MANAGEMENT REPORT 2004

NORTH OF ENGLAND

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Photography front cover: North of England offices seen through Newcastle and Gateshead Millennium Bridge

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MANAGEMENT HIGHLIGHTS

Finance

- Total free reserves rise to US$133.5 million
- North of England's A- rating retained
- Premium income increases to US$156 million

Membership

- The Club's membership reaches 50 million GT
- Net tonnage gain at renewal of 1 million GT
- Major progress in membership refinement

Service

- Claims reduction initiatives
- Integrated risk management support
- High levels of claims handling service

FOUR YEAR COMBINED SUMMARY

Amount in US$ million; All classes

Income and expenditure

	2003/4	2002/3	2001/2	2000/1
Premium	156.5	133.1	106.7	100.3
Investment income less tax	39.7	7.5	0.8	15.8
Exchange gain / (loss)	12.5	10.1	(2.6)	(5.5)
Reinsurance costs	(31.7)	(23.9)	(19.4)	(16.8)
Net claims incurred	(126.7)	(99.1)	(71.2)	(86.1)
Expenses	(16.4)	(15.1)	(11.7)	(12.6)
Increase / (Decrease) in free reserve	33.9	12.6	2.6	(4.9)

Balance sheet

	Feb-04	Feb-03	Feb-02	Feb-01
Investments	421.6	357.5	322.1	303.5
Cash	10.1	14.8	9.7	19.7
Other assets	33.9	37.1	41.1	46.2
	465.6	409.4	372.9	369.4
Creditors	(19.4)	(27.7)	(26.8)	(29.0)
Net assets	446.2	381.7	346.1	340.4
Net outstanding claims	(312.7)	(282.1)	(259.1)	(256.0)
Free reserves	**133.5**	**99.6**	**87.0**	**84.4**

CHAIRMAN'S STATEMENT

Having become Chairman of North of England in mid-June, the publication of the Club's Management Report 2004 provides an early opportunity to share my thoughts with members and, indeed, other readers. I must begin by thanking my predecessor, George Procopiou, for the support that made for a smooth handover. I now look forward to working closely with Vice Chairman Albert Engelsman and my fellow directors.

During George Procopiou's two-year term as Chairman, the Club's membership expanded by 25%. Under his stewardship, this growth was achieved without compromise. There has been no deviation from the Club's long-established principles for expansion through the addition of quality tonnage *and* the maintenance of high standards of service. These principles continue to be respected at a time when the Club's quality thresholds are becoming steadily more onerous.

BILL THOMSON

COMMITMENT TO QUALITY

The Club's entered fleet reached 50 million GT in February 2004. We welcomed eight new members at the 20 February renewal. They share our commitment to quality and added 72 vessels (just over 2.2 million GT) to the Club's book. These accounts are the product of a process which underlines the Club's determination not to regard growth as an end in itself. The new members are first rank owners who have taken time to explore the Club's "personality" before deciding to proceed.

I am also pleased to report continued organic growth. A number of existing members decided to enter more ships. North of England may have grown considerably in recent years, but there has been very little change in the composition of its "Top 10" members.

The Club and its members have benefited from a smooth curve of expansion, free of turbulence and excessive turnover.

Our emphasis on membership refinement and quality will continue under my chairmanship. The Club's quality thresholds will continue to rise. Terms were not offered to some 20 members at the last renewal and a further 10 members did not renew. This removed 1.7 million GT from the portfolio and left the Club with a net gain at renewal approaching 1 million GT.

The last renewal marked a third successive year of premium increases. Once again, however, the vast majority of members accepted the need for higher premiums, so maintaining a financially strong Club. We are well-equipped to represent members' interests in a world increasingly hostile to the shipowner.

Member loyalty is the ultimate test of Club performance. There are no grounds for complacency, as demonstrated by the challenging February 2004 renewal. It was no easy task to get the message across that high freight markets generate

indirect yet significant additional costs, due to deteriorating claims performance.

It may be unpalatable but North of England, in common with other International Group Clubs, must respond to reality and the existence of adverse trends: the remorseless increase in shipowner liabilities, the need to balance claims costs and premium income (freedom from reliance on investment income) and, thirdly, the additional claims arising in an extraordinarily buoyant market.

READY TO FACE THE CHALLENGE

This Club is in good shape to meet the challenges of coming years. This view was endorsed in January 2004, when North of England retained its A- rating and positive outlook from ratings agency Standard and Poor's. Primary Analyst Peter McClean observed: "The positive outlook reflects S&P's expectation that North of England will continue to out perform its peers, particularly in terms of growth of free reserves."

Re-affirmation of the Club's A- rating is an endorsement of strategy and performance. These ratings recognise the Club's strong capitalisation, the continued growth of its free reserves and a very positive management style. That said, a ratings upgrade will depend heavily on our ability to demonstrate effective control over recent loss patterns. We will continue to work closely with members, to make real progress on this front.

Our long term relationships with members, who share the Club's priorities of quality and responsible operation, contribute to the positive outlook. Long-term relationships are important in many areas, including reinsurance. North of England is now in the second year of a three-year retention reinsurance agreement with our long-standing reinsurance partners, AA rated Swiss Re. This provides a combination of stop loss and excess of loss.

The Club and its members form part of a wider international maritime community. The shipping industry must accommodate a world with ever-increasing expectations. We tend to think of this only in the context of safety and pollution prevention. There is, however, more to expectation. There is, for example, the important matter of good governance. This is an area that has revolutionised management practice ashore. It is now having a profound impact in the maritime industries. Best practice is now being driven forward by the desire to be proactive, rather than to respond only as a result of accident or other crisis.

Good governance and transparency have inherent value. North of England's Board supports a progressive policy in this area. Important developments in recent times include the establishment of the Club's

Audit Committee, Investment Committee and Remuneration Committee working alongside the Executive Committee.

It is all too easy to overlook the fact that the provision of P&I cover is an all-year-round activity. This point tends to be masked by the media spotlight on the P&I community during the three months leading up to renewal. Much is made of competition between Clubs, but the day-to-day reality is different. North of England's priorities focus on service rather than competition.

The Club's primary task is easy to define. We provide P&I and other covers within an environment of quality, effective risk management and best value. These factors are inextricably linked, as demonstrated by recent discussions on raising the North of England's quality threshold.

This move has the unanimous support of the Club's Board. There are now 29 shipowner Directors. During this year Barry Gilmour (Stephenson Clarke Shipping) and Kenneth Novack (Lasco Shipping Company) left the Board, having put in much hard work, to the benefit of the Club and the members. We welcomed three new Board Directors: Igor Butorac, of the Croatian cruise/ferry operator Jadrolinija; Lou Kollakis, of Athens-based ship management group Chartworld Shipping Corporation; and Nasser Al-Romaihi, of Qatar Shipping Company.

A VOICE IN THE WIDER WORLD

Turning to the wider arena, the P&I community has shed the isolationist attitudes of the past. There is now a sharper appetite for active involvement in some of the most challenging issues affecting modern shipping. This change of attitude is timely, given the escalation of shipowner liabilities, the failure of many jurisdictions to defend fair play in their courts and the disturbing growth of criminalisation. North of England Board Directors are united in their condemnation of criminalisation. A real effort is required to avoid replays of the unfortunate "Tasman Spirit" affair. The unjust detention of seafarers does nothing to advance the cause of safety and environmental protection. Indeed, it can have exactly the opposite effect, by sending out highly negative signals to shipowners around the world.

"Tasman Spirit" became a cause célébre in 2003-04, but little publicity was given to many other cases where personnel and assets were arrested or held without cause. Criminalisation is rapidly developing against a background of growing public intolerance of shipping accidents and spills. It can be argued that, in a zero tolerance world, zero accidents is the only acceptable goal. Yet shipping is no different from other fields of human activity. There is always a potential for human error or other failure. There must be some recognition that we do not live in an accident-free world.

The shipping industry needs to speak with one voice about these important issues. Unity of purpose must percolate through to all sectors of the industry. North of England, for its part, will continue to play a prominent role in the activities of the International Group. The Club chairs two International Group Subcommittees (Pilotage and Representation) and actively contributes to the work of many more.

Many of the most difficult challenges confronting the industry and the P&I community can be met, at least in part, by more effective communication. One major problem, of course, is the sheer diversity of the audience. It is all too easy to point to the difficulties, but a more constructive frame of mind is now required. We need to invest more time and resources in the construction of a more positive industry profile. We must find ways of conveying the magnitude of shipping's contribution to the world economy. We must also get across a picture of the remarkable reduction in major accidents and spills achieved during the past two decades.

We need to convey our message based on specifics. One example is the ISPS Code. Our members have made a valiant effort to meet the Code's July 1 2004 deadline, but there is little appreciation, beyond immediate shipping circles, of the difficulties involved. It is a pity that the commitment shown by responsible shipowners does not appear to have been matched by some of the world's leading ports.

To conclude, North of England continues to flourish. We can expect more progress in the current year. Despite many external pressures, the Club will not be deflected from its chosen course: continued development as a Club placing an unusual degree of emphasis on conservative, service-driven values. This reflects determination, on the part of the Club's staff, to offer service that is second to none.

BILL THOMSON
CHAIRMAN
JULY 2004

STRATEGY

A CLEAR VISION OF THE FUTURE

North of England is not in the business of setting growth targets and chasing market share. At the same time, this Club has a number of firm goals for its future progress and development. In order to achieve these goals the Club requires a clear vision of its place in the international P&I community. The Club's strategy provides this all-important context.

No organisation can stand still. The Club's central aim is to continue to evolve as the preferred mutual insurance provider for a significant proportion of the world's first tier owners. Much has been achieved but more needs to be done to further enhance the Club's existing reputation for financial strength, quality membership, reliability and service quality.

North of England has experienced strong growth in recent years. The Club's strategy is founded on *controlled* growth - a managed expansion through the application of traditional values and underwriting principles designed to reinforce the quality of a membership now exceeding 50 million GT.

