

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



MUNICIPAL MUTUAL

9th December, 1993

To:

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

Dear Sirs,

Modification to the maximum amount of Commission payable under the proposed Scheme of Arrangement (the "Scheme")

You will have received a letter from the Chairman of MMI dated 15th November, 1993 enclosing a Scheme document, Voting and Proxy Form and Schedule of Outstanding Scheme Liabilities. Terms defined in the Scheme are given the same meaning in this letter unless the context otherwise requires.

The purpose of this letter is:—

- (a) to tell you about an improvement in MMI's financial position;
- (b) to propose, as a consequential modification to the Scheme, a reduction in the Commission from £70 million to £30 million; and
- (c) to ask you to return a new pink Voting and Proxy Form relating to the modification.

Background—an improvement in MMI's financial position

The Explanatory Statement set out in the Scheme document contained an unaudited *pro forma* statement of net assets of MMI as at 31st December, 1992. The *pro forma* statement of net assets showed a surplus, after run-off adjustments, of £907,000. Since publication of the Scheme document on 15th November, 1993 the run-off has proceeded broadly in accordance with the assumptions made for the purpose of preparing the *pro forma* statement of net assets with one notable favourable exception.

As mentioned on page 27 of the Scheme document, MMI has been engaged in discussions with its Inspector of Taxes concerning the extent to which it is appropriate for MMI to be treated as having non-mutual status for taxation purposes. Since the Scheme document was posted, a further meeting has taken place and agreement in

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principle has been reached with the Inspector of Taxes as to the basis for submission of MMI's tax computations for 1989 to 1992. This basis is estimated to increase the *pro forma* net assets of MMI as at 31st December, 1992 by some £43.7 million. At the Board Meeting on 1st December, 1993 the Managing Trustees of MMI resolved to accept the proposed basis for submission of tax computations and the tax computations for 1989 to 1992 will now be submitted to the Inspector of Taxes on the basis agreed.

Whilst this improvement in MMI's net asset position is very welcome, it is not, in the Managing Trustees' view, of sufficient magnitude to ensure that a solvent run-off will be achieved in all conceivable future circumstances. The present anticipated *pro forma* net assets as at 31st December, 1992 of £44.6 million still only represent 4.8 per cent. of the total liabilities to be run-off of £925.3 million as at that date. The solvency of MMI could still be affected adversely by increases in liabilities and adjustments in estimated future claims payments, future fluctuations in the value of property and other investment assets and decreases in investment yields.

Accordingly, the Managing Trustees continue to believe that it is in the best interests of Scheme Creditors for a scheme of arrangement to be implemented in order to ensure the orderly run-off of MMI's liabilities.

Proposed modification of the Scheme

The Scheme provides for a Commission to be payable to Scheme Creditors and to the Policyholders Protection Board (the "PPB"). The Commission is proposed as compensation for Scheme Creditors and the PPB assuming the risk under the Scheme of having to make payments to MMI or having insurance claims payments reduced.

In the light of the improvement in MMI's financial position, the Managing Trustees consider that the maximum amount of Commission payable under the Scheme should be decreased to reflect the reduction in the risk of Scheme Creditors and the PPB having to make payments to MMI under the Scheme or of Scheme Creditors having their insurance claims payments reduced. Taking into account the improvement in MMI's financial position described above, the modification to the Scheme proposed below is estimated to leave Scheme Creditors in substantially the same position as they would have been if MMI had not received a favourable decision on its status for tax purposes and if the level of Commission had remained at the level currently provided for in the Scheme.

The Managing Trustees state in the Scheme document that they will not proceed with the Scheme unless the necessary amendments to MMI's Articles of Association have been approved by the members of MMI. A copy of the circular (omitting the Form of Proxy) to MMI's members relating to the Scheme and the changes proposed to be made to MMI's Memorandum and Articles of Association is enclosed for your information. The Managing Trustees have concluded that, unless the maximum amount of Commission payable under the Scheme were adjusted to reflect the new circumstances, they would not consider the adoption of new Articles of Association, allowing the Scheme to proceed, to be in the best interests of the members of MMI. The Managing Trustees would not, therefore, recommend to the members that they should vote in favour of the amendment of MMI's Articles of Association and in these circumstances they would not proceed with the Scheme unless it is modified as proposed.

Consequently, the Managing Trustees are proposing to amend the Scheme by reducing the figure for the Commission by £40 million to £30 million. The level of reduction in the maximum amount of Commission payable under the Scheme is proposed so as to reflect the increase in the *pro forma* net assets of MMI resulting from the agreement reached with the Inland Revenue.

If the modification is approved, the definition of "Commission" in the Scheme will read as follows:—

"£30 million, being the commission provision for payment of which is made in Clause 5.7;"

The Summary and Explanatory Statement should be read subject to the amendment proposed in this letter.

Voting and Proxy Forms

In order to implement the proposed modification, a new pink Voting and Proxy Form is enclosed. The new Voting and Proxy Form allows you to give specific directions to any proxy appointed by you on how to vote on the modified Scheme.

If you have not returned the Voting and Proxy Form sent under cover of the letter of 15th November, 1993 then it must be discarded and replaced by the new Voting and Proxy Form. If you have already returned a Voting and Proxy Form then you should nonetheless complete and return the new Voting and Proxy Form, which will supersede the earlier Voting and Proxy Form.

I will be writing to those Scheme Creditors which have already returned a Voting and Proxy Form appointing me as their proxy and those which do so using the original Voting and Proxy Form after today, informing them that, if they do not send in a new Voting and Proxy Form as requested and in the absence of any other express written directions being given to the contrary, I will take it that it is their intention to vote in favour or, as the case may be, against the modified Scheme as indicated in their original Voting and Proxy Form in relation to the Scheme in its original form.

Recommendation

The Managing Trustees believe that the Scheme modified as it is proposed in this letter is in the best interests of Scheme Creditors and, accordingly, recommend that creditors which are entitled to do so vote in favour of the proposed modified Scheme using the enclosed pink Voting and Proxy Form.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'John Lovill', written in a cursive style.

Sir John Lovill
Chairman
for and on behalf of
Municipal Mutual Insurance Limited