

STRONGHOLD INSURANCE COMPANY LIMITED

REPORT & ACCOUNTS
2000

Company Registration No. 736581



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STRONGHOLD INSURANCE COMPANY LIMITED

Directors and Management

Directors

J M Massey - Chairman
A M Duffy
H Sopher
K F Watkins

Managing Director

K F Watkins

Secretary

R E Townsend FCIS FCII

Auditors

Ernst & Young

Managing Agents

Cavell Management Services Limited
Rose Lane Business Centre Rose Lane Norwich NR1 1JY England
Telephone: (01603) 599300 Facsimile: (01603) 599432

Registered Office

P O Box 62 Rose Lane Norwich NR1 1JY England

STRONGHOLD INSURANCE COMPANY LIMITED

Report of the Directors

The Directors present their report and the accounts of the Company for the year ended 31 December 2000.

Principal activity and business review

The Company ceased to write new business in 1987 : accordingly the DTI withdrew its authority for the Company to accept contracts of insurance and reinsurance.

The principal activity of the Company continues to be the management of the claims and liabilities which will extend for an indefinite period.

Results and dividends

After allowing for taxation, there was a profit for the year of US\$3,360,000 (1999 - loss US\$778,000). The Directors do not recommend the payment of a dividend for the year (1999 - Nil).

Excess of loss arrangement

During the year, in accordance with the contract terms, the Company commuted a 20% share of the excess of loss arrangement with European International Reinsurance Company, as described in note 15 to the accounts, with a corresponding assumption of the related risk.

Directors

The names of the Directors at the date of this Report appear on page 2. All of the Directors served throughout the year.

The Directors at 31 December 2000 had the following interests in the share capital of the holding company, Stronghold Holdings Limited :

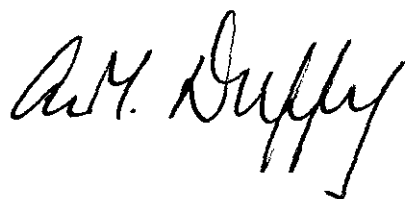
	At 31 December 2000 Ordinary shares	At 31 December 1999 Ordinary shares
A M Duffy	40	40
H Sopher	40	40
K F Watkins	20	20

Auditors

Ernst & Young has stated that, during 2001, it is intending to transfer its business to a limited liability partnership, incorporated under the Limited Liability Partnerships Act 2000, to be called Ernst & Young LLP. If this happens, it is the current intention of the Directors to use their statutory powers to treat the appointment of Ernst & Young as extending to Ernst & Young LLP.

By Order of the Board

A M DUFFY
Director



14 June 2001

Statement of Directors' Responsibilities in respect of the Accounts

Company law requires the Directors to prepare accounts for each financial year which 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 those accounts 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 accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- . prepare the accounts on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Report of the Auditors to the Members of Stronghold Insurance Company Limited

We have audited the accounts on pages 6 to 19 which have been prepared on the basis of the accounting policies set out on pages 6 and 7.

Respective responsibilities of the Directors and Auditors

As described on page 4 the Company's Directors are responsible for the preparation of the accounts in accordance with applicable United Kingdom law and accounting standards. It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion to you. Our responsibilities, as independent auditors, are established in the United Kingdom by Statute, the Auditing Standards Board and by our profession's ethical guidance.

Basis of opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Fundamental uncertainties

In forming our opinion, we have considered the adequacy of the disclosures made in the financial statements concerning the level of uncertainty in respect of :

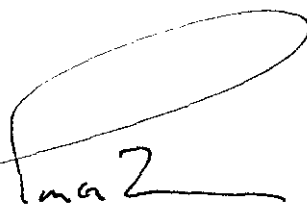
- a. the ultimate liability in respect of the technical provisions relating to gross claims outstanding, related reinsurance recoveries and claims handling expenses. The ultimate liability will vary as a result of subsequent information and events and these may result in significant adjustments to the amounts provided. Details of the circumstances relating to this fundamental uncertainty are described in Note 15.
- b. the adequacy of the current resources of the Company to meet its likely future requirements. As stated in the Statement of Accounting Policies, Basis of preparation, on page 6, the accounts have been prepared on a going concern basis. This basis could be invalidated if the resources of the Company were exhausted by adverse adjustments arising from the resolution of the above uncertainties. The accounts do not include any adjustments which would result from the going concern basis becoming inappropriate.