This enlarged membership confers certain benefits. Greater size offers both flexibility and opportunity. The Club has responded by re-defining its concepts of quality and by developing and applying sharper and more sensitive risk management tools.

As might be expected, a larger North of England attracts an increasing number of prominent owners. From the Club's perspective, the main task is to strike an appropriate balance across a range of factors, including the desired membership profile, the generation of premium income, the level of geographic presence and appropriate representation across the ship types.

CONTROLLED GROWTH

The controlled growth of North of England is a success story. It has progressed from a small Club to its position today as an International Group major with a substantial portfolio. Yet the Club has not lost sight of the human dimension of its' service ethos. While new and more demanding quality standards are now applied, the Club continues to take a holistic view at the level of the individual member.

North of England has always taken decisions based on a sound knowledge of the individual member's business goals, operational environment and management style. The Club's strategy recognises the significance of these factors. While it is essential to apply the new risk management disciplines, in order to achieve higher standards of quality, P&I remains a people business at heart.

Management style is a crucial matter for the Club and its members. North of England recognises benefit in traditional values which contribute to quality. The absence of such values within an owner's organisation would raise inevitable concerns over risk exposure. The Club is aware that action against substandard ships is one thing but any attempt to change a substandard management culture, responsible for such ships, is far more difficult.

Shipowners worldwide operate in an increasingly hostile regulatory environment. Severe external pressures strengthen the case for more cooperation between the International Group Clubs on matters of concern to all within the shipping industry. The Clubs need to speak with one voice on key issues and, for this reason, North of England's strategy favours a more proactive International Group.

A QUALITY PORTFOLIO

At the Club-specific level, North of England's strategy is geared for the continued development of a quality portfolio within a framework of financial strength and comprehensive service and support for members. Good progress has been made in the area of financial strength, with a substantial increase in the Club's free reserves. Three years of premium increases have done much to close the gap between premium income and claims costs, yet the Club remains over-dependent on investment returns. A return of 14% was achieved in 2003-04 but this experience is unlikely to be repeated in the current year. Accordingly, the Club has conservatively budgeted a 4% return on investment this year. The Club seeks to further reduce dependence on this second income stream, by concentrating on balance between premiums and claims. The Club will continue to be more conservative than most in this respect.

High freight rates, an upturn in investment income and enhanced free reserves fail to mask the realities, including the gap remaining between premium income and claims costs. The Club's claims experience in recent years is disappointing. High freight markets have exacerbated the situation, contributing to a worrying increase in claims numbers and costs.

Unprecedented freight rates have been achieved in recent times. The transportation costs of low value commodities have exceeded cargo value in some instances. The negative influence of a buoyant market on claims costs is acute in collision cases, when loss of earnings is factored into the equation. Without doubt, the current market makes it more difficult to achieve a neutral technical result without recourse to investment income.

PROACTIVE CLAIMS PREVENTION

The Club has responded by embarking on a more proactive claims prevention programme. It is dangerous to regard an increase in claims numbers and costs as inevitable symptoms of a strong freight market, as that implies acceptance. Instead, North of England regards this as a battle which must be fought and won by the Club and its members, working in unison.

The Club's responsibilities in this area include more effective communication on measures with the potential to reduce claims. In a strong freight market, for example, it is always important to stress the hazards of deferring maintenance. Today, it is even more important to understand causal factors and adopt timely and effective remedial policies.

Certainly, North of England will continue to be proactive in its response to adverse claims trends. In 2003-04 the Club experienced 21 claims with an estimated value of US$1 million plus - nearly double the number in the preceding year. A significant proportion were Admiralty-type claims such as collisions. These statistics do much to explain why the Club regards more rigorous risk management as a priority. The steady rise in the Club's quality threshold seeks to outpace adverse claims trends. The solution, in the final analysis, rests firmly with the Club and its members.

Looking to the future, the Club's strategy envisages further growth, but in the absence of formal targets (a practice regarded as incompatible with North of England's quality objectives). Measured growth will be accompanied by a further increase in financial strength and the addition of new members from the upper rank of the world's shipowners. The refinement of portfolio quality will proceed apace. In recent years, over 70 member groups have left the Club for a variety of reasons, the most prominent being the Club's application of higher quality standards.

In pursuing these goals North of England will retain its long-standing affinity to small and medium sized owners, whilst ever mindful of opportunities to develop relationships with some of the largest owners. Quality is more important than size.

In summary, the Club is determined to hold true to its traditional values. It provides direct service and, above all, is a members' Club, run for their benefit. In this direct relationship, members enjoy a much greater degree of control and participation.

As North of England develops, its role will also expand in the wider arena. The P&I community is part of a global industry with responsibilities extending beyond commercial interest. In the campaign against substandard ships, for example, the Clubs are now more proactive. One important initiative is the more comprehensive sharing of claims-related information. Prevention is the prime objective, through the detection of adverse claims trends and the dissemination of timely guidance and advice. In this respect, the Clubs have the potential to make a major contribution to an important associated task: building a more positive profile of the shipping industry as a responsible provider of services that are the very foundation of world trade.

North of England will continue to play a part in the International Group's efforts to open a more productive dialogue with government around the world.

INDUSTRY ISSUES

LIABILITY: THE GROWING PRESSURE ON SHIPOWNERS

Factors contributing to the steady increase in shipowner liability continued to develop in 2003-04. Regulatory concerns during the year were dominated by the industry's struggle to meet the compliance deadline of July 1, 2004, set for the International Ship and Port Facility Security (ISPS) Code.

In North America the approach taken in this area is viewed by many as an extreme position. One example is the United States' Vessel Automatic Manifest System, introduced in April 2004 and requiring advance notification of all cargoes bound for that country.

The primary purpose of the ISPS Code is to act as a shield against terrorist attack. Incidents such as the assault on the tanker *Limburg* suggest that the ISPS Code is essential, if the terrorists' declared desire to dislocate world trade is to be frustrated. Nevertheless, more pedestrian concerns associated with the Code must now be addressed by shipowners and insurers. One example is the perennial problem of stowaways. The new maritime security regime is bound to make it more difficult to land stowaways. Furthermore, the very presence of stowaways may be regarded by shore authorities as *prima facie* evidence of a failure to apply the Code with necessary vigour.

Until the events of 9/11 changed global perspectives on security, the industry's regulatory focus was dominated by oil pollution. There have been important recent developments in this area. The United States, of course, has a reputation for hard-line policies. The Oil Pollution Act 1990, a product of the *Exxon Valdez* spill, was designed for deterrence. With the benefit of hindsight, it is clear that OPA 90 has been very effective in this role.

TOUGHER REGULATORY POLICIES

Deterrence appears to be the driving force behind the United States Coast Guard's tough action to enforce specific pollution-related rules, such as the Marpol Convention's provisions on oily water separators. During 2003-04 there were a number of cases ending in very heavy fines. It should be noted that United States law provides for imprisonment for offences involving operational pollution from ships.

At the same time, the USCG now demonstrates more pragmatic attitudes in some areas. Closer contacts between industry and regulator appear to have had a positive influence. During 2003 -04, for example, North of England participated in a number of Coast Guard response exercises. The Club's involvement in drills of this kind continues in the current year.

At the global level, November 2003 saw the introduction of a 50% increase in tanker owners' liability for pollution claims. The new limits which were adopted in October 2000, included amendments to the 1992 Protocols of two International Conventions: Civil Liability for Oil Pollution Damage (CLC) and the International Oil Pollution Compensation Fund (IOPC Fund). Yet another increase is in prospect under the optional "Third Tier" arrangements included in the latest, May 2003 Protocol to the IOPC Fund.

As things stand, a total of about US$260 million is now available for compensation under the CLC and Fund Conventions. The shipowner's liability under CLC has risen from US$76.5 million to US$115 million. There is a mechanism in place allowing a further increase to an ultimate, combined CLC/Fund ceiling of US$386 million. The maximum available per incident before November 2003 was US$173 million.

The optional Third Tier is now awaiting ratification and when in force this will provide additional resources to compensate those suffering loss in catastrophic spill events. It is interesting to note that the limits under discussion for the Third Tier closely parallel recent proposals put forward in the EU arena.

Catastrophic spills, fortunately, are rare events. Only three spills, so far, have produced claims exceeding the limits originally provided for under the 1992 Protocols. That said, oil spills *are* becoming increasingly expensive and hence the perceived need for the current increases in compensation available.

CRIMINALISATION: A DISTURBING TREND

It was against this background that the disturbing trend towards the criminalisation of maritime accidents continued to unfold during 2003-04. Some years ago, the Master of the tanker *Evoikos* was imprisoned in Singapore following a severe spill. In November 2002 the loss of the tanker *Prestige* led to the imprisonment of Captain Mangouras. His treatment by the Spanish authorities has been roundly criticised by the international shipping community. At the time of writing he remains in Spain, awaiting trial and unable to return to Greece.

During 2003 members of the crew of the tanker *Tasman Spirit*, together with a Salvage Master, were detained for some months by the Pakistani authorities following a major pollution incident. They were not released until April 2004, following the completion of the wreck removal.

Many leading shipping organisations have voiced concern about criminalisation. They include the International Chamber of Shipping, BIMCO, Intertanko and the International Salvage Union. The Secretary General of the International Maritime Organization, Efthimios Mitropoulos, has been outspoken on this matter. The P&I community has expressed its disquiet but, in the final analysis, only governments can curb the remorseless advance of criminalisation.

There are few grounds for optimism on this front. In June 2004, EU Transport Ministers agreed that accidental pollution in EU waters should be treated as a crime of gross negligence. This could open the door to OPA 90-style penalties, should the proposals be ratified by the European Parliament. This would further undermine the IMO's primacy in the field of maritime safety and pollution prevention.

