CX Reinsurance Company Limited

Annual Report & Accounts 2004

CONTENTS

CHIEF EXECUTIVE OFFICER'S REVIEW

Performance and developments in 2004

Results

In many respects, much progress was achieved during 2004 in the management of the run-off of CX Reinsurance Company Limited. My reflections on the year are dominated, however, by the impact of further extensive deterioration in the US professional liability component of the portfolio, which is consistent with the two previous CEO's reports since the Tawa Group acquired the Company from CNA. In addition, changes to the patterns in which claims are expected to be paid have reduced the level of discount within the balance sheet and as a consequence of these factors, the Company recorded a loss for the financial year of $32.2 million and its surplus decreased to $63.5 million at the end of the year.

Claims deterioration

These developments are clearly a cause for concern. The impact of the need to increase our assessment of ultimate claims, particularly for US professional liability classes, was reduced by the availability of releases of provisions on accounts written prior to 1986. However, a repeat of this degree of deterioration in the later years of the portfolio would eliminate most of the remaining surplus of the Company. A major cause has been the late reporting of claims development by a small number of key cedants. Part of this late notice problem arises from USA cedants' unwillingness to set up reserves for, or notify reinsurers of the existence of, coverage litigation due to their fear of being adversely impacted by discovery of those reserves. In these circumstances of inadequate information from cedants, the Company faces great difficulties when reserving. The Company was a leading reinsurer of US professional liability risks, writing significant lines, and since it does not have the benefit of continuing and profitable premium income streams, the wave of deterioration has hit the financial resources of the Company hard.

Paid claims and reinsurance

The Company's surplus in the context of the size of the liabilities and the level of the discount makes it susceptible to changes in estimates of claims and assumptions relating to future claims payments. Paid claims and run-off expenses during 2004 were $492.4 million, 43.3% higher than the previous year. This increase was in part associated with commutations with a number of cedants, accelerating the settlement of notified outstandings. Another factor was settlement of prior year claims for which the Company was awaiting fully supported presentations of claims from certain brokers and cedants. The Company remains a significant payer of claims to its cedants and policyholders, however, the impact of claims payments in reducing the overall size of the Company's liabilities has been reduced by the need to increase reserves. As a consequence, although discounted reserves net of reinsurance were reduced to $922.1 million from $1,152.9 million at the end of 2003, the Company's surplus as a percentage of net discounted claims declined from 8.3% to 6.9%. Collection of reinsurance recoverables remains critical to the Company's survival. Reinsurers' share of paid claims was $128.3 million compared to $51.1 million in the previous year. At the end of 2004, the ratio of reinsurers' share of technical provisions to the surplus was 3.6:1, marginally lower than at the end of 2003.

Positive developments

As intimated above, there were a number of positive achievements during 2004. Release of provisions for doubtful reinsurance recoveries has resulted from resolution of disputes and reduction in exposure to old year excess of loss reinsurers. Also, the investment strategy of maintaining a portfolio of investments that matches the liabilities enabled the investment return to equal the unwind of the discount in a year when interest rates behaved in ways different from most investment managers' predictions.

The Company's run-off manager, Tawa Management Limited, has assembled a highly professional and skilled team to manage the run-off, with a number of significant hires being made in the year. The team is supported by systems that provide scope for efficient, detailed analysis of financial transactions and trends.

Claims information

I believe that the presentations of claims and the provision of information by cedants and brokers to the Company's claims handlers is improving, following the continued emphasis placed on the need for such information by the Company. It is clear that our fellow reinsurers are also benefiting from these developments, even if their appreciation is quietly and subtly expressed! We are, however, still being hampered by delays in reporting which make the accurate projection of future claims very challenging.

Objectives for 2005

Our primary responsibilities continue to be to the Company's policyholders, cedants and reinsurers. The developments during 2004 have underlined that the only way to manage the run-off of this volatile portfolio of liabilities successfully and equitably is to deliver the strategy set out in the reports of the last two years.

CHIEF EXECUTIVE OFFICER'S REVIEW (CONTINUED)

The key elements of the strategy for the run-off remain to:

- accelerate the natural period of run-off by the execution of a series of commutations of inwards insurance and reinsurance liabilities and outwards reinsurance protections, with a view to the closure of the run-off in the shortest practicable time;
- protect the Company's finite assets and resources;
- assess the validity of claims presented to the Company with due rigour; and
- continue to develop the systems, procedures and human resources available to the Company to provide the infrastructure and support required to achieve the Company's objectives.

No-one should underestimate the challenges to achieving these objectives inherent in the complex CX RE portfolio. However, I have great confidence in the team which Tawa Management Limited has assembled to address these challenges and I thank them for their dedication and hard work over the past year. I look forward to continuing our partnership throughout 2005.

Colin Bird
Chief Executive Officer

FINANCIAL REVIEW

Overview

In the second complete year since the acquisition of the Company by Tawa UK, the benefits derived from the implementation of the run-off strategy have again been significantly affected by the degree of adverse deterioration in the Company's claims reserves. In addition, the impact of paying a greater volume of claims than anticipated during 2004 and the results of resetting the payment patterns for future claims have further reduced the Company's net assets. The loss for the financial year was $32.2 million (2003: $93.9 million). The Company's surplus was reduced as a consequence to $63.5 million at 31 December 2004 (2003: $95.7 million).