In view of the significance of these uncertainties we consider that they should be drawn to your attention but our opinion is not qualified in this respect.

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the Company as at 31 December 2000 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

ERNST & YOUNG
Registered Auditor
Cambridge



14 June 2001

Statement of Accounting Policies

(a) Basis of preparation

These accounts are prepared in compliance with Section 255 of, and Schedule 9A to, the Companies Act 1985 and in accordance with applicable accounting standards. They also comply with the Statement of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers.

In preparing the accounts for the year ended 31 December 2000, the Directors, having regard to the uncertainties expressed in Note 15 as to the amounts at which the Company's technical provisions will ultimately be settled, consider that the Company has adequate financial resources to meet its day to day obligations as they fall due. Accordingly the accounts have been prepared on a going concern basis, without including any adjustments that would be required should the financial resources of the Company prove inadequate.

(b) Technical account

- (i) Premiums are accounted for and recorded in the technical account in the year of notification.
- (ii) Provision for claims outstanding comprises provisions for the estimated ultimate cost of claims notified but not settled at the date of the balance sheet and for claims incurred but not notified at that date; the provision reflects anticipated reinsurance and other recoveries, and takes into account future claims handling costs.

The provision for claims outstanding for environmental and asbestos losses, and other losses for Casualty classes, are included after taking into account the future attributable investment earnings.

(c) Investment return

Investment return comprises interest and dividends on an accruals basis, together with realised and unrealised investment gains and losses. Realised investment gains and losses are calculated as the difference between net proceeds on disposal and their purchase. 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 unrealised 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. An allocation of the investment return from the non-technical account to the general business technical account is made on the basis of the relationship between average technical provisions and average shareholders' funds.

(d) Investments

Financial investments are stated at market value. Listed securities are taken at middle market value after adjustments for accrued interest, and other investments are stated at Directors' valuation. Unrealised gains and losses are taken to the profit and loss account.

(e) Foreign currencies

Foreign currency transactions are translated to United States dollars at the rate applicable when recorded in the books, with the exception of transactions in sterling and Canadian dollars, which are translated at rates ruling on 31 December 2000.

Assets and liabilities are shown in the balance sheet at rates ruling on 31 December 2000.

Foreign currency translation gains and losses are taken directly to reserves.

Statement of Accounting Policies

(f) Deferred taxation

Deferred taxation, to the extent that it is likely to crystallise in the foreseeable future, is provided for using the liability method.

STRONGHOLD INSURANCE COMPANY LIMITED
**Profit and Loss Account
for the year ended 31 December 2000**

	Notes	2000		1999	
		US\$'000	US\$'000	US\$'000	US\$'000
Technical account - General business					
<i>Discontinued operations</i>					
Gross premiums written	1		187		172
Outwards reinsurance premiums			(12,287)		818
Earned premiums, net of reinsurance			12,474		(646)
Allocated investment return transferred from the non-technical account			9,270		3,052
Total technical income			21,744		2,406
Gross claims paid		37,907		37,157	
Reinsurers' share		24,912		28,247	
Net claims paid		12,995		8,910	
Gross change in the provision for claims		(7,945)		(59,636)	
Reinsurers' share		(13,971)		(54,168)	
Net change in the provision for claims		6,026		(5,468)	
Claims incurred net of reinsurance	3,4	19,021		3,442	
Net operating expenses	5	-		30	
Total technical charges			19,021		3,472
Balance on the general business technical account			2,723		(1,066)
Non-technical account					
Balance on the general business technical account			2,723		(1,066)
Investment income	7	7,857		6,856	
Unrealised gains on investments		2,769		-	
Investment expenses and charges	8	(719)		(850)	
Unrealised losses on investments		-		(2,666)	
Allocated investment return transferred to the general business technical account		(9,270)		(3,052)	
			637		288
Profit/(loss) on ordinary activities before taxation			3,360		(778)
Tax on ordinary activities	9		-		-
Profit/(loss) on ordinary activities after taxation			3,360		(778)

