

Company Registration No. 00157661  
Registered in England & Wales

**CAVELL INSURANCE COMPANY  
LIMITED**

**Annual Report and Financial Statements**

**for the year ended 31 December 2012**

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**OFFICERS AND PROFESSIONAL ADVISORS**

**DIRECTORS**

I P Millar	
G H J Nokes	(Resigned 3 May 2012)
C P Thomas	(Non-Executive)
A J Turner	(Non-Executive)
T J R Wilkes	(Appointed 14 September 2012)

**SECRETARY**

S M Hextall

**REGISTERED OFFICE**

Avaya House  
2 Cathedral Hill  
Guildford  
Surrey  
GU2 7YL

**BANKERS AND INVESTMENT CUSTODIANS**

Citibank  
Barclays Bank plc  
Bank of New York

**CONSULTING ACTUARIES**

Ernst & Young LLP, USA

**AUDITOR**

KPMG Audit plc  
Chartered Accountants and Statutory Auditor  
London, United Kingdom

## DIRECTORS' REPORT

The directors present their annual report and the audited financial statements of Cavell Insurance Company Limited ("the Company") for the year ended 31 December 2012

### PRINCIPAL ACTIVITY

The principal activity of the Company is the conduct of general insurance and reinsurance business. The Company voluntarily ceased to underwrite new business in 1995.

The insurance business of the Canada branch was transferred to Omega General Insurance Company, a Canadian company which offers finality solutions for Canadian insurance business on 30 November 2011, and the branch will be formally wound up during 2013.

### REVIEW OF THE BUSINESS AND FUTURE DEVELOPMENTS

The Company is owned by Enstar Group Limited, a company domiciled in Bermuda. The Company is in run-off and has outsourced the management of its business to Enstar (EU) Limited ("Enstar"), a fellow subsidiary company. The Company does not directly employ its own staff.

The Company's run-off is conducted in a disciplined and professional manner in order to efficiently discharge liabilities associated with the business while preserving and maximizing assets. This may include, where appropriate, negotiating with insureds and reinsureds to buyback and/or commute their insurance or reinsurance agreements. In most cases, policy buybacks and commutations involve the settlement of all claims each party has against the other and are therefore a mechanism to extinguish liabilities for inwards insurance and reinsurance in addition to collecting outwards reinsurance recoveries, thereby eliminating uncertainty over the amount of future claims and reinsurance recoveries.

The Company understands the need to dispose of certain risks expeditiously and cost-effectively by constantly analysing changes in the market and efficiently settling claims with the assistance of Enstar's experienced claims adjusters, together with in-house and external legal counsel. The Company determines which claims are valid through the use of such experts.

The results for the year are shown in the profit and loss account on page 9. The profit for the year after taxation amounted to £2,447,519 (2011 - £1,099,450). This resulted principally from technical profits and investment income offset by foreign exchange losses. The run-off has proceeded satisfactorily during the year and the Company continues to conduct an orderly run-off of its business. All business has been classified as discontinued operations.

#### *Claims Management and Administration*

Enstar has implemented claims handling guidelines, claims reporting and control procedures. To ensure that claims are handled and reported in accordance with these guidelines, all claims matters are reviewed regularly, with all material claims matters being circulated to and reviewed by management prior to any action being taken.

#### *Manage Capital Prudently*

The Company manages its capital prudently relative to its risk exposure and liquidity requirements in order to maximise profitability and long-term growth in shareholder value. The Company's capital management strategy is to deploy capital efficiently to establish (and re-establish, when necessary) adequate loss reserves to protect against future adverse developments.

## DIRECTORS' REPORT

### *Performance Management*

The Companies Act encourages companies to provide both financial information and also to comment on key performance indicators (KPIs). The Company operates within a performance management framework that encompasses business planning and ongoing monitoring, as appropriate to a company in run-off.