Technical account

Net earned premium for the year was $25.5 million (2003: $(15.8) million). This movement, which was most marked within medical malpractice accounts, was predominantly a function of the increases made in ultimate claims in recent years and the impact on contracts with swing-rated premiums. Correspondingly, a charge of $4.0 million was made for additional net commissions payable (2003: a benefit of $6.2 million).

Gross claims and run-off expenses paid during 2004 were $492.4 million (2003: $343.7 million) and reinsurers' share of claims paid was $128.3 million (2003: $51.1 million). The increases in paid claims and reinsurers' share of claims paid were primarily due to the payment of prior year claims awaiting appropriate documentation, along with the impact of certain commutations of inwards and outwards policies agreed during the year.

Net claims incurred prior to discounting (see Note 2h) were $11.9 million (2003: $38.3 million). Substantial deterioration was again experienced within the US liability groups, most notably reinsurance of medical malpractice, directors and officers, errors and omissions and construction risks. Increases in provisions for these classes were in part offset by releases in provisions for policies written prior to 1986, however the benefit of such improvement was reduced by the degree of outwards reinsurance cover on such policies and the impact of discounting. The policy for reserving for asbestos and pollution exposures continues to be the application of suitable industry benchmarks. In order to protect its financial viability, the Company is fully committed to reducing volatility across its liability classes through various strategic initiatives in 2005.

A number of factors have influenced the amount of the discount for the time value of money in the balance sheet which was $270.7 million (2003: $362.3 million) and the impact of the discount on the result for the year which was $(101.0) million (2003: $(8.7) million) after accounting for the effect of foreign exchange movements. Factors which have reduced the benefit of the discount are:

- unwind of the discount due to claims moving closer to maturity;
- changes in the interest rates used to discount reserves;
- commutations of reserves;
- restatement of the level of discount at the start of the year due to refinement in the discounting methodology to enable better application of risk free yield curves to future cash flows by significant currency;
- reassessment of payment patterns for future claims and reinsurance recoveries in the light of actual experience during the year leading to an overall shortening of payment patterns; and
- volume of claims paid during the year being greater than anticipated.

These movements were partially offset by the increase in the impact of the discount due to claims deterioration.

Net operating expenses during 2004 were $(5.4) million (2003: $10.2 million). The negative expense figure in 2004 is attributable to releases of provisions for doubtful reinsurance recoveries due to reductions in the quantum of reinsurance and the resolution of a material dispute over the basis of cession on a particular reinsurance treaty.

Investment return

Investment yield for 2004 was 4.6% (2003: 2.1%). The improved return was a result of the mark to market gains following the flattening of the US dollar and sterling yield curves and the reduction in rates in the medium to longer parts of the curve. The investment return just covered the aggregate of the unwind of the discount and the impact of changes in interest rates on net discounted reserves. The return on the investments relative to the changes in the discounted liabilities was negatively impacted by consistently holding a slightly shorter duration in the portfolio of investments compared to the duration of liabilities in the expectation that interest rates across the curve would rise through 2004. The cost of this was offset by the out-performance of US corporate securities during the year.

The key principle within the investment strategy remains the mitigation of the risks relating to changes in interest rates and foreign exchange rates and to credit and liquidity risks. This mitigation is achieved by broadly matching the duration and currency of the liabilities and maintaining a high quality and readily realisable portfolio of fixed income securities (average rating AA). Within the confines of this strategy, the Company continues to look for opportunities to enhance the return from the portfolio.

FINANCIAL REVIEW (CONTINUED)

Shareholders' funds and solvency

At 31 December 2004, the Company's shareholders' funds were $63.5 million (2003: $95.7 million).

Parent company

Following a restructure of the Tawa Group, with effect from 16 March 2004, the Company's immediate parent company became Tawa UK Limited.

Charles Thresh
Treasurer

REPORT OF THE DIRECTORS

The Directors present their thirty-second annual report together with the financial statements for the year ended 31 December 2004.

Principal activity

The principal activity of CX Reinsurance Company Limited is the carrying out of reinsurance contracts written prior to August 2001 when the Company ceased underwriting new business.

Business review

A review of the Company's business is set out in the Chief Executive Officer's Review and the Financial Review on pages 2 to 5, and the results for the year are set out on pages 9 to 21. As part of the group restructure, on 16 March 2004 the entire issued share capital of the Company was acquired by Tawa UK Limited.

The Directors do not recommend that a final dividend be paid (2003: Nil). The balance from the profit and loss account is to be transferred to reserves.

Directors and Directors' interests

The Directors of the Company are listed on page 7 and, unless otherwise shown, served throughout the year.

None of the Directors held an interest in the shares of the Company. Certain of the Directors are also directors of Tawa Group companies and their interests are disclosed in the accounts of those companies.

None of the Directors had any interest in any material contract entered into or subsisting during the year and relating to the business of the Company.