STRONGHOLD INSURANCE COMPANY LIMITED

**Statement of Total Recognised Gains and Losses
for the year ended 31 December 2000**

	2000 US\$'000	1999 US\$'000
Profit/(loss) on ordinary activities after taxation	3,360	(778)
Currency translation differences on foreign currency net investment	722	179
Total recognised gains/(losses) related to the year	<u>4,082</u>	<u>(599)</u>

Historical Cost Profits and Losses

The inclusion of unrealised gains and losses in the profit and loss account to reflect the marking to market of investments in the balance sheet is not deemed to be a departure from the unmodified historical cost basis of accounting. Accordingly, a separate note of historical cost profits and losses is not given.

**Reconciliation of Movements in Shareholder's Funds
for the year ended 31 December 2000**

	2000 US\$'000	1999 US\$'000
Opening shareholder's funds	8,162	8,761
Total recognised gains/(losses) related to the year	4,082	(599)
Closing shareholder's funds	<u>12,244</u>	<u>8,162</u>

STRONGHOLD INSURANCE COMPANY LIMITED

Balance Sheet **as at 31 December 2000**

	Notes	2000 US\$'000	1999 US\$'000
Assets			
Investments			
Other financial investments	11	103,209	99,208
Deposits with ceding undertakings		<u>1,068</u>	<u>1,141</u>
		<u>104,277</u>	<u>100,349</u>
Reinsurers' share of technical provisions			
Claims outstanding	15	195,645	209,884
Debtors			
Debtors arising out of reinsurance operations		41,269	29,639
Other debtors	12	<u>15</u>	<u>453</u>
		<u>41,284</u>	<u>30,092</u>
Other assets			
Cash at bank and in hand		6,344	11,895
Prepayments and accrued income			
Accrued interest and rent		2,617	2,275
Other prepayments and accrued income		<u>47</u>	<u>66</u>
		<u>2,664</u>	<u>2,341</u>
Total assets		<u>350,214</u>	<u>354,561</u>

STRONGHOLD INSURANCE COMPANY LIMITED

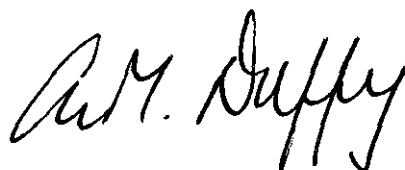
**Balance Sheet
as at 31 December 2000**

	Notes	2000 US\$'000	1999 US\$'000
Liabilities			
Capital and Reserves			
Called up share capital	13	48,079	48,079
Profit and loss account		<u>(35,835)</u>	<u>(39,917)</u>
Shareholder's funds attributable to equity interests	14	<u>12,244</u>	<u>8,162</u>
Technical provisions			
Claims outstanding	15	318,824	328,215
Deposits received from reinsurers		14,987	14,945
Creditors			
Arising out of reinsurance operations		3,636	2,629
Other creditors including taxation and social security		<u>15</u>	<u>6</u>
		<u>3,651</u>	<u>2,635</u>
Accruals and deferred income		508	604
Total liabilities		<u>350,214</u>	<u>354,561</u>



H SOPHER
Director

14 June 2001



A M DUFFY
Director

STRONGHOLD INSURANCE COMPANY LIMITED

**Statement of Cash Flows
for the year ended 31 December 2000**

	Notes	2000 US\$'000	1999 US\$'000
Net cash outflow from operating activities	16	<u>(4,787)</u>	<u>(10,251)</u>
Cash flows were invested as follows:			
Increase/(decrease) in cash holdings		11,362	(3,429)
Net portfolio investment			
Fixed interest securities		(16,149)	(6,822)
Net investment of cash flows	17	<u>(4,787)</u>	<u>(10,251)</u>

