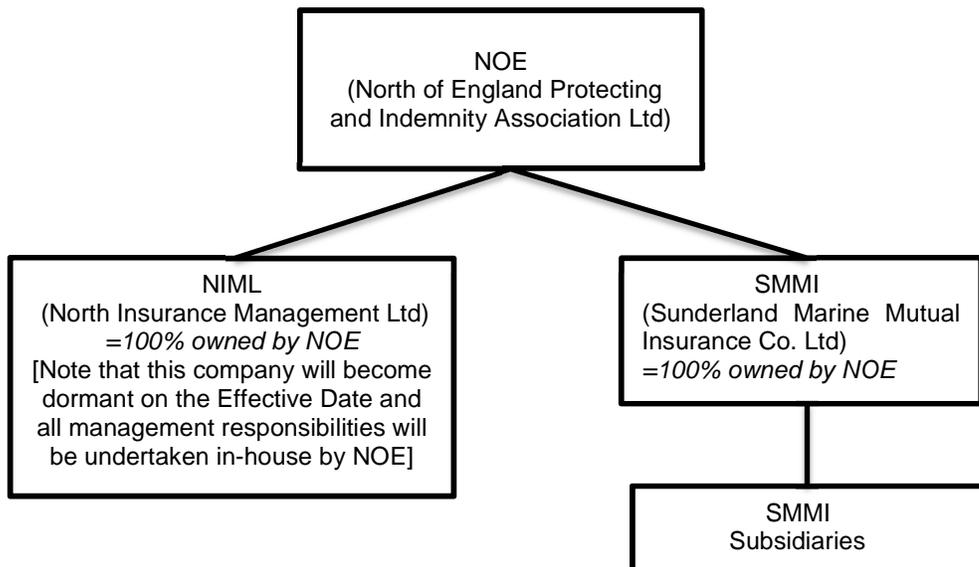
For the period 1989 to 1990 I was the Chief Actuary and Director of Aetna Life UK, responsible for the entire UK actuarial function and a board member. For the period 1987 to 1989 I was the UK Actuary in Alico, part of the AIG group and responsible for the entire UK actuarial function. For the period 1985 to 1987 I was the Deputy Actuary at Liberty Life Insurance Company. For the period 1981 to 1985 I was the Assistant Actuary at Barclays Life. I started my actuarial career in 1971 as a trainee actuary in Provident Life Association of London, which also had a related general insurance company. I worked in the valuation, actuarial and headed the pensions department before leaving to take up a managerial role in 1981 with Barclays Life.

Appendix C Company Structure Charts

Group Structure prior to the Effective Date



Group Structure on the Effective Date:



Appendix D Data

This appendix lists the items of information that I have received and reviewed, following requests to NOE, NIML and MSMI, in order to prepare this Scheme Report.

In addition, I have had access to draft copies of Court documents, including the Insurance Business Transfer Scheme document, prepared in connection with the Scheme and a copy of a memorandum from Norton Rose re: Part VII Transfer Requirements.

I have also relied on discussions and email correspondence with staff of NOE and NIML

List of data

Company Financial Data:

- NOE Combined Financial Statements for year ended 20 February 2014
- NOE Combined Financial Statements for year ended 20 February 2013
- NOE Combined Financial Statements for year ended 20 February 2012
- NOE Combined Financial Statements for year ended 20 February 2011
- NOE PRA Return for financial year ended 20 February 2014
- NOE PRA Return for financial year ended 20 February 2013
- NOE FSA Return for financial year ended 20 February 2012
- NOE FSA Return for financial year ended 20 February 2011
- NOE Management Reports for Quarters ending November 2012, August 2012, May 2012, November 2011, August 2011 and February 2011
- MSMI Directors Report & Financial Statements for period ending 20 February 2014
- MSMI Directors Report & Financial Statements for period ending 20 February 2013
- MSMI Directors Report & Financial Statements for period ending 20 February 2012
- MSMI Directors Report & Financial Statements for period ending 30 June 2011
- MSMI PRA Return for financial year ended 20 February 2014
- MSMI PRA Return for financial year ended 20 February 2013
- MSMI FSA Return for financial year ended 20 February 2012
- MSMI FSA Return for financial year ended 30 June 2011
- SMMI Annual Report and Financial Statements for the year ended 31 December 2013
- SMMI PRA Return for financial year ended 31 December 2013