The Company made no political or charitable donations during the year (2003: Nil).

Statement of Directors' responsibilities

United Kingdom company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit or loss of the Company for that period. In preparing those 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 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 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 financial statements comply with the Companies Act 1985. They are also responsible for the system of internal control, for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors in accordance with the provisions of the Companies Act 1985.

By order of the Board

C H E Jones

Company Secretary
31 March 2005

CORPORATE INFORMATION

Directors

G M J Erulin (France) - Chairman
C G Bird - Chief Executive Officer (Appointed CEO 12 January 2004)
P J Singer
C R Thresh (Appointed 31 March 2004)
P A Jardine - Non-Executive
P M Marcell - Non-Executive (Appointed 31 March 2004)
G Pagniez (France) - Non-Executive
E M Rosenstiehl (France) - Non-Executive (Appointed 6 April 2004)
A J Hamilton - Non-Executive (Resigned 22 March 2004)

Head Office & Registered Office

The London Underwriting Centre
3 Minster Court
Mincing Lane
London
EC3R 7DD

Registered Number: 1086556

(England and Wales)

Company Secretary

C H E Jones FCIS

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CX REINSURANCE COMPANY LIMITED

We have audited the financial statements of CX Reinsurance Company Limited for the year ended 31 December 2004 which comprise the profit and loss account, the balance sheet, and the related notes numbered 1 to 21. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 auditors' 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 auditors

As described in the Statement of Directors' responsibilities, the Company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. They are also responsible for the preparation of the other information contained in the annual report. Our responsibility is to audit the financial statements in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company is not disclosed.

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom 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 financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the Company, 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 financial statements 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 financial statements.

Uncertainties and estimation techniques

In forming our opinion we have considered the adequacy of the disclosures made in Note 3 to the financial statements concerning the principal estimation techniques adopted by the Company and the uncertainties relating to the assessment of provisions for outstanding claims and related reinsurance recoveries. These uncertainties are such that the ultimate liability, which will vary as a result of subsequent information and events, may result in material, but presently unquantifiable, adjustments to the amounts provided. Adjustments to the amount of the provisions are reflected in the financial statements for the period in which the adjustments are made. Our opinion is not qualified in this respect.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2004 and of its loss for the year then ended, and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
London

31 March 2005

PROFIT AND LOSS ACCOUNT

For the year ended 31 December 2004

Technical Account – General Business

	Notes	2004		2003	
		US$000	US$000	US$000	US$000
Gross premiums written	4		**22,054**		(13,501)
Outward reinsurance premiums			**3,447**		(2,327)
Net premiums written			**25,501**		(15,828)
Change in the provision for unearned premiums					
Gross amount		-		-	
Reinsurers' share		-		-	
			-		-
Earned premiums, net of reinsurance	4		**25,501**		(15,828)
Allocated investment income from the Non-Technical Account			**52,722**		26,817
Claims paid					
Gross amount		**(492,409)**		(343,739)	
Reinsurers' share		**128,289**		51,068	
		(364,120)		(292,671)	
Change in the provision for claims					
Gross amount		**530,332**		313,975	
Reinsurers' share		**(178,153)**		(59,641)	
Impact of discounting		**(100,977)**		(8,672)	
		251,202		245,662	
Net claims incurred	4		**(112,918)**		(47,009)
Net operating income/(expenses)	4,5		**5,438**		(10,154)
Balance on the Technical Account – General Business	4		**(29,257)**		(46,174)

Since the Company ceased underwriting in August 2001, the results of the operations relate to discontinued activities. However, the Company continues to manage its general insurance and reinsurance business.

The notes on pages 12 to 21 form part of these financial statements.

PROFIT AND LOSS ACCOUNT (CONTINUED)

For the year ended 31 December 2004

Non-Technical Account

	Notes	2004		2003	
		US$000	US$000	US$000	US$000
Balance on the Technical Account – General Business			**(29,257)**		(46,174)
Exceptional item	6		**-**		(38,808)
Investment return					
Investment income and realised gains	7	**47,320**		64,786	
Unrealised investment gains/(losses)	7	**6,860**		(36,575)	
Investment expenses and charges	7	**(1,458)**		(1,394)	
Allocated to the Technical Account		**(52,722)**		(26,817)	
			-		-
Other charges			**(2,904)**		(8,893)
Loss on ordinary activities before tax			**(32,161)**		(93,875)
Tax on loss on ordinary activities	11		**-**		-
Loss for the financial year	16		**(32,161)**		(93,875)

A statement of total recognised gains and losses is not presented as there have been no gains and losses other than as shown above.

The notes on pages 12 to 21 form part of these financial statements.