Spain issued a Royal Decree in February 2004 which allows for demands for huge guarantees from those requesting a place of refuge for a casualty. Recent French legislation provides for the imposition of draconian fines for pollution incidents. Once again, this is legislation designed for deterrence. The law vaguely identifies various levels of offence and provides for savage fines. The Loi Preben II legislation recognises an offence of "basic negligence", which attracts fines of up to €200,000. At the other end of the scale, multipliers (based on up to four times cargo value) may be applied. An accident involving a large container vessel could lead to a fine of astronomic proportions. Fines will be set according to "consequences", but there appears to have been little effort to define scale of damage.

Many parties share North of England's deep concern that the balance between civil and criminal liabilities has been undermined. We are witnessing the rapid evolution of a culture determined to impose criminal penalties for simple negligence. *It need hardly be said that no-one sets out with the deliberate intent of grounding or colliding with another vessel, in the hope of causing the next spill disaster.*

The "*Prestige*" has done much to harden attitudes in Europe. Central to this loss and catastrophic spill was the failure to grant a place of refuge. Spanish policies, post-*Prestige*, have left Spain increasingly isolated at the international level. While the first use of the February Decree caused no great difficulties in relation to the granting of shelter for a casualty (in terms of timing and size of financial guarantee demanded), things may be very different when the next laden tanker seeks refuge along the Spanish coast. It is hard to escape an interpretation that such developments represent a major failure, on the part of governments, to shoulder responsibility.

The impact of criminalisation on the morale of Masters should not be underestimated. This problem is most acute for those individuals with the most experience: Masters moving towards the final years of their careers. Why should a man with, say, three years remaining in a command position run an active risk of imprisonment? Growing numbers of experienced Masters are leaving and will continue to leave the sea earlier than might otherwise have been expected. Who can blame them? After all, there are no parallels ashore. No other industry places employees in the position of direct exposure to such risks.

A WAVE OF LIABILITY

New developments continue to increase the shipowner's exposure to liability. In February 2004 Malta became the tenth state to ratify the 1996 Protocol to the International Convention on Limitation of Liability for Maritime Claims 1976. This fulfilled the conditions for implementation of higher liability limits.

The EU, meanwhile, has signalled its intention to take action if faster progress is not made in implementing the Hazardous and Noxious Substances Convention 1996 and its associated liability regime. In addition, much higher liability limits now apply in the passenger shipping sector. New limits under the Athens Convention were adopted in November 2002. They provide for a 500% increase in liability! These limits were adopted despite the P&I Clubs' deep reservations. Doubts remain over the International Group Clubs' ability to shoulder this onerous burden.

There is more to come! Work is progressing on the IMO's Wreck Removal Convention. This is a significant matter, as the new Convention is likely to require compulsory insurance. The wave of new regulatory initiatives and tougher enforcement policies leads to an inescapable conclusion: owners and Clubs face a flood of more expensive claims. The shipping industry is responsible for the carriage of over 90% of world trade but remains vulnerable to the imposition of ever greater burdens. Indeed, shipping appears to be seen as a soft target.

There are, however, some hopeful signs. In April 2004, for example, IMO's Legal Committee accepted for consideration a joint industry paper on the unfair detention of seafarers. In addition, the European Community Shipowners' Association has now taken up the case of French owners who strongly oppose the ill-defined yet severe penalties under Loi Preben II.

North of England is making a useful contribution to the industry's defence. For example, together with one long standing German member, it has taken the lead in pressing the IMO to draft amendments to the Safety of Life at Sea and Search and Rescue conventions, to give greater recognition to the plight of refugees and other persons in distress. In particular, these revisions should enable Masters to land people without delay or penalty.

To conclude, there has never been more reason for the various sectors of the maritime industry to join together and speak with one voice. This industry has an income exceeding US$200 billion annually. It provides employment for over two million people. In its absence, world trade would collapse overnight. This is an industry with sufficient weight to win more control over its destiny.

"THERE HAS NEVER BEEN MORE REASON FOR THE VARIOUS SECTORS OF THE MARITIME INDUSTRY TO JOIN TOGETHER AND SPEAK WITH ONE VOICE"

RISK MANAGEMENT

THE HOLISTIC APPROACH

In April 2003 North of England took the strategic decision to integrate the Club's Loss Prevention and Survey departments, so establishing the Risk Management Department.

This was no simple reorganisation but, rather, a major step towards the goal of more effective risk management. The change recognises the importance of taking a holistic approach to the management of risk. In the past, the Club's Survey Department focused on the "hardware" - the ships - whereas the Loss Prevention Department concentrated on the "software", the human element.

Pioneering work on the successful application of Safety Management Systems mandated under the ISM Code has been carried out by Dr Phil Anderson, the Club's Risk Management Director. This work highlights the major benefits of an integrated risk management regime embracing both hardware and software.

The merger of the two departments has created one of the largest, multi-disciplinary risk management teams within the ranks of the International Group Clubs. This team has all the technical resources required to investigate the underlying causes of claims and, where appropriate, offers comprehensive support to members. In some cases this involves a "hardware" assessment of the ships and a "software" review of shipboard and shore-based management systems. Such assignments are conducted in a spirit of partnership with members. The Club's role is not to tell a member how to run his business but, rather, to offer support and guidance based on North of England's experience across a very large vessel population. Proactive cooperation, rather than interference, is the objective of North of England's new, holistic approach to risk management.

PRESSURE ON TECHNICAL RESOURCE

This development is timely, for several reasons. Firstly, the Club continues to make real progress in enhancing the quality of the portfolio. Secondly, input from the Club helps to offset the inevitable pressure on owners' technical resources arising from efforts to comply with the ISPS Code deadline of July 1, 2004. The intense activity in the 18-month run-up to this deadline has stretched resources usually dedicated exclusively to safety and pollution prevention. The Club's Risk Management Department is an additional resource, available to members. The aim is to ensure that ISPS-related tasks do not disrupt important safety and environmental work, a factor which might otherwise lead to an increase in claims.

While much attention is now paid to the software component of risk management, and rightly so, the hardware element remains a critical element of the Club's strategy. The Condition Survey Programme is at the heart of effective risk management. A dedicated team is engaged full-time on this programme; some 350 ships were surveyed during the course of the year.

The Condition Survey Programme has taken on a more proactive character. In the past, the emphasis was on vessels of 12 years and over entering the portfolio, together with surveys arising from known deficiencies. The new, wider focus on prevention draws increasingly on members' individual claims records and, in certain cases, explores opportunities to partner and support those members in a position to benefit from the Club's expert input. This programme is expanding in the current year.

COMMUNICATION AND RISK MANAGEMENT

The effectiveness of risk management depends largely on good communication. With this in mind, North of England published four editions of *Signals* during 2003. The first of the issues of this risk management quarterly included a special report on the ISPS Code. Other communications activities included the continued production of publications and posters addressing specific risks. Output on this front included a series of four STCW posters and a related training package. Publications also included new titles in the Club's series of *Loss Prevention Guides*, on subjects such as port state control and the International Collision Regulations.

Looking ahead, the communications priorities include emphasising the importance of investing in personnel of the highest quality - a significant risk management policy in its own right.

During the current year, North of England continues to encourage members to regard the Club's Risk Management Department as a responsive extension to their own offices. This support is of particular value when, for example, an owner enters a period of rapid fleet expansion. In addition, the Club is reinforcing its capability to provide members with timely warning of adverse claims trends.

MEMBERSHIP

PROGRESS IN IMPROVING PORTFOLIO QUALITY

During 2003-04 North of England made substantial progress in its continual drive to improve portfolio quality. At the February 2004 renewal, the Club's P&I book of some 2,500 vessels consisted of around 340 member groups, typically with 6-10 vessels entered. Over the three years to February 2004 the number of member groups has been reduced by around 70.

This profound change is in line with the Club's strategy for consolidation of the book and a sharper focus on members with appropriate risk profiles and the ability to meet higher expectations of quality.

At the February 2004 renewal 135 vessels (representing 1.7 million GT) were not renewed or otherwise left the portfolio (as against 1.5 million GT in the preceding year).

In some cases the decision not to renew arose from a failure to agree terms, but most departures related to claims performance and an inability to meet (or a refusal to accept) the Club's demanding quality thresholds. These thresholds will continue to advance in future years.

The departures were more than offset by an encouraging influx of new members. These owners meet the risk management standards set by North of England. The owners concerned each entered a series of vessels with the Club. The members took their decisions following extensive discussions with the Club, in some cases over periods of several years.

BUILDING RELATIONSHIPS

North of England recognises that growth is not an end in itself. Under this rationale, the Club takes time to build relationships with first class owners who share its ethos of quality.

A landmark was achieved in the first quarter of 2004, when the portfolio reached 50 million GT (40 million GT owned and the remainder chartered). This compares with 35 million GT and 8 million GT as at February 2003.

Some 2.5 million GT was added to the book at renewal, of which 2.2 million GT (72 vessels) represented new business for North of England. The Club welcomed eight new members. In total, there were 92 new vessel entries, 20 representing organic growth - with existing members electing to place more ships with the Club. The outcome met the Club's parameters for controlled expansion: growth with the maintenance of high service standards.

Gross premium income in 2003-04 totalled US$156 million over all classes (P&I: US$147 million). This represents a 17.5 and 18.1% increase on 2002-03 premium income (US$133.1 million and US$124.5 million respectively).

Enhanced portfolio quality remains the central objective. Even the best of owners may experience one or two claims, but the failure to control a persistently adverse claims record is unacceptable - given that the Club is willing to place technical resources at any member's disposal, to help owners deal with problems.