KPIs are used primarily to compare actual performance to the business plan. For the year ended 31 December 2012 KPI's include

#### *Financial KPI's*

Percentage reduction in gross reserves during the year was 12% (2011: 8%)

Investment income return for the year was 3.8% (2011: 2.7%)

Operating profit before tax for the year was £2,760,052 (2011: profit £1,014,171)

#### *Non Financial KPI's*

Risk identification and control assessment process now operating quarterly on a Risk Management System

Formal Risk Management reporting (including risk appetite monitoring) to Board as business as usual

Own Risk & Solvency Assessment (ORSA – a Solvency II requirement) under discussion

### *Future Developments*

Solvency II will set out new, strengthened EU-wide requirements on capital adequacy and risk management for insurers with the aim of increasing policyholder protection, instilling greater risk awareness and improving the international competitiveness of EU insurers. The Company will continue to work on its Solvency II project plan and expects to be fully compliant with the requirements under Solvency II prior to its implementation.

The Company continues to monitor the appropriateness of various strategies to achieve complete finality and conclude its run-off. Possible exit strategies include a solvent scheme of arrangement whereby a UK court-sanctioned scheme, approved by a statutory majority of voting creditors, provides for a one-time full and final settlement of an insurance or reinsurance company's obligations to its policyholders. An alternative exit strategy could involve a portfolio transfer of the Company's remaining regulated business to another company within the Enstar Group through the mechanism set out in Part VII of the Financial Services and Markets Act 2000.

## IDENTIFICATION AND MANAGEMENT OF PRINCIPAL RISKS AND UNCERTAINTIES

### *Strategic Risk*

If the Company is unable to implement business plans and strategies, the business and financial condition may be adversely affected. The experience of the management team supported by a robust risk management framework will continue to allow the Company to manage the run-off of the business efficiently, while mitigating the impact and likelihood of the associated risks.

### *Reserving Risk*

The Company is managed to ensure it holds adequate loss reserves to protect it against future claims development.

To help manage this risk, the Company engages independent, external actuaries who use statistical methods including industry benchmarking methodologies to estimate appropriate Incurred But Not Reported ("IBNR") reserves for the Company's various exposures. These methods are based on comparisons of the Company's loss experience on its various exposures relative to industry loss experience for comparable exposures.

### *Claims Management and Commutation Risk*

As noted above, Enstar has implemented effective claims handling guidelines along with claims reporting and control procedures. To ensure that claims are appropriately handled and reported in accordance with these guidelines, all claims matters are reviewed regularly, with all material claims matters being circulated to and authorised by management prior to any action being taken.

When appropriate, the Company negotiates with direct insureds to commute or buyback policies either on favourable terms or to mitigate against existing and/or potential future indemnity exposures and legal costs in an uncertain and constantly evolving legal environment.

The Company also pursues commutations on favourable terms with ceding companies of reinsurance business.

## **DIRECTORS' REPORT**

A disciplined approach is followed throughout the commutation and policy buyback process to minimise risk and increase the probability of a positive outcome

### *Liquidity Risk*

The Company follows a conservative investment strategy designed to emphasize the preservation of its invested assets and provide sufficient liquidity for the prompt payment of claims as they fall due and settlement of commutation and policy buyback payments

### *Credit Risk*

The Company has purchased reinsurance to manage its existing liabilities. There is therefore credit risk that a counterparty will be unable to pay amounts in full when due. The Company places limits on its exposure to a single counterparty, or groups of counterparties, and to geographical and industry segments. Where necessary the Company will establish provisions against any bad or doubtful debts.

### *Foreign Currency Risk*

The Company currently does not use foreign currency hedges to manage its foreign currency exchange risk. The Company manages its exposure to foreign currency exchange risk by broadly matching its non-U S dollar denominated assets against its non-U S dollar denominated liabilities. This matching process is done quarterly in arrears and therefore any mismatches occurring in the period may give rise to foreign exchange losses, which could adversely affect the Company's operating results. The assets backing shareholders' funds are largely kept in U S Dollars, the Enstar Group's main currency.

### *Outsourcing Risk*

Those business activities / services that are outsourced via Service Level Agreements (including to Enstar) are reviewed on a regular basis to ensure that they are appropriate for the requirements of the business. Although these activities are outsourced, the Board remains fully accountable for the risks inherent in the business in accordance with the Outsourcing Policy. Regular review of outsource providers is a control that is attested to quarterly.