BALANCE SHEET
As at 31 December 2004

	Notes	2004 US$000	2003 US$000
Assets			
Investments			
Other financial investments	13	**992,703**	1,222,412
Reinsurers' share of technical provisions			
Claims outstanding	17	**227,352**	350,125
Debtors			
Debtors arising out of direct insurance operations		**969**	4,645
Debtors arising out of reinsurance operations		**102,918**	105,944
Other debtors	14	**3,466**	2,499
		107,353	113,088
Other assets			
Cash at bank and in hand		**20,107**	3,292
Prepayments and accrued income			
Other prepayments and accrued income		**13,147**	14,189
Total assets		**1,360,662**	1,703,106
Liabilities			
Capital and reserves			
Called up share capital	15	**513,226**	513,226
Share premium account	15	**11,330**	11,330
Profit and loss account	16	**(461,043)**	(428,882)
Shareholders' funds attributable to equity interests		**63,513**	95,674
Technical provisions			
Claims outstanding	17	**1,149,465**	1,503,053
Creditors			
Creditors arising out of direct insurance operations		**3,555**	188
Creditors arising out of reinsurance operations		**135,118**	98,358
Other creditors including tax and social security	19	**9,011**	5,833
		147,684	104,379
Total liabilities		**1,360,662**	1,703,106

The notes on pages 12 to 21 form part of these financial statements.

These financial statements were approved by the board of directors on 22 March 2005 and were signed on its behalf on 31 March 2005 by:

Colin Bird
Chief Executive Officer

NOTES TO THE ACCOUNTS

1. Basis of preparation

The financial statements have been prepared in accordance with the provisions of Section 255 of, and Schedule 9A to, the Companies Act 1985 and in accordance with applicable Accounting Standards in the United Kingdom. The financial statements have been prepared in accordance with the historical cost convention, as modified by the revaluation of certain assets, and comply with the Statement of Recommended Practice on Accounting for Insurance Business issued in November 2003 by the Association of British Insurers.

The Company is exempt under Financial Reporting Standard No. 1 (Revised) from the requirement to disclose a cash flow statement since its ultimate parent company includes a cash flow statement in its accounts which are publicly available.

2. Accounting policies

A summary of the more important accounting policies, which have been applied consistently unless otherwise stated, is set out below.

a) Basis of accounting for underwriting activities
All classes of business are accounted for on an annual basis, whereby the incurred cost of claims, commissions and expenses are charged against the earned proportion of premiums, net of reinsurance arising in the financial year.

b) Premiums
Written premiums, gross of commission payable to intermediaries, comprise the Company's share of written premiums on contracts entered into during a financial year, regardless of whether such amounts may relate in whole or in part to a later financial year, exclusive of taxes and duties levied on premiums. Premiums written include adjustments to premiums written in prior accounting periods and estimates for pipeline premiums. For inwards proportional reinsurance treaties and certain binding authorities and lineslips, written premium is included in line with anticipated writing patterns of cedants and agents. Outward reinsurance premiums are accounted for in the same accounting period as the premiums for the related direct insurance or inwards reinsurance business.

c) Unearned premiums
Provision for unearned premiums comprises those elements of gross premiums written and outward reinsurance premiums due which are estimated to be earned in the following or subsequent financial years, computed separately for each insurance or reinsurance contract using the daily pro rata method and taking into account the risk profile of the contracts.

d) Acquisition costs
Acquisition costs comprise the expenses, both direct and indirect, of acquiring insurance policies written during the financial year. Deferred acquisition costs represent the proportion of acquisition costs incurred which correspond to the proportion of gross premiums written which are unearned at the balance sheet date.

e) Claims incurred
Claims incurred include all claims and internal and external claims settlement expense payments made in respect of the financial year, together with the movement in the provision for claims outstanding and internal and external claims settlement expenses, including claims incurred but not reported.

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

f) Claims outstanding
Claims outstanding comprise provisions for the estimated cost of settling all claims incurred up to, but not paid at, the balance sheet date, whether reported or not, together with all future costs related to the management of the run-off of the portfolio of claims. Where applicable, prudent estimates are made for salvage and subrogation recoveries.

The gross claims outstanding provisions and related reinsurance recoveries, net of specific provision for doubtful recoveries, are determined on the basis of information currently available. Adjustments to the amount of the provisions are reflected in the financial statements for the period in which the adjustments are made. The methods used and the estimates made are reviewed regularly.

g) Equalisation provisions
Equalisation provisions are established in accordance with the requirements of UK legislation. These provisions, which are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the balance sheet date, are required by Schedule 9A to the Companies Act 1985 to be included within technical provisions in the balance sheet, notwithstanding that they do not represent liabilities at the balance sheet date. These provisions have no effect on the financial statements for the year (2003: nil).

2. Accounting policies (continued)

h) Discounting
The Company's net technical provisions, estimated as set out in note 3 below, will be paid over a period of many years dependent upon the nature of the underlying risk, the claims outstanding and the related reinsurance recoveries. The net future liabilities have been reduced or "discounted" by an amount representing an estimate of future investment income from income producing assets set aside to meet net claims liabilities. The payment patterns for claims outstanding are derived by the Company's actuaries from analysis of historical patterns experienced by the Company and other comparable companies in run-off. The Company's investment portfolio has been structured to minimise interest rate exposure such that the maturity profile of the fixed income investments matches the maturity profile of the technical provisions. The discount rate, hence anticipated future investment income, has been calculated with reference to relevant dates on the yield curve for Treasury bonds in the currencies in which the investments are held. This is consistent with a mark-to-market value for the invested assets of the Company at the balance sheet date.

i) Foreign currencies
The Company has chosen to represent its financial statements in US dollars as the Directors consider this more closely reflects the trading activities of the business. Premium, claim and commission transactions and investment income during the year are recorded in ledgers denominated in the recognised settlement currencies and translated into US dollars at the exchange rates prevailing at the balance sheet date. Other revenue transactions are recorded at average rates of exchange during the year. Monetary assets and liabilities are converted into US dollars at the exchange rates prevailing at the balance sheet date. Differences on exchange are dealt with in the Non-Technical Account.