FLEXIBILITY AND THE SERVICE ETHIC

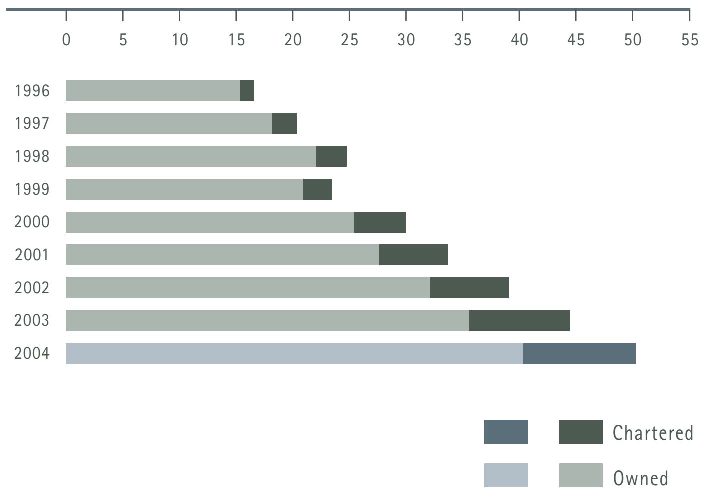
The Club's internal organisation continues to evolve. The aim is to deliver even more effective service. There is now greater emphasis on teams with a specific geographic focus. The Club has yet to be convinced that the benefits of full scale syndication outweigh the potential disadvantages. North of England prefers to serve its members through multi-disciplinary teams, each with a particular geographic orientation but with broader responsibilities towards all members, regardless of their location around the world. This inherent flexibility is an important component of the Club's service ethic.

The wide geographic spread of membership contributes to the Club's balanced portfolio, with no undue weighting from a particular region.

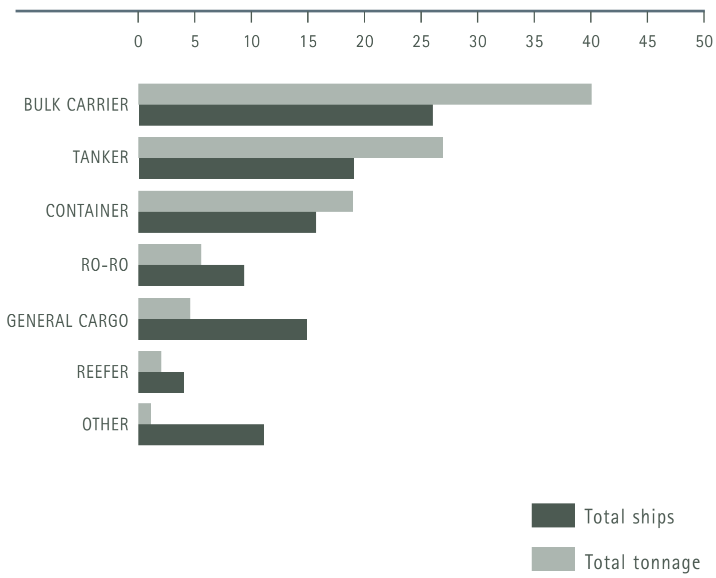
Service quality was further enhanced during the year to February 2004, with all three Club offices increasing staffing levels. The new extranet service North On-line (https://members.nepia.com) was also commissioned. The new facility allows individual accounts to be monitored on-line. It includes the unique *Global Legal Navigator*, compiled for the Club by law firms in 80 countries and providing information on nearly 70 frequently asked questions on shipping law in these jurisdictions.

- Gross premium income rose to US$156.4 million
- P&I tonnage reached a record 50 million GT at renewal
- Tonnage growth primarily from existing members
- Tonnage quality continuously reviewed

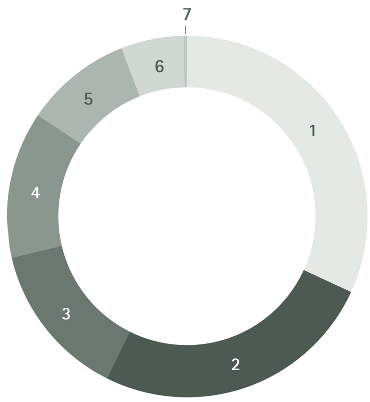
ENTERED TOTAL TONNAGE Millions GT



PERCENTAGE OF TOTAL ENTERED TONNAGE BY SHIP TYPE



TOTAL ENTERED TONNAGE (BY AREA OF MANAGEMENT)



1	Northern Europe	30%
2	Southern Europe	24%
3	Middle East	14%
4	Scandinavia	13%
5	Far East	12%
6	North America	6%
7	Other	1%

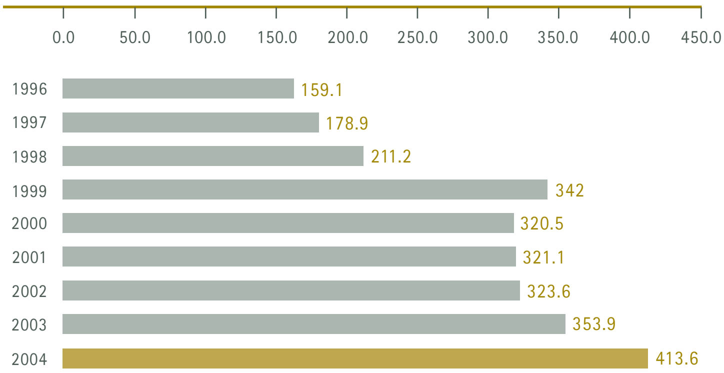
FINANCES

POSITIVE TRENDS CONTINUE

North of England's financial strength continued to grow during the year. Free reserves rose by over US$33 million, to US$133.5 million.

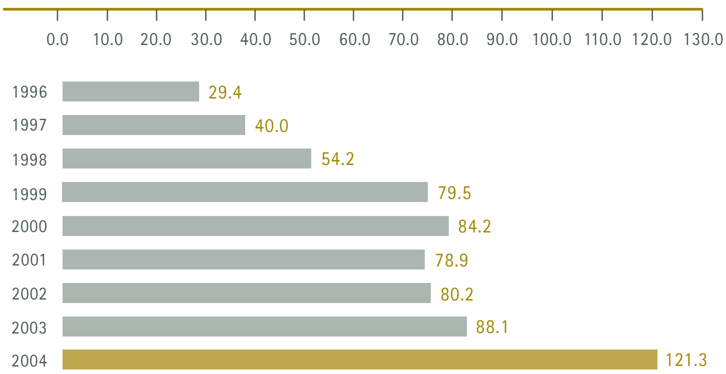
- Investment income increased to US$53.4 million
- Investment strategy remained focused on capital preservation
- Return on P&I investments was 14.11%

P&I CLASS NET ASSETS (US$ MILLIONS)



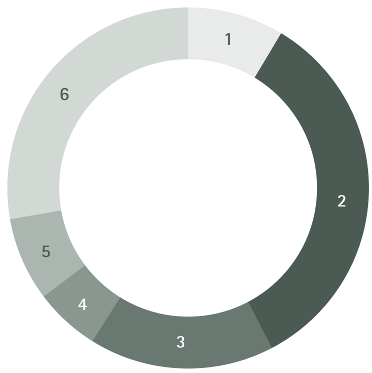
Net assets for the P&I class increased by 17%

P&I CLASS FREE RESERVES (US$ MILLIONS)



The P&I class free reserve increased by 38%

P&I CLASS INVESTMENT PORTFOLIO



1	Cash	8.6%
2	Bonds up to 2 years	33.6%
3	Bonds 2 to 5 years	16.6%
4	Bonds 5 to 10 years	5.9%
5	Bonds over 10 years	7.5%
6	Equities	27.8%

The equity content of the P&I class investments increased to 28% with 72% in bonds and cash.

P&I class net assets rose strongly to US$414 million, an increase of US$60 million. P&I class free reserves increased from US$88.1 million to US$121.3 million.

This highly positive financial outcome reflects, in part, good returns from the Club's investment portfolio. The year saw a very strong rally in the global equity markets. The Club's investment managers made the most of their opportunities.

The P&I class investment portfolio yielded a return of 14.11%, as against 12.24% from the benchmark index. The P&I investment portfolio made a US$50 million contribution to the financial outcome (including exchange gains).

High levels of investment income helped to offset the impact of a poor year for claims. During the 2003-04 P&I year the Club experienced 21 claims exceeding US$1 million (including one claim of US$10 million), as against 11 claims of such magnitude during 2003. Furthermore, claims increased in numbers and values in all areas - offering fresh confirmation of the historic link between strong freight markets and deterioration in claims performance.

The 2003-04 policy year has a US$33 million current deficit, but future investment income and the Club's claims liability development will almost certainly reduce this over time. Indeed, the two preceding policy years each had deficits originally reported at approximately US$20 million, but 2001-02 has already achieved breakeven and 2002-03 is expected to breakeven. That said, the 2003-04 deficit is unlikely to improve to much less than a US$15 million deficit.

PRUDENT INVESTMENT STRATEGY

North of England has three primary investment objectives: to preserve capital, to produce a return outperforming equity and bond indices over the medium term (a five-year rolling period) and, finally, to achieve a performance that is competitive in relation to other members of the International Group of P&I Clubs.

The Club's P&I class investment portfolio retained its conservative character during the year under review, with 72.2% in bonds and cash and 27.8% in equities at February 2004. In broad brush terms, the current strategy provides for equity exposure capped at 30% with the balance of funds held in bonds and cash. The Club moved much closer to this level of equity exposure during the year from the position at February 2003 when equities represented just 18% of the portfolio.

North of England's equity managers performed well during the year. Marathon Asset Management and Capital International both exceeded their indices, returning 58.8% and 50% respectively.

The FD&D portfolio, invested in bonds and cash, produced a 9.6% return - an outcome in line with the index.

The Club's bond managers are Strategic Fixed Income, Citigroup Group, Lazard and Cheyne Capital. It was a relatively benign year for bonds. The only significant change was the decision to cut the average bond duration from 5 years to 2.5 years - a response to concerns about future interest rate rises. The change was implemented by increasing holdings in short dated instruments and cash equivalent investments, which represented 36.1% of the portfolio at February 2004. This reflects the primary objective of capital preservation. The immediate effects of this change were neutral. The Club's UK Investment Committee, meeting in March 2004, agreed to recommend the continuation of this strategy, subject to regular review until such time that it becomes attractive to re-establish the longer duration position.