General Corporate Information:

- Summary of NOE Reinsurance Programme 2012/2013

- Details of MSMI reinsurances
- NOE ARROW Risk Assessment and Individual Capital Assessment Review, dated 10 September 2010
- NOE current Group Structure Chart
- Board papers regarding NOE's ICA for 2013 and 2012
- Details of NOE's ECR calculations for 2013 and 2012
- NOE's ECR and ICA calculations for 2014
- SMMI's ECR, ICA and Solvency II calculations for 2013
- Board papers regarding NOE's Solvency II Gap Analysis and Implementation Plan
- MSMI ARROW Risk Assessment and Individual Capital Assessment Review, dated 10 September 2010
- Email correspondence with FSA re: NOE/MSMI Annual Returns
- Email correspondence with FSA re: MSMI capital requirements
- Waiver application form re: MSMI change of accounting reference date
- FSA notice of variation to MSMI permission
- Framework Agreement of 23 August 2011
- Framework Agreement of 19 December 2013 between NOE and SMMI
- Parent Company Guarantee of 28 February 2014 (NOE and SMMI)
- Reinsurance Agreement between MSMI and NOE dated 2 November 2011
- Management Agreement between NOE, NIML and MSMI of November 2003
- Summary of policyholder information for MSMI
- Copies of members' circulars regarding the merger of NOE and SMMI

Reserve investigation reports prepared by Moore Stephens LLP:

- MSMI Deterministic and Stochastic Review of Likely prospective Gross Claims Development as at 31 December 2011
- NOE Deterministic and Stochastic Review of Likely prospective Gross Claims Development as at 20 February 2012
- MSMI Stochastic Review of Net Ultimate Claims Costs as at 30 June 2011
- NOE Stochastic Review of Prospective Asbestos Losses as at 1 January 2012

Appendix E Definition of Terms and Glossary

FSMA means the Financial Services and Markets Act 2000 and its subsequent amendments.

Affected Policyholders means collectively:

- the policyholders transferring from MSMI to NOE;
- the policyholders, if any, remaining in MSMI; and
- the current policyholders of NOE.

ASA means Associate of the Society of Actuaries, being a professional body for actuaries in the United States of America.

Court means the High Court of Justice of England and Wales.

CRR means Capital Resources Requirement, the amount of capital that an insurance company must hold under the existing Solvency I regime, being the amount of admissible assets in excess of the regulatory liabilities. This is disclosed publicly in the annual returns to the Regulator of financial and other information. The CRR is an amount equal to or greater than the MCR (defined below).

ECR means the Enhanced Capital Requirement, a more risk sensitive calculation of capital for UK insurers as measured by the Regulator but not publicly disclosed.

Effective Date means the date on which the Scheme will be effected.

External Reinsurance Arrangements means the existing reinsurance agreements between MSMI (as the ceding company) and External Reinsurance Parties whereby some of the insurance risks of MSMI are reinsured. Following the Effective Date such reinsurance agreements will continue to cover the same insurance risks which will then reside in NOE as the ceding company.

External Reinsurance Parties means those parties other than NOE that have existing reinsurance agreements with MSMI whereby some of the insurance risks of MSMI have been ceded.

FCA means the Financial Conduct Authority (see **Regulator** below).

FD&D means Freight Demurrage & Defence, a type of insurance underwritten by NOE to cover legal costs and expenses in relation to a range of disputes.

FIA means Fellow of the Institute and Faculty of Actuaries, being the chartered professional body for actuaries in the United Kingdom.

Framework Agreement means the agreement dated 23 August 2011 between MSMI and NOE whereby members of MSMI will receive a distribution of a proportion of the reserves of MSMI and cease to be members of MSMI, and whereby NOE will become the sole member of MSMI and acquire all the assets and liabilities of MSMI.

FSA means the Financial Services Authority (see **Regulator** below).

ICA means Individual Capital Assessment, an insurance or reinsurance company's own assessment of the capital that it needs for regulatory purposes in the UK.

ICAS means Individual Capital Adequacy Standards, the regulatory framework currently in operation in the UK that was introduced in 2004 whereby insurance and reinsurance companies carry out capital modelling and risk management exercises in order to assess their own regulatory capital

requirements or ICA. After reviewing a company's ICA, the Regulator will set the company's ICG which may differ from the ICA. The ICA and ICG are not publicly disclosed.