The Company pursues a strategy of matching its estimate of the discounted net liability in each significant currency of exposure with currency or currency denominated instruments.

j) Investment income, expenses and charges
Investment income is accounted for on a receivable basis, excluding the imputed tax credit. Interest is accrued up to the balance sheet date. Realised gains or losses represent the difference between net sales proceeds and purchase price.

k) Unrealised gains and losses on investments
Unrealised gains and losses represent the difference between the valuation of investments at the balance sheet date and their purchase price. The movement in unrealised gains and losses comprises the increase/decrease in the year in the value of the investments held at the balance sheet date, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investments disposed of in the current period.

l) Allocation of investment return
All investment income is allocated from the Non-Technical Account to the Technical Account.

m) Taxation
Taxation is provided for by reference to the profits and losses recognised in these accounts after taking account of group relief. Deferred taxation is provided in full on timing differences between recognition of gains and losses in the financial statements and the recognition for taxation purposes. Deferred taxation liabilities are provided in relation to transactions that have occurred by the balance sheet date. Deferred taxation assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

n) Investments
Investments are shown in the financial statements at market value at the balance sheet date. Investment transactions are recognised on a settlement date basis.

3. Estimation techniques and uncertainties

Introduction

The uncertainty inherent in insurance is inevitably reflected in the financial statements of insurance companies. The uncertainty in the financial statements principally arises in respect of the technical provisions of the Company. There is considerable uncertainty as regards the eventual outcome of the claims that have occurred by the balance sheet date but remain unsettled. This includes claims that may have occurred but have not yet been notified to the Company and those that are not yet apparent to the insured.

As a consequence of this uncertainty, the Company needs to apply sophisticated estimation techniques to determine the appropriate provisions.

Estimation techniques

As stated in Note 2, the Company sets its provision for claims outstanding 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 costs and net of salvage and subrogation recoveries. The provision also includes the estimated cost of claims incurred but not reported at the balance sheet date based on statistical methods and market benchmarks, as appropriate.

The adequacy of the claims outstanding provision is assessed by reference to actuarial projections of the ultimate development of claims in respect of each underwriting year. This provision is derived through extensive analysis by the Company's in-house actuaries. The methods used, and the estimates made, are reviewed regularly. The methodology used to project ultimate development for liability classes is reviewed annually by the Company's external actuary.

The provision for claims outstanding and the provision for all future expenses related to the run-off of the net liabilities are discounted to take account of future investment income which will be generated prior to settlement of the claims, as outlined in Note 2h above. The use of discounted technical provisions in representing the economic position of the Company necessarily depends upon the accuracy of the Company's estimate of:

(i) future claims payments and associated reinsurance recoveries;
(ii) the payment profiles attributable to claims payments and related reinsurance recoveries; and
(iii) the future rate of return expected on invested assets.

Uncertainties

Whilst the Directors consider that the gross provision for claims and the related recoveries are fairly stated on the basis of the information currently available to them, there is inherent uncertainty in relation to the insurance industry by its nature. This uncertainty is such that the ultimate liability, which will vary as a result of subsequent information and events, may result in adjustments to the amount provided. Adjustments to the amount of the provisions are reflected in the financial statements for the period in which the adjustments are made.

Significant delays occur in the notification of certain claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the balance sheet date. In particular, estimates of technical provisions inevitably contain inherent significant uncertainties because extensive periods of time may elapse between the occurrence of an insured loss, the claim triggering the insurance under a claims-made coverage, the reporting of that claim and the payment of the claim and the receipt of reinsurance recoveries.

The specific uncertainties affecting the Company's financial statements are as follows:

(i) Asbestos, pollution and other latent claims

Following the commutation during 2002 of the whole account stop loss reinsurance contract with Continental Casualty Company protecting the 1987 & prior underwriting years, the Company has net exposure to claims and claims related expenses emanating from exposures to asbestos, environmental pollution and other latent injuries. In determining the reserves for such claims, the Company's actuaries have taken account of paid and incurred development, suitable industry benchmarks and the nature of the Company's exposure. In addition to the work performed by the in-house actuaries, during the year, a partial exposure analysis was performed by an external consultant. Such claims are frequently subject to disputes such as the extent of coverage and definitions of occurrence and possible legislative changes. Consequently, reserves for claims of this type cannot be determined using traditional actuarial techniques and the uncertainty surrounding the ultimate cost of settlement is greater than for more standard claims within the Company's portfolio. Significant adverse development may have a material impact on the Company's future results and net assets.