## **GOING CONCERN**

The Directors regularly review the Solvency calculations, available capital resources and run-off plans of the Company. Senior Management work alongside the local regulatory authorities to ensure sufficient capital remains within the Company as required under current regulations. Any capital extractions require the prior approval of the Financial Services Authority to ensure the Company continues to retain adequate resources in order to conduct an orderly, solvent run off. Having reviewed the run off plans and solvency calculations for the Company, safe in the knowledge the Company has ceased underwriting, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Further details regarding the adoption of the going concern basis can be found in the Statement of Accounting Policies in the financial statements.

## **DIVIDENDS**

The directors do not recommend the payment of a dividend for the year under review (2011 - £8,500,000)

## **DIRECTORS**

The present membership of the Board of Directors and changes in the composition of the Board up to and including the date of approval of these financial statements are as shown on page 1.

## **CHARITABLE DONATIONS**

No charitable donations were made in the year (2011 - £nil)

**DIRECTORS' REPORT**

**DISCLOSURE TO THE AUDITOR**

The directors who were in office on the date of approval of these financial statements have confirmed, as far as they are aware, that there is no relevant audit information of which the auditor is unaware. Each of the directors have confirmed that they have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that it has been communicated to the auditor.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

During the year, Deloitte LLP resigned as auditors to the Company. On 21<sup>st</sup> June 2012 the Directors resolved to appoint KPMG Audit plc ('KPMG') to fill the vacancy arising, and KPMG were duly appointed.

KPMG have indicated their willingness to be appointed for another term and appropriate arrangements have been put in place for them to be reappointed as auditor in the absence of an Annual General Meeting.

Approved by the Board of Directors and signed on behalf of the Board



I P Millar  
Director  
26<sup>th</sup> February 2013

**STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS**

The directors are responsible for preparing the Directors Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice)

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.



## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAVELL INSURANCE COMPANY LIMITED**

We have audited the financial statements of Cavell Insurance Company Limited for the year ended 31 December 2012 set out on pages 9 to 19. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective responsibilities of directors and auditor**

As explained more fully in the Directors' Responsibilities Statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate).

### **Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its profit for the year then ended,
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### **Opinion on other matter prescribed by the Companies Act 2006**


In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAVELL INSURANCE COMPANY LIMITED (continued)**

### **Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit



**Jonathan Bell (Senior Statutory Auditor)**  
**for and on behalf of KPMG Audit plc, Statutory Auditor**

***Chartered Accountants***

KPMG Audit plc

15 Canada Square

London

E14 5GL

28<sup>th</sup> February 2013

# CAVELL INSURANCE COMPANY LIMITED

## PROFIT AND LOSS ACCOUNT for the year ended 31 December 2012

TECHNICAL ACCOUNT – GENERAL BUSINESS	Notes	2012 £'000	2011 £'000
<b>EARNED PREMIUMS, NET OF REINSURANCE</b>			
Gross premiums written		(15)	31
Outward reinsurance premiums		-	-
Earned premiums, net of reinsurance		<u>(15)</u>	<u>31</u>
<b>CLAIMS INCURRED, NET OF REINSURANCE</b>	4		
Gross claims paid		(1,761)	(3,395)
Reinsurers' share		(302)	105
Net claims paid		<u>(2,063)</u>	<u>(3,290)</u>
Change in the provision for claims - gross		4,856	4,353
Reinsurers' share		(10)	39
Net change in the provision for claims		<u>4,846</u>	<u>4,392</u>
Claims incurred, net of reinsurance		2,783	1,102
Net operating expenses	5	(1,855)	(1,956)
Total technical income/(charges)		<u>928</u>	<u>(854)</u>
<b>BALANCE ON THE TECHNICAL ACCOUNT</b>		<u>913</u>	<u>(823)</u>
<b>NON - TECHNICAL ACCOUNT</b>			
Balance on the general business technical account		913	(823)
Investment income	7	2,769	3,255
Investment expenses and charges	8	(58)	(65)
Unrealised gains/(losses) on investments		1,188	(981)
Other charges	9	(2,052)	(371)
<b>OPERATING PROFIT ON ORDINARY ACTIVITIES BEFORE TAX</b>		2,760	1,015
Tax on profit on ordinary activities	10	(313)	85
<b>PROFIT FOR THE FINANCIAL YEAR</b>		<u>2,447</u>	<u>1,100</u>

There are no recognised gains or losses in either the current or previous financial years other than the profit of £2,447,519 (2011 - £1,099,450) shown above. Accordingly, no statement of total recognised gains and losses is required.