ICG means Individual Capital Guidance, the final agreed figure used by the Regulator for the required solvency capital requirement for an insurance or reinsurance company in the UK. It is often expressed as a percentage of the ICA.

Independent Expert in the context of this Scheme Report means Keith Tucker FIA, ASA.

Insurance Business Transfers Statement of Policy means the April 2015 Statement of Policy issued by the PRA: "The Prudential Regulation Authority's approach to insurance business transfers".

Interim Management Agreement means the agreement between MSMI, NOE and NIML whereby MSMI is managed by NIML for the period following the termination of the Management Agreement.

Management Agreement means the agreement between MSMI, NOE and NIML dated 19 November 2003, whereby MSMI was managed by NIML. This agreement terminated on 30 June 2013 when the Interim Management Agreement took effect.

MCR means Minimum Capital Requirement, the minimum amount of capital that an insurance company must hold under the existing Solvency I regime, being the amount of admissible assets in excess of the regulatory liabilities. This is disclosed publicly in the annual returns to the Regulator of financial and other information. The MCR represents the very minimum amount of capital resources to satisfy the Regulator that an insurance company can continue trading and represents the threshold below which the Regulator would intervene.

members in the context of this Scheme Report means members of a mutual insurance company. The members can be both the insurers and the insured. Such companies exist for the purpose of satisfying the insurance needs of their members, whereby members contribute through a system of premiums or calls, forming a fund from which all losses and liabilities are paid. Any profits are essentially divided among the members of the company in amounts proportionate to their individual interests. Not all policyholders are necessarily members. Not all members are necessarily policyholders. The exact situation for any such mutual company is usually contained within the company's Articles of Association and within the company's rules.

MSMI means the Marine Shipping Mutual Insurance Company Limited.

NIML means North Insurance Management Limited, a wholly owned subsidiary company of NOE.

NOE means the North of England Protecting and Indemnity Association Limited.

P&I means Protecting and Indemnity, a type of insurance underwritten by NOE to cover liabilities, costs and expenses arising in respect of cargo, seamen and passengers as well as third party liabilities in respect of pollution, property damage, wreck removal, salvage and collision.

Policy years and open policy years. Both NOE and MSMI's insurance policies are written with reference to a fixed policy year, which commences on a fixed date each year. Policy years usually remain open until such time as the directors of the company are satisfied that the claims, expenses and outgoings arising in respect of that policy year have largely been satisfied and no further contributions are required from the members of that policy year; at which time the directors will ordinarily declare the relevant policy year closed and the members of that policy year will have no further liability to make further contributions in respect of that policy year. The liability of a member of NOE to make contributions in respect of a policy year will ordinarily continue for so long as that policy year remains "open" or a "Release Call" is paid in order to release the member from any further liability to make contributions. A similar situation applied to MSMI members prior to the Framework Agreement under which they relinquished their membership rights and obligations to make any further contributions. Thus, whilst MSMI does have some open policy years, NOE is now the only member of

MSMI and would be liable to make any further calls or contributions in respect of those open policy years.

PRA means the Prudential Regulation Authority (see **Regulator** below).

Regulator means the Financial Services Authority (the FSA) or its successor regulator(s) in the United Kingdom, including the Prudential Regulation Authority (the PRA) and the Financial Conduct Authority (the FCA). On 1 April 2013 the FSA reorganised and became two new regulators, the PRA and the FCA. NOE and MSMI were authorised by the FSA to carry out contracts of non-life insurance and reinsurance. With effect from 1 April 2013 insurance companies such as NOE and MSMI are authorised by the PRA and regulated by the PRA and the FCA.

Reinsurance Agreement means the existing reinsurance agreement between MSMI and NOE dated 2 November 2011 whereby all of the insurance risks of MSMI net of amounts recovered or recoverable under External Reinsurance Arrangements, are reinsured 100% with NOE.

Remaining (remaining) policyholders means those MSMI policyholders, if any, that have Residual Policies.

Residual Policies means any policies remaining in MSMI post-Effective Date, which will be reinsured to NOE under the Residual Policies Reinsurance Contract.

Residual Policies Reinsurance Contract means the reinsurance contract between MSMI and NOE to reinsure the Residual Policies of MSMI to NOE.

Scheme means the proposed scheme to transfer all of the insurance business of MSMI to NOE pursuant to Part VII of the FSMA.