Movement in opening and closing cash and portfolio investments

	2000 US\$'000	1999 US\$'000
Net cash inflow/(outflow) for the period	11,362	(3,429)
Cash outflow : portfolio investments	(16,149)	(6,822)
Movement arising from cash flows	<u>(4,787)</u>	<u>(10,251)</u>
Non-cash movements	-	(232)
Changes in market values and exchange rates	3,237	(2,738)
Total movement in cash and portfolio investments	<u>(1,550)</u>	<u>(13,221)</u>
Cash and portfolio investments net of financing at 1 January	111,103	124,324
Cash and portfolio investments net of financing at 31 December	<u>109,553</u>	<u>111,103</u>

STRONGHOLD INSURANCE COMPANY LIMITED

Notes to the Accounts

1 Premiums

Premium income substantially relates to reinstatement premiums and is attributable to discontinued operations.

2 Segmental information

	2000	1999
<i>Technical account</i>	US\$'000	US\$'000
Gross premiums earned	187	172
Gross claims incurred	(29,962)	22,479
Gross operating expenses	(1)	(3)
Gross technical result	(29,776)	22,648
Reinsurance balance	23,229	(26,766)
Net technical result	(6,547)	(4,118)

All premiums relate to general reinsurance business concluded in the United Kingdom.

3 Claims incurred net of reinsurance

	Gross US\$'000	Reins. US\$'000	Net US\$'000
2000			
Claims paid	34,355	24,912	9,443
Claims handling expenses paid	3,552	-	3,552
	37,907	24,912	12,995
Outstanding claims carried forward	318,824	195,645	123,179
Outstanding claims brought forward	326,769	209,616	117,153
	(7,945)	(13,971)	6,026
Claims incurred	29,962	10,941	19,021
1999			
Claims paid	30,873	28,247	2,626
Claims handling expenses paid	6,284	-	6,284
	37,157	28,247	8,910
Outstanding claims carried forward	328,215	209,884	118,331
Outstanding claims brought forward	387,851	264,052	123,799
	(59,636)	(54,168)	(5,468)
Claims incurred	(22,479)	(25,921)	3,442

STRONGHOLD INSURANCE COMPANY LIMITED

Notes to the Accounts

4 Claims handling expenses paid

Claims handling expenses include:

	2000 US\$'000	1999 US\$'000
Auditors' remuneration - audit services	41	42
- non-audit services	-	17

5 Net operating expenses

	2000 US\$'000	1999 US\$'000
Acquisition costs - gross	1	3
- reinsurance	<u>1</u>	<u>(27)</u>
- net	<u>-</u>	<u>30</u>

6 Directors' emoluments

The total remuneration received by the Directors for the year is as follows:

	2000 US\$	1999 US\$
Fees	108,373	117,223
Other emoluments	<u>278,134</u>	<u>317,943</u>
	<u>386,507</u>	<u>435,166</u>

The highest paid director received emoluments of US\$256,094 (1999 - US\$303,103).

7 Investment income

	2000 US\$'000	1999 US\$'000
Income from other investments	7,048	6,856
Gains on the realisation of investments	<u>809</u>	<u>-</u>
	<u>7,857</u>	<u>6,856</u>

8 Investment expenses and charges

	2000 US\$'000	1999 US\$'000
Investment management expenses	146	167
Interest payable on reinsurance balances	573	618
Losses on the realisation of investments	<u>-</u>	<u>65</u>
	<u>719</u>	<u>850</u>

Notes to the Accounts

9 Taxation

No provision has been made in the accounts for corporation tax on the assessable profits for the year as they have been set off against losses of previous years.

10 Deferred taxation

No provision has been made in the accounts for deferred taxation.