Notes on pages 11 to 19 form an integral part of these accounts.

All business is discontinued as defined by Financial Reporting Standard 3.

# CAVELL INSURANCE COMPANY LIMITED

## BALANCE SHEET As at 31 December 2012

	Notes	2012 £'000	2011 £'000
<b>ASSETS</b>			
<b>Investments</b>			
Land and buildings	11	1,669	1,948
Deposits with ceding undertakings		6,343	6,027
Other financial investments	11	60,969	61,681
		<u>68,981</u>	<u>69,656</u>
<b>Reinsurers' share of technical provisions</b>			
Claims outstanding		194	204
<b>Debtors</b>			
Arising out of reinsurance operations		39	272
Other debtors including taxation	12	22,106	24,366
<b>Other assets</b>			
Cash at bank and in hand		11,885	10,586
Prepayments and accrued income		5	9
Accrued interest and rent		1,369	569
		<u>13,259</u>	<u>11,164</u>
<b>TOTAL ASSETS</b>		<u>104,579</u>	<u>105,662</u>
<b>LIABILITIES</b>			
<b>CAPITAL AND RESERVES</b>			
Called up equity share capital	14	20,000	20,000
Share premium account	15	-	-
Profit and loss account	15	29,206	26,759
		<u>49,206</u>	<u>46,759</u>
Equity shareholders' funds			
<b>Technical provisions</b>			
Claims outstanding – gross amount		48,221	54,802
<b>Deposits received from reinsurers</b>		-	51
<b>Creditors</b>			
Arising out of reinsurance operations		3,950	3,802
Other creditors		3,093	-
		<u>7,043</u>	<u>3,802</u>
<b>Accruals and deferred income</b>		109	248
<b>TOTAL LIABILITIES</b>		<u>104,579</u>	<u>105,662</u>

Notes on pages 11 to 19 form an integral part of these accounts

These financial statements were approved by the Board of Directors on 26<sup>th</sup> February 2013

Signed on behalf of the Board of Directors



I P Millar  
Director  
Company Registration No 00157661

**NOTES TO THE ACCOUNTS  
for the year ended 31 December 2012**

**1. ACCOUNTING POLICIES**

**Basis of preparation**

The financial statements have been prepared in accordance with the provisions of Section 396 of the Companies Act 2006 and Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008

In accordance with FRS 1 (Revised 1996), Cash Flow Statements, the Company is not required to prepare a cash flow statement because more than 90% of the voting rights of the Company are held within the group and the group's consolidated financial statements are publicly available

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards and under the historical cost accounting rules as modified by the revaluation of investments, including land and buildings. The company has adopted all material recommendations of the Statement of Recommended Practice on Accounting for Insurance Business issued in December 2005 (as amended in December 2006) by the Association of British Insurers ("the ABI SORP")

The principal risks and uncertainties of the business have been addressed within the director's report on pages 2 to 5

All business is classified as discontinued as defined by Financial Reporting Standard 3

The particular accounting policies are described below. They have been applied consistently throughout the current and preceding years

**Going Concern**

Having reviewed the capital resources and cash available to the Company along with forecast results for future periods, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements

**Underwriting**

Full provision is made for outstanding losses, irrecoverable reinsurances and the costs of settling claims, on the basis of information currently available and anticipating trends of future settlements

**Claims incurred**

Claims incurred comprise the estimated cost of all claims occurring during the year, whether reported or not, including related direct and indirect claims handling costs and adjustments to claims outstanding from previous years

Outwards reinsurance recoveries are accounted for in the same accounting period as the claims for the related direct or inwards reinsurance business being reinsured

**Claims outstanding**

The provision for claims outstanding is made on an individual case basis and is based on the estimated ultimate cost of all claims notified but not settled by the balance sheet date, together with the provision for related claims handling. The provision also includes the estimated costs of claims incurred but not reported at the balance sheet date, based on statistical methods