Scheme Report means this report in its entirety.

SMI means the Sunderland Marine Insurance Company Limited - the current name of **SMMI** (see below) following the recent merger of NOE and SMMI. The change of name was registered at companies house on 31 July 2014.

SMMI means the Sunderland Marine Mutual Insurance Company Limited.

Solvency I means the existing regulatory regime relating to capital and other requirements for insurance firms that operate in the European Union.

Solvency II means the updated regulatory regime relating to capital and other requirements for insurance firms that operate in the European Union, including the UK. The implementation date for this new regime is 1 January 2016.

SUP 18 means Chapter 18 "Transfer of Business" of the FCA Supervision manual, part of the FCA Handbook.

War Risks means a type of insurance underwritten by NOE to cover losses caused by war and terrorism or as consequence of a ship being blocked or trapped in an area of conflict.

Appendix F Balance Sheets Pre- and Post-Transfer
[Based on 20 February 2014 published financial statements]

MSMI Balance Sheet (prior to Effective Date):

	US\$ (000's)	US\$ (000's)
ASSETS		
Financial Investments (fixed income securities)		14,632
Reinsurer's share of technical provisions		19,330
Debtors		
Arising out of direct insurance operations	68	
Arising out of reinsurance operations	2,129	
Total Debtors		2,197
Cash at bank and in hand		6,506
Prepayments and accrued Income		57
Total Assets		42,722
LIABILITIES		
Reserves		
Income and Expenditure account	(1,440)	
NOE Capital Reserve	7,250	
Total Reserves		5,810
Technical provisions (claims outstanding)		19,330
Creditors		
Amounts due to parent company	5,490	
Arising out of reinsurance operations	11,729	
Other creditors	274	
Total Creditors		17,493
Accruals and deferred Income		89
Total Liabilities		42,722

NOE Combined Balance Sheet (prior to and post Effective Date)

	US\$ (000's)	US\$ (000's)
ASSETS		
Intangible assets		8,252
Property, plant and equipment		14,445
Reinsurer's share of technical provisions		342,021
Financial assets		
Equity securities	61,557	
Debt securities	717,068	
Loans and receivables (including insurance and reinsurance receivables)	98,555	
Total financial assets		877,180
Corporation tax debtor		176
Cash and cash equivalents		119,283
Total Assets		1,361,357
LIABILITIES		
Accumulated Surplus		
Income and Expenditure account	(36,462)	
Contingency funds	348,736	
Total Accumulated Surplus		312,274
Technical provisions (unearned premiums and claims outstanding)		973,047
Derivative financial instruments		444
Reinsurance payables		13,232
Trade and other payables		36,057
Retirement benefit liability		26,303
Total Liabilities		1,361,357

Appendix G External Reinsurance Arrangements of MSMI with External Reinsurance Parties (other than NOE)