3. Estimation techniques and uncertainties (continued)

(ii) 11 September 2001

The Company has material exposure to claims arising from the tragic events in the United States on 11 September 2001. Due to the size and complexity of these losses, the ultimate outcome of the gross claims is subject to greater uncertainty than has been the case with other catastrophes to which the Company has been exposed. Similarly, as a consequence of the issues relating to the gross claims, there is uncertainty surrounding the quantum of retrocessional recoveries accruing to the Company on these losses. The Company has undertaken a careful review of all contracts with exposure to losses from the terrorist attacks and the Directors consider that the reserves and the related reinsurance recoveries have been established on an appropriate basis. The results for the year reflect gross undiscounted reserves of $62.0 million (2003: $103.2 million) and undiscounted reinsurance recoveries of $0 (2003: $44.3 million). As a result of the uncertainty implicit within these claims, these estimates may be subject to potentially significant adjustments in future years.

(iii) Personal accident programme

In 1997, the Company entered into an arrangement with IOA Global Limited ("IOA"), an independent managing general agent based in Philadelphia, Pennsylvania, to develop and manage a book of accident and health coverages. Pursuant to this arrangement, IGI Underwriting Agencies Limited ("IGI"), a personal accident reinsurance managing general underwriter, was appointed to underwrite and market the book under the supervision of IOA. Between April 1, 1997 and December 1, 1999, IGI underwrote a number of reinsurance arrangements with respect to personal accident insurance worldwide (the IGI Program). Under various arrangements, the Company both assumed risks as a reinsurer and also ceded a substantial portion of those risks to other companies, including other CNA insurance subsidiaries, and ultimately to a group of reinsurers participating in a reinsurance pool known as the Associated Accident and Health Reinsurance Underwriters ("AAHRU") Facility. With effect from 1 January 2002, the Company acquired additional reinsurance protection from Continental Casualty Company, a member of the CNA Group so that, from that date, the Company has no remaining net exposure to risks written through IGI.

A portion of the premiums assumed under the IGI Program related to United States workers compensation "carve-out" business. Some of these premiums were received from John Hancock Mutual Life Insurance Company ("John Hancock") under four excess of loss reinsurance treaties ("the Treaties") issued by the Company. While John Hancock has indicated that it is not able to quantify accurately its potential exposure to its cedants on business which is retroceded to the Company, John Hancock has reported $172 million (2003: $92 million) of paid and unpaid losses, under the Treaties. John Hancock is disputing portions of its assumed obligations resulting in these reported losses. The Company has been advised that John Hancock is, or has been, involved in multiple arbitrations with its own cedants, in which proceedings John Hancock is seeking to avoid and/or reduce risks that would otherwise arguably be ceded to the Company through the Treaties. The Company has also been informed that John Hancock has settled several of these disputes, but the Company is not aware of the details of the settlements. To the extent that John Hancock is successful in reducing its liabilities in these disputes, that development may have an impact on the recoveries it is seeking under the Treaties from the Company.

In addition, the Company has instituted arbitration proceedings against John Hancock in which the Company is seeking rescission of the Treaties as well as access to and the right to inspect the books and records relating to the Treaties. Based on information known at this time, the Company believes it has strong grounds to challenge successfully its alleged exposure derived from John Hancock through the ongoing arbitration proceedings. The Company has also undertaken legal action seeking to avoid portions of the remaining exposure arising out of the IGI Program.

The Company has established reserves for its estimated exposure under the IGI Program, other than that derived from John Hancock, and an equal amount due from reinsurers. The Company has not established any reserve for any exposure derived from John Hancock because, as indicated, the Company believes the Treaties will be rescinded. Although the results of the Company's various loss mitigation strategies with respect to the entire IGI Program to date support the recorded reserves, the estimate of ultimate losses is subject to considerable uncertainty due to the complexities described above. As a result of these uncertainties, the Company's results gross of the impact of reinsurance in future periods may be adversely affected by potentially significant additions to gross reserves, although the Company is not able to determine the extent of loss beyond the reserves established. Any such additions to reserves would be fully recoverable from the Company's reinsurers.

(iv) Reinsurer default

The level of uncertainty inherent in the recoverability of reinsurance recoveries is enhanced at this point in time due to the fact that losses resulting from 11 September 2001, coming on top of several years of poor results in the reinsurance industry, have stressed reinsurers' resources. Included in the Company's balance sheet are substantial reinsurance recoveries. The Directors have assessed exposure to bad debts arising from reinsurance dispute or failure and, following careful review, have made a provision against bad debts based on current information available.