The provision for claims outstanding is based on information available at the balance sheet date. Significant delays may be experienced in the notification and settlement of certain claims and accordingly the ultimate cost of such claims cannot be known with certainty at the balance sheet date. Subsequent information and events may result in the ultimate liability being less than, or greater than, the amount provided. Any differences between provisions and subsequent settlements are dealt with in the general business technical account in the year in which they arise

**Premiums**

Written premiums comprise adjustments arising in the financial year to premiums receivable in respect of business written in previous years

**NOTES TO THE ACCOUNTS  
for the year ended 31 December 2012**

**1. ACCOUNTING POLICIES (CONTINUED)**

**Investments**

Investments are held on the balance sheet at market value. Cavell's investments include an investment in a Limited Partnership which is accounted for on an equity basis based on the most recently available financial information.

The carrying value of leasehold buildings is based on their latest formal valuation, having been adjusted for capitalised development expenditure and depreciation based on the expected remaining future life. Other financial investments are held on the balance sheet at market value. Unrealised gains and losses are taken to the profit and loss account.

**Investment income**

Investment earnings include dividends and interest income receivable in the year, interest on an accruals basis and realised profits and losses on sale of investments. Realised gains are calculated as the difference between net sales proceeds and costs. In accordance with the ABI SORP (revised) on accounting for insurance business, unrealised profits and losses on investments are also included in investment earnings. Unrealised investment gains and losses are calculated as the difference between the valuation at the balance sheet date and their valuation at the last balance sheet date, or purchase price if acquired during the year. Unrealised investment gains and losses include adjustments in respect of gains and losses recorded in prior years which have been realised during the year and are reported as realised gains and losses in the current profit and loss account.

**Expenditure**

All expenses are charged to the technical account in the year in which they are incurred except investment management expenses, which are charged to the non-technical account, in the year in which they are incurred.

**Foreign Currency**

Transactions in foreign currencies during the year are translated into sterling at average rates of exchange for the period. Monetary assets and liabilities are translated into sterling at the rates ruling at the balance sheet date. All differences arising from the translation of assets and liabilities are dealt with in the non-technical account.

**Taxation**

The charge for taxation is based on the profit for the year at rates which have been enacted or substantively enacted by the balance sheet date, taking into account deferred taxation.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or a right to receive more tax, with the following exception. Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable tax profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax is calculated based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

**Run-off costs**

Run-off costs are the future costs of managing the Company, including claims handling costs. Provision is made for run-off costs to the extent that they are expected to exceed future investment income.

**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**1. ACCOUNTING POLICIES (CONTINUED)**

**Estimation Techniques**

The provision for outstanding claims comprises an estimate of the cost of settling all notified outstanding claims including claims handling costs, and an estimate of the cost of settling IBNR claims including claims handling costs

The notified outstanding claims are based on advices from policyholders, intermediaries and assessors. IBNR claims are estimated using a variety of statistical techniques including

- The development of previously settled claims (Chain Ladder Method)
- The development of previously notified claims (Chain Ladder Method)
- Expected loss ratios
- A combination of the above (Bornhuetter-Ferguson Method)

In addition reference is made to external reviews and industry data. The methods are predominantly deterministic, however, where possible, stochastic methods are used to produce a range of possible outcomes. The reinsurers' share of the provision for outstanding claims is then estimated based on the gross provisions having due regard to collectability, and contract terms and conditions.

The estimation of the provisions for the ultimate cost of asbestos, environmental pollution and other latent health hazards is subject to a larger range of uncertainties than those in other classes of business. This is largely due in part to the long delay between the exposure to the harmful conditions and the notification of a claim to the insurer. As a consequence traditional claims estimation techniques cannot wholly be relied on, and estimates are made using the specialised knowledge of both internal and external experts and professional advisors.

The establishment of outstanding claims provisions is subject to a great degree of variability in that, notwithstanding every effort to make appropriate provision, the eventual cost of settling outstanding claims may vary significantly from the initial estimate.