Unique Market Reference	Policy Year	Broker	Reinsurers	Domicile of Reinsurer	Law & Jurisdiction
B0576RQTH536	2010/2011	Willis	Alterra Re UK	Bermuda	England & Wales
B0576RQXH138	2010/2011	Willis	Lloyd's Underwriters	UK	England & Wales
N/A	2010/2011	N/A	General Reinsurance UK Ltd	UK	England & Wales
B0576RQXH538	2010/2011	Willis	Hannover Ruckversicherung AG Lloyd's Underwriters	Germany UK	England & Wales
B0576RQFH140	2010/2011	Willis	Lloyd's Underwriters	UK	England & Wales
B0576RQTH136	2010/2011	Willis	Lloyd's Underwriters Flagstone Reassurance Suisse SA Alterra Re UK Hannover Ruckversicherung AG Partner Reinsurance Europe Ltd Transatlantic Reinsurance Company Scor Switzerland Ltd	UK Switzerland Bermuda Germany Ireland USA Switzerland	England & Wales
B0576RQFH551	2010/2011	Willis	Lloyd's Underwriters HCC International Insurance Company Ltd	UK UK	England & Wales
B0576RQTH128	2010/2011	Willis	Lloyd's Underwriters Flagstone Reassurance Suisse SA Hannover Ruckversicherung AG Partner Reinsurance Europe Ltd Transatlantic Reinsurance Company	UK Switzerland Germany Ireland USA	England & Wales
B0576RQTH537	2010/2011	Willis	Scor Switzerland Ltd	Switzerland	England & Wales
B0576RQFH545	2010/2011	Willis	Lloyd's Underwriters	UK	England & Wales
B0576RQFH550	2010/2011	Willis	Lloyd's Underwriters	UK	England & Wales
B0576RPFH369	2009/2010	Willis	Lloyd's Underwriters	UK	England & Wales
B0576RPTH128	2009/2010	Willis	Lloyd's Underwriters Hannover Ruckversicherung AG Flagstone Reassurance Suisse SA Munchener Ruckversicherung-Gesellschaft AG Swiss Re Europe SA Transatlantic Reinsurance Company Harbor Point Re UK Scor Switzerland Ltd	UK Germany Switzerland Germany Luxembourg USA UK Switzerland	England & Wales
B0576RPTH129	2009/2010	Willis	Lloyd's Underwriters Hannover Ruckversicherung AG Flagstone Reassurance Suisse SA Munchener Ruckversicherung-Gesellschaft AG Swiss Re Europe SA Transatlantic Reinsurance Company Scor Switzerland Ltd	UK Germany Switzerland Germany Luxembourg USA Switzerland	England & Wales
B0576RPTH136	2009/2010	Willis	Lloyd's Underwriters Hannover Ruckversicherung AG Flagstone Reassurance Suisse SA Munchener Ruckversicherung-Gesellschaft AG Swiss Re Europe SA Transatlantic Reinsurance Company Harbor Point Re UK Scor Switzerland Ltd	UK Germany Switzerland Germany Luxembourg USA UK Switzerland	England & Wales
MSMIWAR0901A	2009/2010	Miller	Lloyd's Underwriters	UK	England & Wales
B0576RPXH361	2009/2010	Willis	Munchener Ruckversicherung-Gesellschaft AG	Germany	England & Wales
B0576RPXH360	2009/2010	Willis	Munchener Ruckversicherung-Gesellschaft AG	Germany	England & Wales
B0621M01A	2009/2010	Miller	Lloyd's Underwriters	UK	England & Wales
N/A	2009/2010	N/A	General Reinsurance UK Ltd	UK	England & Wales

B0576RPFH140	2009/2010	Willis	Lloyd's Underwriters	UK	England & Wales
B0576RPXH138	2009/2010	Willis	Lloyd's Underwriters	UK	England & Wales
B0518M073343	2008/2009	Arthur J Gallagher	Lloyd's Underwriters	UK	England & Wales
B0518M083373	2008/2009	Arthur J Gallagher	Lloyd's Underwriters	UK	England & Wales
B0518M083599	2008/2009	Arthur J Gallagher	Lloyd's Underwriters	UK	England & Wales
B0518M081505	2008/2009	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland	England & Wales
MSMIWAR0801A	2008/2009	Miller	Lloyd's Underwriters	UK	England & Wales
B0518M081500	2008/2009	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland	England & Wales
B0518M081464	2008/2009	Arthur J Gallagher	Munchener Ruckversicherung-Gesellschaft	Germany	England & Wales
B0518M081463	2008/2009	Arthur J Gallagher	Munchener Ruckversicherung-Gesellschaft	Germany	England & Wales
B0518M081462	2008/2009	Arthur J Gallagher	Munchener Ruckversicherung-Gesellschaft	Germany	England & Wales
B0518M081465	2008/2009	Arthur J Gallagher	Munchener Ruckversicherung-Gesellschaft	Germany	England & Wales
B0518M081480	2008/2009	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland	England & Wales
B0518M071480	2007/2008	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft New Reinsurance Company Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland Switzerland	England & Wales
B0518M071500	2007/2008	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft New Reinsurance Company Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland Switzerland	England & Wales
B0518M071505	2007/2008	Arthur J Gallagher	Lloyd's Underwriters Munchener Ruckversicherung-Gesellschaft Swiss Reinsurance Company (UK) Limited Transatlantic Reinsurance Company Hanover Ruckversicherung-Aktiengesellschaft New Reinsurance Company Flagstone Reassurance Suisse	UK Germany UK USA Germany Switzerland Switzerland	England & Wales
B0518M073236	2007/2008	Arthur J Gallagher	Lloyd's Syndicate 4020 ARK	UK	England & Wales
MSMIWAR0701A	2007/2008	Miller	Lloyd's Underwriters	UK	England & Wales