4. Segmental reporting

	Insurance Operations 2004 US$000	Reinsurance Operations 2004 US$000	Total 2004 US$000	Insurance Operations 2003 US$000	Reinsurance Operations 2003 US$000	Total 2003 US$000
Gross premiums written	**125**	**21,929**	**22,054**	(317)	(13,184)	(13,501)
Outward reinsurance premiums	**53**	**3,394**	**3,447**	345	(2,672)	(2,327)
Net premiums written	**178**	**25,323**	**25,501**	28	(15,856)	(15,828)
Gross earned premiums	**125**	**21,929**	**22,054**	(317)	(13,184)	(13,501)
Outward reinsurance premiums	**53**	**3,394**	**3,447**	345	(2,672)	(2,327)
Net earned premiums	**178**	**25,323**	**25,501**	28	(15,856)	(15,828)
Allocated investment income from the Non-Technical Account	**6,344**	**46,378**	**52,722**	4,330	22,487	26,817
Gross claims incurred	**92,062**	**(54,139)**	**37,923**	(46,235)	16,471	(29,764)
Reinsurers' share	**(47,756)**	**(2,108)**	**(49,864)**	55,938	(64,511)	(8,573)
Impact of discounting	**(12,151)**	**(88,826)**	**(100,977)**	(1,400)	(7,272)	(8,672)
Net claims incurred	**32,155**	**(145,073)**	**(112,918)**	8,303	(55,312)	(47,009)
Gross operating income/(expenses)	**(591)**	**6,010**	**5,419**	(4,102)	(9,170)	(13,272)
Reinsurers' share	**1**	**18**	**19**	936	2,182	3,118
Net operating income/(expenses)	**(590)**	**6,028**	**5,438**	(3,166)	(6,988)	(10,154)
Balance on the Technical Account – General Business	**38,087**	**(67,344)**	**(29,257)**	9,495	(55,669)	(46,174)

Gross written premium by geographical segment (calculated by domicile of ceding company):

	2004 US$000	2003 US$000
Worldwide	**22,054**	(13,501)
	22,054	(13,501)

Items within the Non-Technical Account are not allocated to lines of business since the Directors do not consider such an allocation to be meaningful.

Net assets are maintained to meet the solvency requirements of the Company as a whole and, as a consequence, segmental analysis of net assets has not been provided.

5. Net operating expenses

	2004 US$000	2003 US$000
Acquisition costs	**(4,028)**	3,053
Other expenses including decreases/(increases) to provisions for doubtful reinsurance recoveries	**9,447**	(16,325)
Gross operating expenses	**5,419**	(13,272)
Reinsurance commissions and profit participation	**19**	3,118
	5,438	(10,154)

5. Net operating expenses (continued)

The provision for unallocated loss adjustment expenses and subsequent adjustments to the provision are included within net claims incurred in 2004 and 2003 respectively.

6. Exceptional item

	2004 US$000	2003 US$000
Settlement of inter-company balance	**-**	(38,808)

During 2003, balances due to and from the Company's former parent company, CX Management Company Limited, as at 31 December 2002 were settled as agreed by the respective boards of directors. This settlement gave rise to the exceptional charge indicated above.

7. Investment return

	2004 US$000	2003 US$000
Investment income	**52,056**	61,733
Realised investment (losses)/gains	**(4,736)**	3,053
	47,320	64,786
Unrealised investment gains/(losses)	**6,860**	(36,575)
Investment management expenses	**(1,458)**	(1,394)
Investment return	**52,722**	26,817

8. Employees' remuneration

From 1 January 2004, all members of staff were transferred from the Company's former parent company, CX Management Company Limited, to Tawa Management Limited. The Company's share of the total remuneration and numbers of employees, including the Directors and Directors' emoluments in note 9, are as follows:

	2004 US$000	2003 US$000
Wages and salaries	**8,338**	6,442
Social security costs	**987**	718
Other pension costs	**806**	667
	10,131	7,827
Average number of employees	**77**	66

The pension scheme for employees of Tawa Management Limited, which is a defined contribution scheme, has been funded by Tawa Management Limited with effect from 1 January 2004. Details of the pension scheme are disclosed in that company's accounts. Previously, the scheme was funded by CX Management Company Limited.

9. Directors' emoluments

	2004 US$000	2003 US$000
Highest paid Director		
Emoluments	**92**	67
Contributions to defined contribution pension scheme	**-**	-
	92	67
All Directors		
Emoluments	**449**	206
Contributions to defined contribution pension scheme	**-**	-
	449	206
Number of Directors qualifying for defined contribution pension scheme	**-**	-

10. Auditors' remuneration

Loss on ordinary activities before tax is stated after charging auditors' remuneration as follows:

	2004 US$000	2003 US$000
Audit services		
Current year	**381**	355
Non-audit services	**265**	216
	646	571

11. Taxation

	2004 US$000	2003 US$000
UK corporation tax at 30%		
Based on the loss for the year	**-**	-
	-	-

The difference between available tax credit on the loss for the year, at the taxation rate of 30%, and the actual tax recognised in the current year financial statements, is due to deferred taxation not being recognised.

12. Rates of exchange

The rates of exchange used to translate items denominated in foreign currency relative to US$1 for significant currencies are as follows:

	2004	2003
United Kingdom	**£ 0.52**	£ 0.56
Euro	**€ 0.74**	€ 0.80

13. Investments

	Market Value		Cost	
	2004 US$000	**2003 US$000**	**2004 US$000**	**2003 US$000**
Listed variable yield securities and unit trusts	**107,241**	25,248	**106,129**	22,092
Listed debt securities and other fixed interest securities	**799,601**	1,152,434	**797,924**	1,159,496
Deposits with credit institutions	**85,861**	44,730	**85,860**	44,730
	992,703	1,222,412	**989,913**	1,226,318

All the listed investments are quoted on a recognised investment exchange.