**2. UNCERTAINTIES REGARDING THE ADEQUACY OF RESERVES FOR ASBESTOS AND ENVIRONMENTAL ISSUES**

The uncertainties relating to asbestos and environmental claims on insurance policies written many years ago are exacerbated by inconsistent court decisions and judicial and legislative interpretations of coverage that in some cases have tended to erode the clear and express intent of such policies and in others have expanded theories of liability. The industry as a whole is engaged in extensive litigation over these coverage and liability issues and is thus confronted with a continuing uncertainty in its effort to quantify these exposures.

Asbestos remains the most significant and difficult mass tort for the insurance industry in terms of claims volume and exposure value. Based on current published projections, it is expected that the Company will continue receiving asbestos claims.

Significant uncertainty remains as to the ultimate liability of the Company in respect of asbestos related claims due to such factors as the long latency period between asbestos exposure and disease manifestation and the resulting potential for involvement of multiple policy periods for individual claims as well as the increase in the volume of claims by plaintiffs claiming exposure but with no symptoms of asbestos related disease.

Reserves for asbestos and environmental claims cannot be estimated with traditional loss reserving techniques that rely on historical accident year loss development factors. Case reserves and expenses reserves for costs of related litigation have been established where sufficient information has been developed to indicate the involvement of a specific insurance policy. In addition, incurred but not reported reserves have been established to cover additional exposures on both known and unasserted claims.

The reserve carried for asbestos and environmental claims at 31 December 2012 is management's best estimate of ultimate loss and loss adjustment expenses based upon known facts and current law. However, the conditions surrounding the final resolution of these claims continue to change.

Because of future unknowns, additional liabilities may arise for amounts in excess of the current reserves.

These additional amounts, or a range of these additional amounts, cannot now be reasonably estimated and could result in a liability exceeding the reserve by an amount that would be material to the Company's results and shareholders' funds in a future period.

**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**2. UNCERTAINTIES REGARDING THE ADEQUACY OF RESERVES FOR ASBESTOS AND ENVIRONMENTAL ISSUES (continued)**

The Company uses retrocessional agreements to reduce its exposure to the risk of reinsurance assumed. The Company remains liable to the extent that certain quota share reinsurances are finite or that the retrocessionaires do not meet their obligation under these agreements, and therefore the Company evaluates and monitors concentration of credit risk. Provisions are made for amounts considered potentially uncollectible.

As noted above, the Company's loss portfolio includes long-tail risks some of which relate to exposure to losses arising from claims for latent disease and environmental pollution. At 31 December 2012 the Company held gross reserves of £16,909,725 (2011: £18,447,976) in respect of these risks. Reinsurance reserves in respect of these risks are immaterial.

**3. SEGMENTAL ANALYSIS**

All the Company's business is in run-off and, as such, the directors consider its run-off business to be the only segment for reporting under SSAP 25.

**4. CLAIMS INCURRED NET OF REINSURANCE**

	<b>Gross £'000</b>	<b>Reinsurance £'000</b>	<b>Net £'000</b>
<b>2012</b>			
Claims paid	1,761	302	2,063
Outstanding claims brought forward	54,802	(204)	54,598
Revaluation	(1,725)	-	(1,725)
Reduction in outstanding claims	(4,856)	10	(4,846)
Outstanding claims carried forward	48,221	(194)	48,027
Claims incurred	(3,095)	312	(2,783)
<b>2011</b>			
Claims paid	3,395	(105)	3,290
Outstanding claims brought forward	59,538	(167)	59,371
Revaluation	(383)	2	(381)
Reduction in outstanding claims	(4,353)	(39)	(4,392)
Outstanding claims carried forward	54,802	(204)	54,598
Claims incurred	(958)	(144)	(1,102)

The provision for outstanding claims has been set on the basis of information that is currently available, includes estimates of incurred but not reported claims and has been calculated in accordance with accounting policy for Estimation Techniques as set out in Note 1. The process of estimating outstanding claims is inherently imperfect and the resultant calculation of the provision is a best estimate within a range of possible outcomes. Whilst the directors consider that the gross provision for claims and the related reinsurance recoveries are fairly stated on the basis of information currently available to them, the ultimate liability is uncertain and may vary as a result of subsequent information and events as these provisions include claims in respect of long-tail risks. This may result in material adjustments to the gross and net amounts provided.