The Club reports in US dollars and the dollar weakened significantly during the year under review. There were higher returns from non-dollar assets, but non-dollar liabilities also increased. For these reasons, the overall impact was broadly neutral. Looking ahead, the dollar is expected to strengthen in 2004-05, given the expectation of rising US interest rates and growth prospects in the USA relative to Europe. Nevertheless, the dollar is unlikely to recapture all lost ground.

FUTURE PROSPECTS

North of England's financial outcome can be characterised as middle range - a product of conservative strategies that helped the Club avoid losses over a very challenging four-year period. It is unlikely that such high investment returns can be achieved in the 2004-05 year. For this reason, the Club has set a conservative forecast of a 4% return. Against this background, the Club will continue to seek to achieve the goal of a neutral result without recourse to investment income. North of England's strategy will remain conservative, with firm adherence to five key principles:

- Prudent and cautious underwriting.
- Careful and conservative claims reserving.
- Low-risk investment strategy based upon capital preservation.
- Comprehensive and highly secure reinsurance.
- Close monitoring of management expenses.

REINSURANCE

STRIKING A DELICATE BALANCE

Reinsurance issues confronting North of England and all other members of the international P&I community drive straight to the heart of the treatment of risk. As might be expected, there are diverse views amongst the International Group Clubs as to what constitutes an appropriate degree of retention at the pool and Club level.

INTERNATIONAL GROUP REINSURANCE STRUCTURE 2004/2005

Overspill		Liability (shared by pool)		4,250 (approx)
Layer 4	500m	One reinstatement		2,050
Layer 3	500m	Unlimited reinstatements		1,550
Layer 2	500m	Unlimited reinstatements		1,050
Layer 1	500m	75% Unlimited reinstatements	25% Co-insurance	550
Pool retention	45m			50
Club retention	5m			5

US$m (from the ground up)

The 2004-05 reinsurance renewal saw pool retention increase from US$30 million to US$50 million. As a result the International Group's brokers achieved a reduction in reinsurance costs for 2004-05. The savings will be allocated to the International Group's proposed "Hydra" segregated cell facility in Bermuda, a resource allowing it to fund more risk retention in the future.

North of England is comfortable with the increase to US$50 million, yet it must be recognised that it is vital to strike an appropriate balance in this area. Some Clubs favour a further increase on grounds of cost-effectiveness, arguing that the contract is over-insured. Yet an increase to, say, US$100 million could represent a move into unknown territory and could undermine the contract by reducing premium income to the point where the current system, of great importance to the Clubs, becomes much less interesting to reinsurers.

The P&I community's reinsurance arrangements hinge on a delicate balance of interests. With the benefit of hindsight, it can be seen that a US$100 million retention, had it been in place over the past decade, would have freed some US$400 million for accumulation in a captive. At the same time, a single catastrophic event has the potential to completely transform the picture.

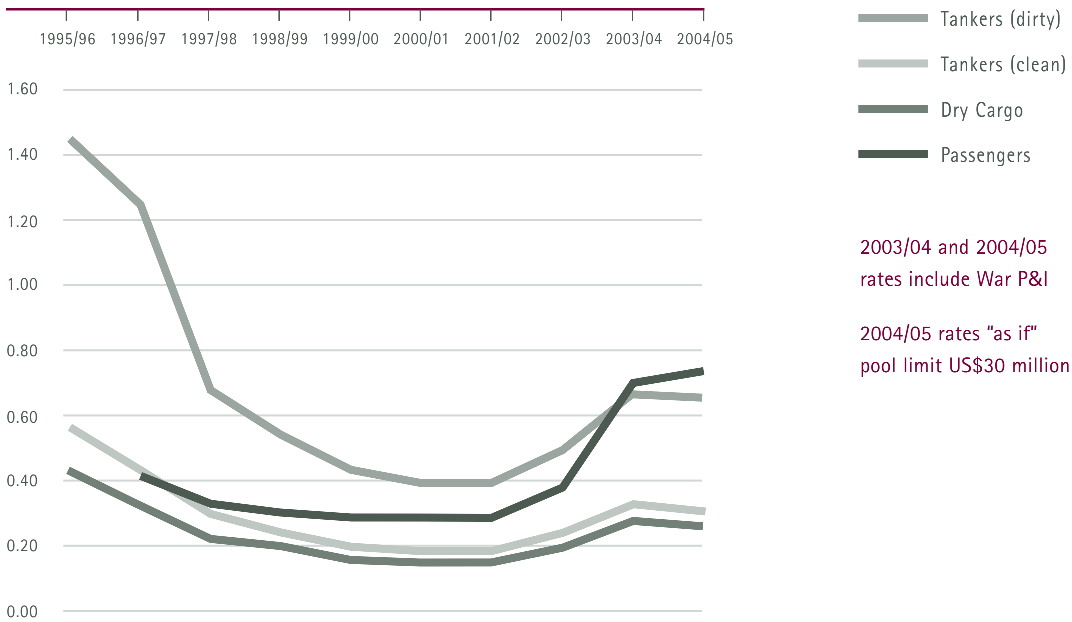
A QUESTION OF DEGREE

With these factors in mind and looking to the future, North of England would favour the acceptance of more risk by the Club and by the International Group, but it is all a question of degree.

This Club would argue that it is important not to lose sight of the very considerable benefits of current relationships with reinsurers. The existing system represents the only available current mechanism allowing the International Group Clubs to provide very substantial levels of cover. Furthermore, the arrangements provide a large measure of accounting convenience. In effect, the Clubs' reinsurance system

"COMPREHENSIVE AND HIGHLY SECURE REINSURANCE PROTECTION"

INTERNATIONAL GROUP REINSURANCE RATES



2003/04 and 2004/05 rates include War P&I

2004/05 rates "as if" pool limit US$30 million

allows them to deliver a high degree of financial certainty to their members, from one year to the next.

It is perfectly legitimate to remind the reinsurers, from time to time, of the significant contribution to their income stream made by the P&I community over the past decade. The Clubs may take the view that reinsurance costs are front-end loaded to an excessive extent, but it must be appreciated that any move to erode the present balance, through a decision to sanction a dramatic increase in the International Group's share of risk, would also incur higher costs. In the final analysis, it is vital to maintain a united International Group position for future dialogue with the reinsurance community.

The reality is that the present pooling system represents the purest expression of risk-sharing, free of profit-chasing, and this factor alone deserves support through solidarity. The guiding principle, however, is constant: to meet the shipowners' needs and the importance of long-term relationships with reinsurers is underlined by North of England's long-established partnership with Swiss Re. The Club's retention contract with Swiss Re was renewed for a further three years, in February 2003.

P&I CLAIMS

LIABILITIES CONTINUE TO BUILD

The total cost of P&I claims during the 2003-04 policy year rose to US$125 million, including the Club's contribution to International Group pool claims. The number of claims totalled 5,181 during the year, as against 5,113 during the preceding year. Once again, cargo claims accounted for a high proportion of total claims - 55%, as against almost 60% in 2002-03.

As recorded elsewhere in this report, higher freight markets produce more claims. This publication also documents the increasing liabilities faced by shipowners, a trend recently reinforced by the May 2004 introduction in the UK of higher limits under the new Protocol to the 1976 Convention on Limitation of Liability for Maritime Claims.

In November 2003 shipowner liability for oil pollution damage increased by 50% under the Civil Liability Convention. There is now the prospect of an optional "Third Tier", to supplement the higher limits in the event of a catastrophic spill. It was envisaged that the "Third Tier" would be funded entirely by oil industry contributions, but the international shipowning community can expect to come under increasing pressure to accept a share of this burden.

The International Group Clubs have signalled their willingness to accept even higher limits under the CLC, rather than participate in "Third Tier" funding, but this approach has been received coolly by the oil industry. It is to be hoped that some accommodation, based on voluntary agreement, can be reached on the difficult issue of shipowners and the "Third Tier". Certainly, compromise on this front would be attractive to the many parties who are reluctant to open up a fresh round of talks on revision of the highly complex CLC and Fund instruments.

Meanwhile, pressure continues to build for a fresh look at liability tests and the nature of claims that are recoverable. Another consideration is the threat posed by "channelling" on a strict liability basis. It is to be hoped that common sense will prevail. If the existing system functions well, why disturb it?

DISAPPOINTING CLAIMS EXPERIENCE

The claims experience during the year was disappointing. There were a number of substantial Admiralty claims, primarily involving collisions and dock damage incidents. There were 21 significant claims (each with an estimated value exceeding US$1 million), as against 11 in the preceding year. As always, the final outcome in financial terms must await the passage of time.

The Club remains concerned at the exaggerated awards made in certain jurisdictions. In some cases the lack of impartiality is blatant, with local claimants openly favoured. There is an increasing reluctance on the part of courts in these jurisdictions to recognise the shipowner's rightful contractual defences. In extreme circumstances, cargoes are rejected and claims made simply as a means of regulating a market in a particular commodity.

Adverse claims trends raise important questions. To what extent does a good freight market exert a negative influence on claims? How many claims arise from working vessels too hard? Cargo interests, of course, have an obvious interest in recovering very high demurrage payments. Is maintenance suffering as owners seek maximum advantage from an abnormally high market? It is impossible to answer such questions with any precision but common sense would suggest that much reduced maintenance windows must have some negative impact.

New pressures have arisen in the effort to meet the ISPS Code's July 1, 2004, compliance deadline. Have other vital activities, such as shipboard safety training, suffered in consequence? Whatever the answer here, the claims picture clearly underlines the shortsightedness of any cutback in training. That would be false economy at its worst.

CLAIMS REDUCTION INITIATIVES

Initiatives to reduce claims continued to receive top priority during the year. North of England is a strong supporter of the International Group's Claims Cooperation Committee and its recent moves to expand the sharing of claims-related information.