In accordance with normal market practice, Citibank N.A. and Barclays Bank PLC have issued letters of credit for unearned premiums and outstanding losses. The collateral against these letters of credit includes a pledge to the value of $94.6 million (2003: $100.0 million) against an investment portfolio, and charges to the value of $3.2 million (2003: $3.1 million) against certain bank deposits.

The Company has established trust funds for the benefit of its US reinsurance and US surplus lines policyholders. The values of the trust investments in the respective trusts included above are $500.9 million (2003: $631.3 million) and $61.9 million (2003: $63.4 million).

14. Other debtors

	2004 US$000	**2003 US$000**
Amounts due from group companies	**1,821**	398
Other debtors	**1,645**	2,101
	3,466	2,499

15. Called up share capital and shareholders' funds

Called up share capital	**2004**	**2003**
Authorised 400,000,000 ordinary shares of £1 each (2003: 400,000,000)	**400,000,000**	400,000,000
Allotted, called up and fully paid 343,924,280 (2003: 343,924,280) ordinary shares of £1 each	**$513,226,000**	$513,226,000

Shareholders' funds attributable to equity interests	**2004 US$000**	**2003 US$000**
Loss for the financial year	**(32,161)**	(93,875)
Issue of share capital	**-**	32,137
Net reduction in shareholders' funds	**(32,161)**	(61,738)
Shareholders' funds as at 1 January	**95,674**	157,412
Shareholders' funds as at 31 December	**63,513**	95,674

15. Called up share capital and shareholders' funds (continued)

On 30 January 2003, the Company made the following issues of share capital:

- 12,654,013 £1 shares (equivalent to $20.8 million) at par to strengthen the capital base of the Company; and
- 1 £1 share (at a premium equivalent to $11.3 million) representing a contribution taken into account in 2002 by the Company's former parent company, CNA Financial Corporation, through a hedging arrangement that protected the Company from deterioration of rates of exchange. The contribution, which was accounted for as income in 2002, was capitalised in 2003 with a corresponding charge to Other charges within the Profit and Loss Account.

16. Profit and loss account

	Profit & loss account 2004 US$000
At 1 January as reported	**(428,882)**
Retained loss for the year	**(32,161)**
At 31 December 2004	**(461,043)**

17. Claims outstanding

	Gross Claims 2004 US$000	**Reinsurance 2004 US$000**	**Net 2004 US$000**	**Gross Claims 2003 US$000**	**Reinsurance 2003 US$000**	**Net 2003 US$000**
Provision before discounting	**1,511,500**	**318,711**	**1,192,789**	1,993,526	478,341	1,515,185
Discount	**(362,035)**	**(91,359)**	**(270,676)**	(490,473)	(128,216)	(362,257)
Net of discount	**1,149,465**	**227,352**	**922,113**	1,503,053	350,125	1,152,928

All claims outstanding and the provision for future administrative expenses are discounted to reflect the investment income which will be generated prior to settlement of the underlying claims and expenses.

The average mean term of the total portfolio of net liabilities is 7.44 years (2003: 7.71 years). The mean terms of gross claims outstanding and related reinsurance recoveries are projected separately taking into account historic payment patterns and the expected impact of the Company's cessation of underwriting activities and the implementation of the Company's run-off strategy.

The average, effective rate of investment return used for discounting is 4.27% (2003: 4.28%).

18. Changes to prior year estimates

In the normal course of business the Company's ultimate projections of accident year premiums, commissions and claims are estimated using actuarial methodologies (see Note 3). The impact of movements during the year on prior year estimates, reflected in the Technical Account - General Business, prior to the impact of discounting, was a net gain of $9.6 million (2003: loss of $47.9 million), comprising movements in net earned premiums of (gain) $25.5 million, net incurred commissions of (loss) $4.0 million and net incurred claims (loss) of $11.9 million.

19. Other creditors including tax and social security

	2004 US$000	2003 US$000
Sundry creditors	**9,011**	5,833
	9,011	5,833

20. Related party transactions

Following its sale, the Company entered into a management agreement with Tawa Management Limited for the provision of management services to the Company. The Company is exempt under Financial Reporting Standard No. 8 from the requirement to disclose details of transactions with companies within the same group since its parent company prepares consolidated accounts which are publicly available.

21. Parent company

Following a restructure of the Tawa Group, with effect from 16 March 2004, the Company's immediate parent company became Tawa UK Limited (previously CX Management Company Limited), a company registered in England and Wales, and copies of the financial statements are obtainable from The Registrar of Companies, Companies House. The Company's ultimate holding company is Financiere Pinault SCA, a company incorporated in France. The results of the Company are incorporated in the group financial statements of Financiere Pinault SCA, representing the smallest group in which the Company is consolidated. These financial statements may be obtained from the Tribunal de Commerce de Paris, 1 Quai de Corse, 75004 Paris, France.