Details of the full potential recovery for deferred taxation not provided are given below:

	2000 US\$'000	1999 US\$'000
Realisation of investments at values stated in the balance sheet	-	330
Short-term timing differences	(244)	(579)
Accelerated capital allowances	(1)	(2)
Trading losses available for carry forward	<u>(3,601)</u>	<u>(5,438)</u>
	<u>(3,846)</u>	<u>(5,689)</u>

11 Investments

	Current value		Historical cost	
	2000 US\$'000	1999 US\$'000	1999 US\$'000	1999 US\$'000
Other financial investments				
Debt securities and other fixed income securities (listed)	86,637	99,208	83,604	98,896
Deposits with credit institutions	<u>16,572</u>	<u>-</u>	<u>16,572</u>	<u>-</u>
	<u>103,209</u>	<u>99,208</u>	<u>100,176</u>	<u>98,896</u>

The facility provided to the Company in respect of its letter of credit liabilities is secured by a charge over certain of the Company's investments in debt securities and other fixed income investments.

12 Other debtors

	2000 US\$'000	1999 US\$'000
Amounts due from group undertakings	-	16
Other debtors	<u>15</u>	<u>437</u>
	<u>15</u>	<u>453</u>

STRONGHOLD INSURANCE COMPANY LIMITED

Notes to the Accounts

13 Share capital

	2000 US\$'000	1999 US\$'000
<i>Authorised</i>		
30,000,000 ordinary shares of £1 each	<u>53,445</u>	<u>53,445</u>
<i>Issued and fully paid</i>		
27,000,000 ordinary shares of £1 each	<u>48,079</u>	<u>48,079</u>

14 Shareholder's funds

	Share capital US\$'000	Profit & loss a/c US\$'000	Total US\$'000
2000			
Balance at 1 January	48,079	(39,917)	8,162
Currency translation differences on foreign currency net investment	-	722	722
Retained profit for the financial year	-	<u>3,360</u>	<u>3,360</u>
Balance at 31 December	<u>48,079</u>	<u>(35,835)</u>	<u>12,244</u>
1999			
Balance at 1 January	48,079	(39,318)	8,761
Currency translation differences on foreign currency net investment	-	179	179
Retained loss for the financial year	-	<u>(778)</u>	<u>(778)</u>
Balance at 31 December	<u>48,079</u>	<u>(39,917)</u>	<u>8,162</u>

STRONGHOLD INSURANCE COMPANY LIMITED

Notes to the Accounts

15 Claims outstanding

	Gross US\$'000	Reins. US\$'000	Net US\$'000
2000			
Provision before discounting	445,034	321,851	123,183
Discounting adjustment	<u>(148,322)</u>	<u>(126,206)</u>	<u>(22,116)</u>
	<u>296,712</u>	<u>195,645</u>	<u>101,067</u>
Claims handling expenses	31,050	-	31,050
Discounting adjustment	<u>(8,938)</u>	<u>-</u>	<u>(8,938)</u>
	<u>22,112</u>	<u>-</u>	<u>22,112</u>
	<u>318,824</u>	<u>195,645</u>	<u>123,179</u>
1999			
Provision before discounting	456,714	348,250	108,464
Discounting adjustment	<u>(151,410)</u>	<u>(138,366)</u>	<u>(13,044)</u>
	<u>305,304</u>	<u>209,884</u>	<u>95,420</u>
Claims handling expenses	32,079	-	32,079
Discounting adjustment	<u>(9,168)</u>	<u>-</u>	<u>(9,168)</u>
	<u>22,911</u>	<u>-</u>	<u>22,911</u>
	<u>328,215</u>	<u>209,884</u>	<u>118,331</u>

The level of the gross technical provisions has been set on the basis of information which is currently available, including potential outstanding loss advices, experience of development of similar claims and case law. The methods used, and estimates made, are reviewed regularly. The level of the related reinsurance recoveries is dependent upon both the accuracy of the estimated gross technical provisions and the ultimate ability to pay of the underlying security. The reinsurance recoveries are stated net of the provision for estimated future irrecoverable amounts. The level of the provision for claims handling expenses is dependent upon the settlement of gross technical provisions, collection of related reinsurance recoveries and changes in the factors influencing these.