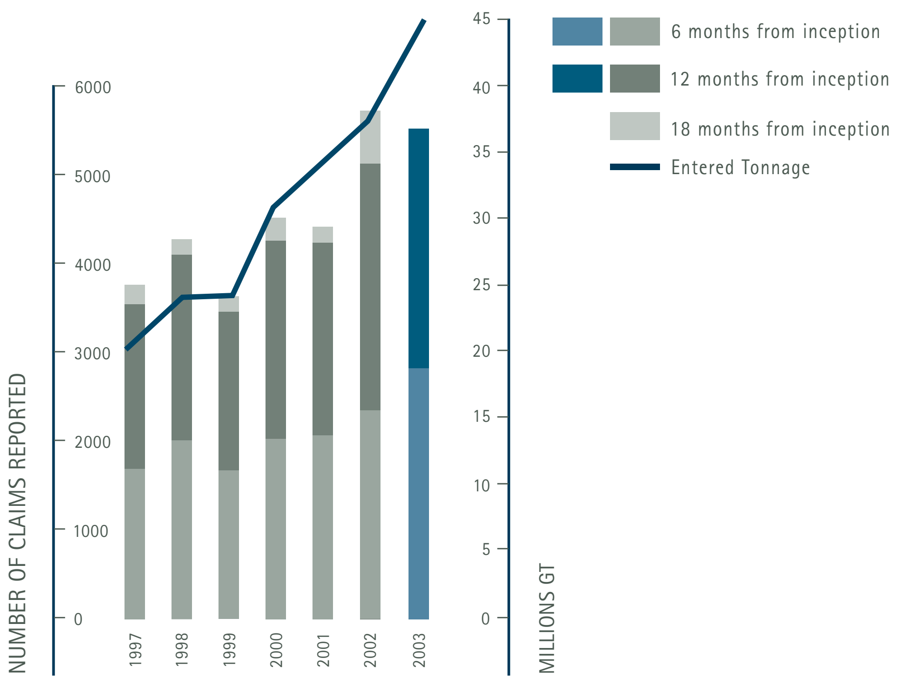
At the Club level, major effort is devoted to major claims prevention. One response during the year was the preparation of the Club's loss prevention guide *Colregs* –

- Total of 5,181 P&I claims reported
- 21 P&I claims with an estimated value greater than US$1 million
- Cargo claims account for 55% of total number

P&I ONLY: NUMBER OF CLAIMS BY VALUE, EXCLUDING POOL CLAIMS
12 months from inception

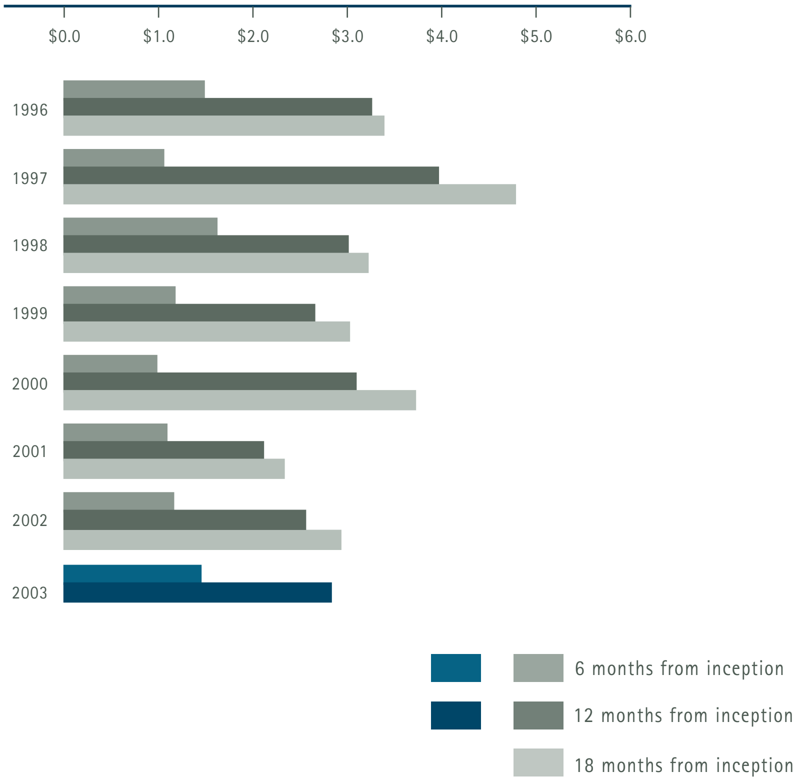
	1997	1998	1999	2000	2001	2002	2003
Over $2.0m	9	4	3	10	2	3	11
$1.0m - $2.0m	2	3	3	3	4	8	10
$0.5m - $1.0m	16	15	20	15	14	22	24
$0 - $0.5m	3,464	4,076	3,423	4,218	4,196	5,080	5,137
Total	3,491	4,098	3,449	4,246	4,216	5,113	5,181

P&I claims breakdown by value



"INITIATIVES TO REDUCE CLAIMS CONTINUED TO RECEIVE TOP PRIORITY"

INCURRED CLAIMS (US$/GT)



A Guide to Good Practice. This publication was distributed in April 2004. It pays particular attention to the significance of human factors in collision cases.

While a high freight market tends to lead to an increase in the number and cost of claims, it also creates fresh opportunities to adjust the commercial balance between charterers and owners, to the benefit of the latter. Yet there is little evidence to suggest that this is taking place. It is a curious fact, but most owners appear to be content with the same tired charterparties, rather than seize the opportunity to negotiate better terms with charterers.

FUTURE PROSPECTS

As to the future, there are many uncertainties surrounding the ISPS Code. It is impossible to gauge its true impact on day-to-day shipping operations. There are suggestions that the Code will disrupt trade and lead to a proliferation of cargo claims - in the worst case ending in the loss of entire cargoes. At the time of writing, however, such views amount to mere speculation. All that can be said, with a degree of confidence, is that some level of disruption is inevitable and that, in the United States at least, the authorities will take a tough line on compliance.

In addition, it seems likely that the introduction of the ISPS Code will make it more difficult to remove stowaways from ships. It is hoped that tighter security will make it more difficult for stowaways to board vessels in the first place, but that remains to be seen.

FD&D

THE INFLUENCE OF HIGH FREIGHT RATES

Vessels entered for FD&D cover increased to 1,164 in the 2003-04 policy year, representing some 43% of North of England's P&I fleet. The number of new claims was slightly down at 789 for the year but loss prevention enquiries during the year totalled 2,149, an increase of 20% on the preceding year.

- 1,164 ships entered for FD&D
- Over 43% of P&I Ships are also entered for FD&D
- Loss prevention enquiries increased to 2,149
- Investment return 9.6%
- Reserves increased to US$8.5 million

FD&D activities during the year were heavily influenced by the dramatic increase in freight rates, which reached levels unprecedented in modern times.

As might be expected, the dynamics of the current market tend to produce claims involving options to extend charters, early and late redelivery, and options to purchase. Consequently, the number of general enquiries on such matters increased. Clauses addressing such matters assume a greater importance in a high freight market. These clauses require extreme care at the drafting stage if they are to be free of challenge.

Over the past few years the Association has adopted a prudent approach to the writing of new building risks and remains aware of the potential exposure to the Class from risks of this type. With the significant increase in new building prices over the period the managers were pleased to note that only two claims were reported in this category.

Both cases involved disputes over options. The circumstances reaffirmed the need for extreme caution when drafting clauses, as the "balance of power" in negotiation has shifted sharply in favour of ship yards overwhelmed by the demand for slots.

During the current year North of England will continue to be measured in its approach to the writing of new build risks.

ISPS CODE SUPPORT

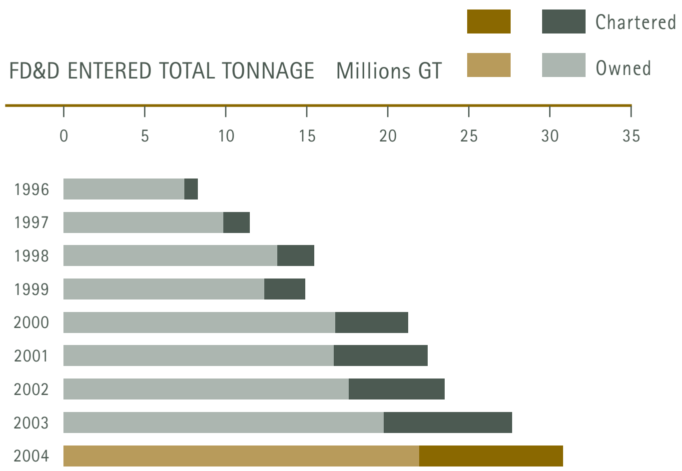
Moves to implement the ISPS Code absorbed much of the industry's management time during 2003-04. The extent of the demands, especially in the case of the United States and Canada, appeared to take some owners by surprise as did the introduction of new reporting procedures (AMS regulations) coupled with the need for the establishment of Carrier Bonds. In this area, North of England's FD&D team took on an important role, offering advice and guidance on the drafting of appropriate clauses, resolving disputes and liaising with organisations such as BIMCO.

Another feature of the year was the upturn in the number of bunker quality disputes, possibly a reflection of increased vessel utilisation and pressure on suppliers.