The directors believe that the uncertainties have been appropriately considered in estimating ultimate losses and that the provision included to meet all unknown outstanding liabilities is adequate to cover claims and losses which have occurred including future developments on known claims as well as those yet to be reported.



**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**5. NET OPERATING EXPENSES**

Expenses charged to the profit and loss account include

<b>Auditor's remuneration</b>	<b>2012 £'000</b>	<b>2011 £'000</b>
Fees payable to the Company's auditor for the audit of the company's annual accounts		
KPMG	57	-
Deloitte	17	97
Fees payable to the Company's auditor for the audit of the annual accounts of the Company's immediate parent company		
KPMG	5	5
<b>Total audit fees</b>	<b>79</b>	<b>102</b>
Fees payable to the Company's auditor for other services		
Taxation compliance services		
KPMG	-	-
Deloitte	(11)	6
<b>Total non-audit fees</b>	<b>(11)</b>	<b>6</b>

All administrative expenses have been charged to the technical account in the current and preceeding years

The Company had no employees during the current and preceding year

Management services were provided by Enstar (EU) Ltd, which charges a management fee

**6. DIRECTORS' EMOLUMENTS**

The directors are not remunerated for their services by the Company. They are employees of Enstar (EU) Limited. They are remunerated by Enstar (EU) Limited for their services to the group and they receive no remuneration as directors of this company. Disclosures regarding Directors' emoluments and staff costs are contained in the financial statements of Enstar (EU) Limited.

**7. INVESTMENT INCOME**

	<b>2012 £'000</b>	<b>2011 £'000</b>
Income from land and buildings	-	258
Income from financial investments	2,842	2,181
Realised (loss)/gain on investments	(73)	816
	<b>2,769</b>	<b>3,255</b>

**8. INVESTMENT EXPENSES AND CHARGES**

	<b>2012 £'000</b>	<b>2011 £'000</b>
Other investment related expenses	58	65
	<b>58</b>	<b>65</b>

**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**9. OTHER (CHARGES)/INCOME**

	<b>2012</b>	<b>2011</b>
	<b>£'000</b>	<b>£'000</b>
Land & Building Depreciation	(278)	(278)
Recovery of Building dilapidation costs	250	-
Loss on translation of foreign currency	(2,024)	(93)
	<u>(2,052)</u>	<u>(371)</u>

**10. TAXATION**

**(a) Analysis of charge/(credit) in the year**

	<b>2012</b>	<b>2011</b>
	<b>£'000</b>	<b>£'000</b>
Current tax	-	-
UK corporation tax on profit for the year	64	(13)
Adjustment in respect of prior years	249	(72)
Foreign tax	<u>313</u>	<u>(85)</u>

**(b) Factors affecting the tax charge/(credit) for the year**

The tax charged for the period and prior period is lower than the standard rate of corporation tax in the UK of 24.5% (2011 26.5%). The differences are explained below

	<b>2012</b>	<b>2011</b>
	<b>£'000</b>	<b>£'000</b>
Profit on ordinary activities before tax	<u>2,760</u>	<u>1,015</u>
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 24.5% (2011 26.5%)	676	269
<i>Factors affecting the charge for the period</i>		
Expenses not deductible for taxation purposes	68	74
Capital allowances for the period in excess of depreciation	(1)	(2)
Foreign tax expensed	(94)	-
Group relief claimed for nil consideration	(649)	(341)
Prior Year adjustment	64	(13)
Foreign tax	<u>249</u>	<u>(72)</u>
Total amount of current tax charge/(credit) on ordinary activities	<u>313</u>	<u>(85)</u>

The rate of corporation tax has reduced from 26% to 24% effective 1 April 2012 and as a result a composite rate of 24.5% has been used in respect of the year ended 31 December 2012. A composite rate of corporation tax of 26.5% was used in respect of the year ended 31 December 2011 following the reduction in the corporation tax rate from 28% to 26% effective 1 April 2011.