Whilst the Directors consider that the gross provision for claims and the related reinsurance recoveries, together with the provision for claims handling expenses, are fairly stated on the basis of the information currently available to them, the ultimate liability will vary as a result of subsequent information and events and may result in significant adjustments to the amounts provided. Adjustments to the technical provisions are reflected in the financial statements for the period in which the adjustments are made.

Technical provisions for environmental and asbestos losses, and other losses for Casualty classes, are included after taking into account the future attributable investment earnings at an assumed compound discount rate of 4.5% (1999 - 4.5%) per annum. The assumed settlement pattern for gross claim payments results in an average term for the liabilities of 11.09 years (1999 - 11.07 years). This settlement pattern has been derived from the historic development of claims payments appropriate for the types of claims within these classes, in particular those relating to environmental and asbestos losses. Separate discount factors are applied to the insurance funds for each underwriting year. The unwinding of the discount, included within claims incurred net of reinsurance, during the year was immaterial.

During the year a negative run-off deviation of US\$11.4m (1999 - positive US\$15.5m) was experienced in respect of environmental and asbestos losses.

An excess of loss arrangement was entered into with European International Reinsurance Company on 1 October 1996 and a provision for reinsurance recoveries under this arrangement has been included within the provision for claims outstanding as shown above. During the year, in accordance with the contract terms, the Company commuted a 20% share of this arrangement, with a corresponding assumption of the related risk. The proceeds from this transaction have been included within outwards reinsurance premiums in the profit and loss account.

STRONGHOLD INSURANCE COMPANY LIMITED

Notes to the Accounts

16 Reconciliation of result before tax to net cash flow from operating activities

	2000 US\$'000	1999 US\$'000
Profit/(loss) on ordinary activities before tax	3,360	(778)
Realised investment (gains)/losses	(809)	65
Unrealised investment (gains)/losses	(2,769)	2,666
Decrease in provision for claims outstanding	6,026	(5,468)
Increase in debtors	(11,525)	(2,351)
Increase/(decrease) in creditors	920	(1,807)
Decrease/(increase) in deposits with ceding undertakings	11	(22)
Increase/(decrease) in deposits received from reinsurers	96	(2,495)
Realised exchange losses	(97)	(61)
Net cash outflow from operating activities	<u>(4,787)</u>	<u>(10,251)</u>

17 Movement in cash and portfolio investments

	At 1 Jan 2000 US\$'000	Cash flow US\$'000	Changes to market value and currencies US\$'000	At 31 Dec 2000 US\$'000
Cash at hand and in bank	11,895	11,362	(341)	22,916
Fixed income securities	99,208	(16,149)	3,578	86,637
	<u>111,103</u>	<u>(4,787)</u>	<u>3,237</u>	<u>109,553</u>

Notes to the Accounts

18 Related parties

Companies treated as related parties of the Company for disclosure purposes under Financial Reporting Standard 8, together with the nature of the relationship, are listed below :

Parent undertaking
Stronghold Holdings Limited

Companies related to the Directors
Isis Consulting, Inc.

19 Related party transactions

Details of the emoluments paid to Directors can be found in note 6.

Ms A M Duffy and Mr H Sopher, directors of Stronghold Insurance Company Limited, are also directors of Isis Consulting Inc. During 2000 Isis provided Stronghold with consultancy services for fees totalling US\$587,812, of which US\$76,338 was outstanding at 31 December 2000.

As at 31 December 2000 a balance of US\$1,039 was due to the parent undertaking.

20 Holding company

The Company is a subsidiary undertaking of Stronghold Holdings Limited, the ultimate parent undertaking, which is registered in England. Copies of the accounts of the parent undertaking can be obtained from Clifford Chance, 200 Aldersgate Street, London EC1A 4JJ, England.