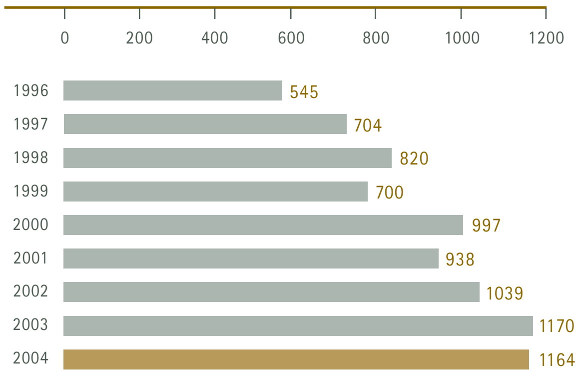
The Club's main service objective for FD&D is unchanged: to provide effective and timely legal support to members and to seek acceptable commercial outcomes. The Club also remains proactive in its response to new commercial and contractual challenges of consequence to members. During 2003-04 the Club further reinforced the FD&D team with the addition of two experienced lawyers, one based in Newcastle and the other in Greece.

The FD&D class bond portfolio realised a healthy investment return, with reserves increased to US$8.5 million. However, the Managers remain aware of the need to continue to strengthen the FD&D class finances particularly as any sustained downturn in the current market is likely to result in an increase in claims and consequent expense to the Class.

FD&D ENTERED TOTAL TONNAGE Millions GT



AVERAGE NUMBER OF SHIPS INSURED FOR FD&D



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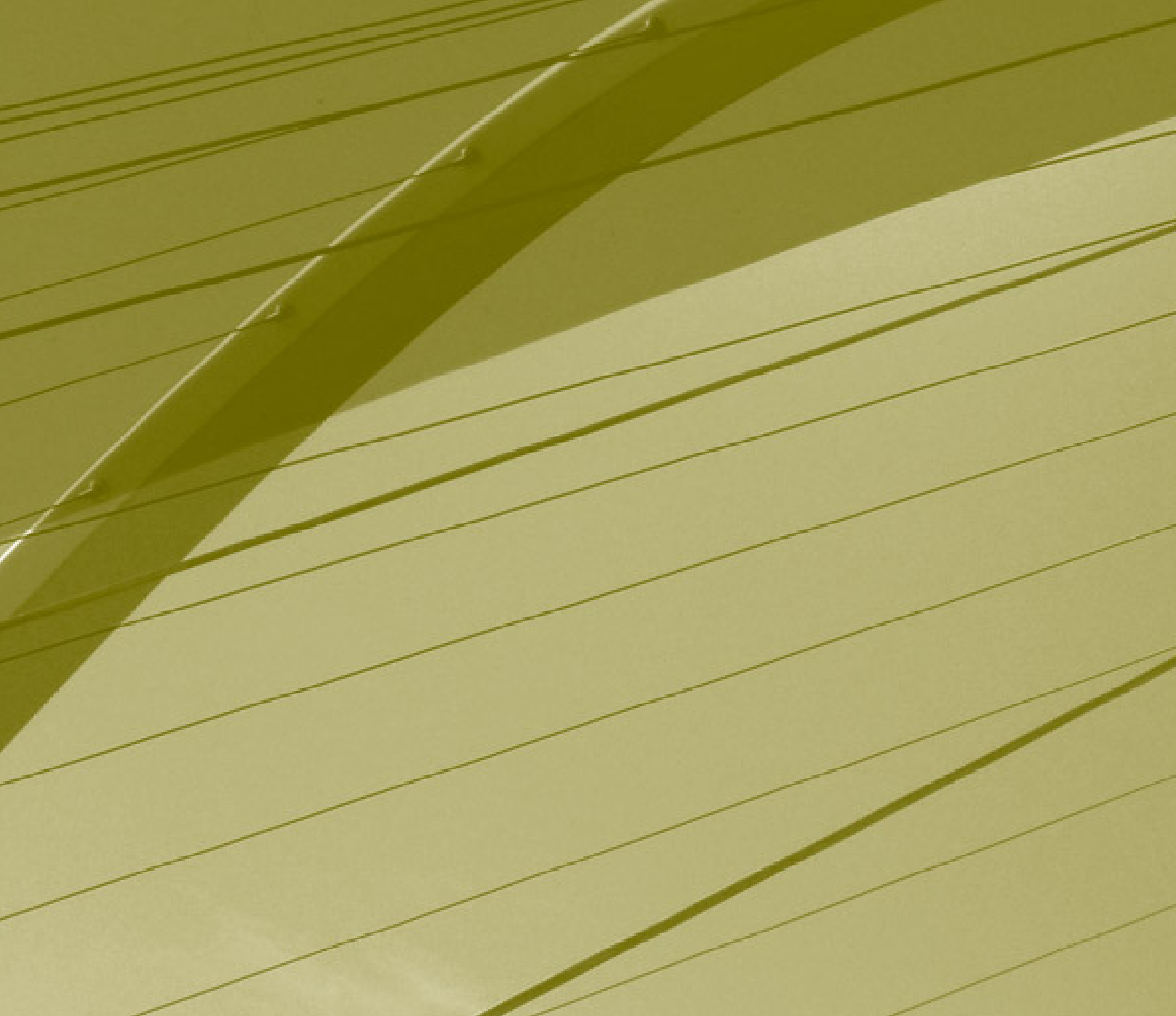
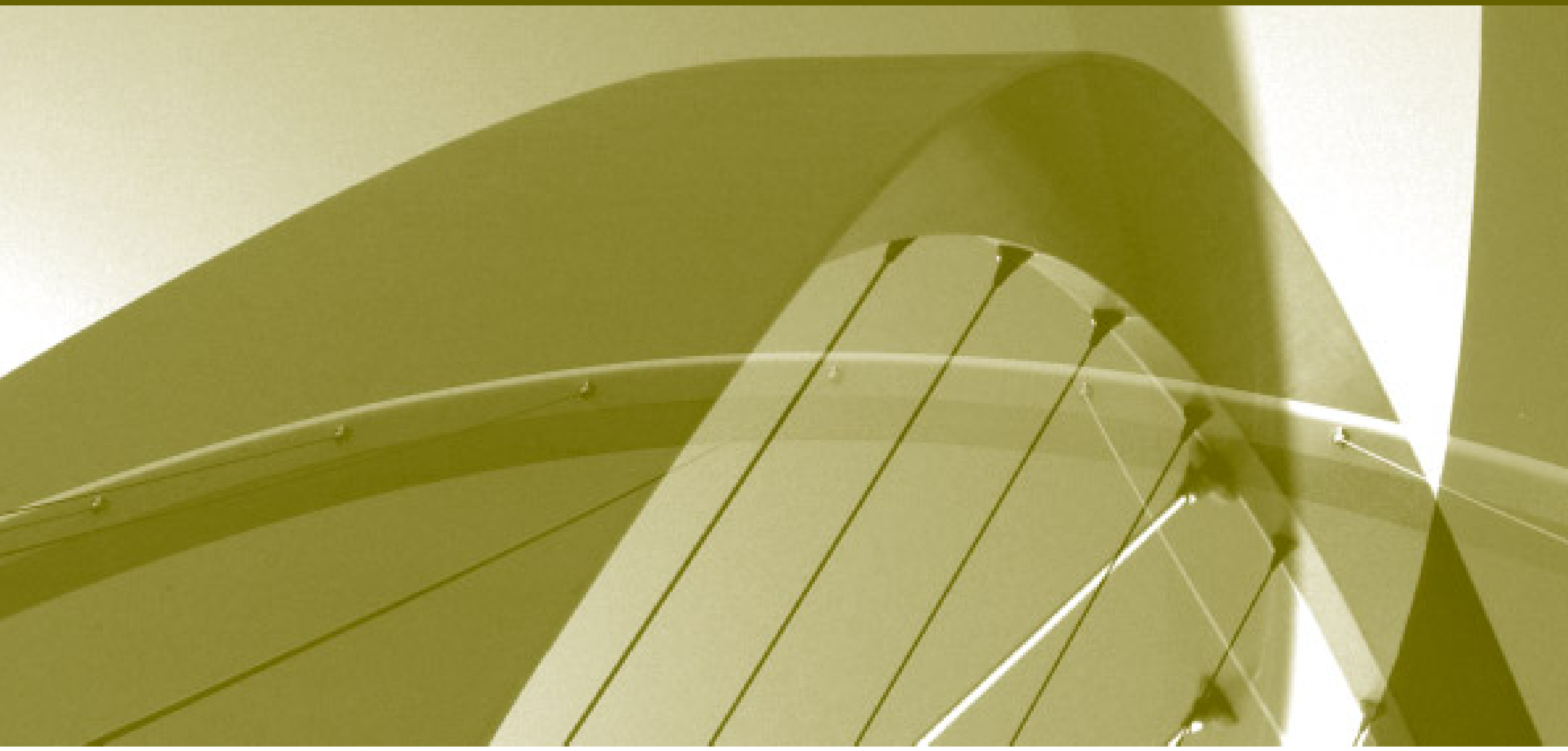




COMBINED FINANCIAL STATEMENTS

North of England P&I Association Limited's financial statements for the year ended 20 February 2004 are enclosed as a separate document and North of England Mutual Insurance Association (Bermuda) Limited's financial statements for the same period will be issued to Members on behalf of the Managers of that company. Financial Statements which combine the results and financial position of the UK and Bermuda Associations follow on pages 29 to 43 and have been prepared to allow Members to gain a picture of the overall position. The statements have been prepared for illustrative purposes only and have no legal standing. The return to the Financial Services Authority is based upon the combined position.

Any reference to the Club in the preceding narrative relates to the combined position of the UK and Bermuda Associations, which have common membership but do not have common control.

ACCOUNTANTS' REPORT

Accountants' Report to The Members of North of England Protecting and Indemnity Association Limited and North of England Mutual Insurance Association (Bermuda) Limited

We report on the unaudited combined financial statements and policy year statement of North of England Protecting and Indemnity Association Limited ("NEPIA") and North of England Mutual Insurance Association (Bermuda) Limited ("NoE(Bermuda)") for the year ended 20 February 2004 ("the combined financial statements").

Our Report is prepared solely for the confidential use of NEPIA and NoE(Bermuda), and solely for the purpose of informing the members of NEPIA and NoE(Bermuda). To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than NEPIA and NoE(Bermuda) and of the common members of NEPIA and NoE(Bermuda) as a body, for our work, for this report, or for the opinions we have formed.