**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**10 TAXATION (continued)**

**(c) Factors that may affect future tax charges**

A reduction in the rate of corporation tax to 23% (effective 1 April 2013) has been substantively enacted and the Government has announced its intention to reduce the UK corporation tax rate to 21% with effect from 1 April 2014. It has not been possible to quantify the effect of the announced further rate reduction, although this may reduce the company's current tax charge in future periods.

There is an unrecognised deferred tax asset valued at the substantively enacted rate of corporation tax of 23% (2011: 25%) of £4,000 (2011: £5,000) in respect of decelerated capital allowances.

**11 INVESTMENTS**

	<b>At cost</b>	<b>Market</b>
	<b>£'000</b>	<b>Value</b>
		<b>£'000</b>
<b>2012</b>		
Land and buildings		
Long leasehold	4,675	1,669
Debt securities and other fixed income securities – unlisted	49,369	49,883
Unlisted equity securities	3,529	3,371
Other financial investments	6,806	7,715
	<u>59,704</u>	<u>60,969</u>
	<b>At cost</b>	<b>Market</b>
	<b>£'000</b>	<b>Value</b>
		<b>£'000</b>
<b>2011</b>		
Land and buildings		
Long leasehold	4,675	1,948
Debt securities and other fixed income securities – unlisted	53,786	53,737
Unlisted equity securities	3,634	3,510
Deposits with credit institutions	924	934
Other financial investments	3,267	3,500
	<u>61,611</u>	<u>61,681</u>

None of the land and buildings are occupied by the Company for its own activities.

Certain of the Company's investments are deposited as security for reinsurance obligations with ceding companies or in countries outside the United Kingdom as required under local legislation.

Market value is assessed at bid price, rather than mid-market value.

**NOTES TO THE ACCOUNTS**  
**for the year ended 31 December 2012**

**12. OTHER DEBTORS**

	2012 £'000	2011 £'000
<i>Due within one year</i>		
Amounts due from other group companies	22,054	23,048
Other debtors including taxation	52	1,318
	<u>22,106</u>	<u>24,366</u>

The loan to another group company is repayable on demand and at commercial terms

**13. PLEDGES AND LIENS**

The Company has granted a charge over its invested asset, to collateralise letters of credit provided in the ordinary course of business, totaling £2,198,810 as at 31 December 2012 (2011 £2,382,427)

**14. CALLED UP SHARE CAPITAL**

	2012 £'000	2011 £'000
<b>Authorised share capital</b>		
58,000,000 ordinary shares of £1 each	58,000	58,000
<b>Allotted, called-up and fully paid ordinary shares of £1 each</b>		
Balance at January 1	20,000	30,874
Share capital reduction	-	(10,874)
	<u>20,000</u>	<u>20,000</u>
Balance at December 31	20,000	20,000

**15. SHAREHOLDERS' FUNDS**

	Share capital £'000	Share premium £'000	Profit & loss account £'000	Total £'000
<b>2012</b>				
Balance at 1 January	20,000	-	26,759	46,759
Retained profit for the financial year	-	-	2,447	2,447
	<u>20,000</u>	<u>-</u>	<u>29,206</u>	<u>49,206</u>
<b>2011</b>				
Balance at 1 January	30,874	10,281	13,004	54,159
Retained profit for the financial year	-	-	1,100	1,100
Dividend	-	-	(8,500)	(8,500)
Share capital and share premium reduction	(10,874)	(10,281)	21,155	-
	<u>20,000</u>	<u>-</u>	<u>26,759</u>	<u>46,759</u>

**NOTES TO THE ACCOUNTS  
for the year ended 31 December 2012**

**16. RELATED PARTY TRANSACTIONS**

The Company has taken advantage of the exemption granted in Financial Reporting Standard 8 "Related Party Disclosures" not to disclose transactions between the Company and other wholly owned members of the Enstar Group Limited group

**17. ULTIMATE PARENT UNDERTAKING**

The Company's ultimate parent company and controlling entity is Enstar Group Limited, incorporated in Bermuda. The immediate parent company is Cavell Holdings Limited, incorporated in the United Kingdom.

The annual U.S. Securities and Exchange Commission filing of Enstar Group Limited may be obtained from

U.S. Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, D.C. 20549  
U.S.A.