RESPONSIBILITIES

NEPIA is responsible for the preparation of the combined financial statements and the policy year statement.

It is our responsibility to carry out procedures designed to enable us to express an opinion as to whether the combined financial statements and policy year statement have been accurately extracted from the financial statements of NEPIA and NoE(Bermuda) for the year ended 20 February 2004.

BASIS OF OPINION

We have performed the procedures enumerated below with respect to the combined financial statements. The procedures were performed solely to assist the Directors with the preparation of the combined financial statements and are summarised as follows:

1. We agreed NEPIA's figures used in the combined financial statements working papers to the signed statutory consolidated financial statements of NEPIA as at 20 February 2004.

   The auditors' report on the statutory consolidated financial statements of NEPIA was issued by ourselves on 24 May 2004 and was unqualified;

2. We agreed NoE(Bermuda)'s figures used in the combined financial statements working papers to the signed statutory financial statements of NoE(Bermuda) as at 20 February 2004.

   The auditors' report on the statutory financial statements of NoE(Bermuda) was issued by Moore Stephens & Butterfield on 20 May 2004 and was unqualified;

3. We checked the numerical accuracy of the combined financial statements working papers, including the policy year statement; and

4. We reviewed the accounting policies adopted by NEPIA and NoE(Bermuda), as defined in their respective statutory financial statements, to review whether they are consistent.

Our procedures did not constitute an audit in accordance with Auditing Standards. In particular we have not verified any information or documentation provided to us and we should not be taken to have done so beyond the procedures described above.

OPINION

We report that:

(a) The combined financial statements and policy year statement have been accurately compiled from the statutory financial statements of NEPIA and NoE(Bermuda); and

(b) Consistent accounting policies have been adopted by NEPIA and NoE(Bermuda).

Deloitte & Touche LLP

Chartered Accountants

Newcastle upon Tyne

24 May 2004

COMBINED INCOME AND EXPENDITURE ACCOUNT

FOR THE YEAR ENDED 20 FEBRUARY 2004

	Notes	Total 2004 US$000's	Total Restated – Note 1 2003 US$000's
TECHNICAL ACCOUNT – GENERAL BUSINESS			
Gross premiums written	2	156,446	133,103
Outward reinsurance premiums	3	(31,686)	(23,850)
		124,760	109,253
Allocated investment return transferred from the non-technical account		40,883	8,110
Gains / (Losses) on exchange		12,470	10,095
Total technical income		178,113	127,458
Claims paid			
Gross amount	4	(105,872)	(98,201)
Reinsurers' share		9,700	22,083
		(96,172)	(76,118)
Change in the provision for claims			
Gross amount	5	(64,163)	(20,324)
Reinsurers' share		33,599	(2,709)
		(30,564)	(23,033)
Net operating expenses	6	(16,361)	(15,080)
Total expenditure		(143,097)	(114,231)
Balance on the technical account for general business		35,016	13,227
NON-TECHNICAL ACCOUNT			
Balance on the general business technical account		35,016	13,227
Investment income	7	4,165	2,608
Unrealised gains / (losses) on investments		38,251	6,963
Investment expenses and charges		(1,533)	(1,461)
		40,883	8,110
Allocated investment return transferred to the general business technical account		(40,883)	(8,110)
Surplus / (Deficit) on ordinary activities before tax		35,016	13,227
Tax on ordinary activities	8	(1,152)	(626)
Surplus / (Deficit) for the financial year		33,864	12,601
Transfer to Contingency fund	11	(14,166)	(9,232)
Transfer to / (from) Income and Expenditure reserve		19,698	3,369
Income and Expenditure reserve brought forward		(50,314)	(53,683)
Income and Expenditure reserve carried forward		(30,616)	(50,314)

	Protecting & Indemnity Class	Protecting & Indemnity Class Restated – Note 1	Freight, Demurrage & Defence Class	Freight, Demurrage & Defence Class	War Risks Class	War Risks Class
	2004 US$000's	2003 US$000's	2004 US$000's	2003 US$000's	2004 US$000's	2003 US$000's
	146,943	124,460	8,957	8,381	546	262
	(30,780)	(23,228)	(420)	(383)	(486)	(239)
	116,163	101,232	8,537	7,998	60	23
	39,650	6,124	285	2,093	948	(107)
	10,346	9,450	2,131	603	(7)	42
	166,159	116,806	10,953	10,694	1,001	(42)
	(101,507)	(94,835)	(4,361)	(3,363)	(4)	(3)
	9,786	22,083	(86)	–	–	–
	(91,721)	(72,752)	(4,447)	(3,363)	(4)	(3)
	(61,988)	(18,072)	(2,175)	(2,252)	–	–
	33,664	(2,137)	(65)	(572)	–	–
	(28,324)	(20,209)	(2,240)	(2,824)	–	–
	(13,663)	(13,291)	(2,541)	(1,673)	(157)	(116)
	(133,708)	(106,252)	(9,228)	(7,860)	(161)	(119)
	32,451	10,554	1,725	2,834	840	(161)
	32,451	10,554	1,725	2,834	840	(161)
	2,740	2,521	1,425	1,341	–	(1,254)
	38,308	4,964	(1,034)	841	977	1,158
	(1,398)	(1,361)	(106)	(89)	(29)	(11)
	39,650	6,124	285	2,093	948	(107)
	(39,650)	(6,124)	(285)	(2,093)	(948)	107
	32,451	10,554	1,725	2,834	840	(161)
	(1,076)	(512)	(54)	(119)	(22)	5
	31,375	10,042	1,671	2,715	818	(156)
	(10,322)	(6,357)	(3,844)	(2,875)	–	–
	21,053	3,685	(2,173)	(160)	818	(156)
	(51,547)	(55,232)	(1,594)	(1,434)	2,827	2,983
	(30,494)	(51,547)	(3,767)	(1,594)	3,645	2,827

COMBINED BALANCE SHEET

AT 20 FEBRUARY 2004

	Notes	Total 2004 US$000's	Total Restated – Note 1 2003 US$000's
ASSETS			
Investments			
Land and buildings		9,910	8,448
Other financial investments	9	411,684	349,019
		421,594	357,467
Reinsurers' share of technical provisions			
Claims outstanding		112,861	79,262
Debtors			
Debtors arising out of direct insurance operations	10	24,273	24,796
Debtors arising out of reinsurance operations		2,667	2,825
Other debtors		1,665	1,533
		28,605	29,154
Other assets			
Tangible assets		2,305	1,849
Cash at bank and in hand		10,059	14,828
		12,364	16,677
Prepayments and accrued income		2,988	6,086
Total assets		578,412	488,646
LIABILITIES			
Reserves			
Income and expenditure account		(30,616)	(50,314)
Contingency fund	11	164,074	149,908
		133,458	99,594
Technical provisions			
Claims outstanding			
Gross amount		425,520	361,357
Creditors			
Creditors arising out of direct insurance operations		1,889	2,065
Creditors arising out of reinsurance operations		10,370	6,882
Amounts owed to credit institutions		3,691	3,922
Provision for taxation		910	670
Other creditors		438	12,294
		17,298	25,833
Accruals and deferred income		2,136	1,862
Total liabilities		578,412	488,646

Protecting & Indemnity Class	Protecting & Indemnity Class Restated – Note 1	Freight, Demurrage & Defence Class	Freight, Demurrage & Defence Class	War Risks Class	War Risks Class
2004 US$000's	2003 US$000's	2004 US$000's	2003 US$000's	2004 US$000's	2003 US$000's
9,910	8,448	–	–	–	–
379,203	322,270	28,492	23,737	3,989	3,012
389,113	330,718	28,492	23,737	3,989	3,012
112,780	79,116	81	146	–	–
23,298	23,946	951	850	24	–
2,547	2,737	120	88	–	–
2,899	2,296	(1,020)	(763)	(214)	–
28,744	28,979	51	175	(190)	–
2,305	1,849	–	–	–	–
9,681	13,776	334	1,011	44	41
11,986	15,625	334	1,011	44	41
2,775	5,846	213	240	–	–
545,398	460,284	29,171	25,309	3,843	3,053
(30,494)	(51,547)	(3,767)	(1,594)	3,645	2,827
151,804	141,482	12,270	8,426	–	–
121,310	89,935	8,503	6,832	3,645	2,827
405,033	343,045	20,487	18,312	–	–
1,869	1,964	20	72	–	29
10,085	6,696	98	–	187	186
3,691	3,922	–	–	–	–
910	670	–	–	–	–
438	12,294	–	–	–	–
16,993	25,546	118	72	187	215
2,062	1,758	63	93	11	11
545,398	460,284	29,171	25,309	3,843	3,053

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES

Basis of preparation

The combined accounts aggregate the consolidated financial statements of North of England P&I Association Limited ("the Association") and the financial statements of North of England Mutual Insurance Association (Bermuda) Limited ("NoE(Bermuda)"), after the elimination of intercompany transactions and balances. Figures for the Association are extracted from the audited consolidated financial statements as at 20 February 2004, which have been prepared in accordance with UK company law, and which included an unqualified audit report from Deloitte & Touche LLP, Newcastle upon Tyne. Figures for NoE(Bermuda) are extracted from the audited financial statements as at 20 February 2004, which have been prepared in accordance with accounting principles generally accepted in the United Kingdom, and which included an unqualified audit report from Messrs Moore, Stephens & Butterfield, Bermuda.

These are non-statutory accounts and, as such, a cashflow statement, a statement of total recognised gains and losses and certain notes have been excluded.

Prior Year Adjustment

As required by FRS 18 "Accounting Policies", the Association has reviewed its accounting policies to ensure that they remain the most appropriate to its particular circumstances. The Association has changed its accounting policy for the land and buildings owned and occupied by the Association. Under the Association's new accounting policy:

- unrealised gains and losses on foreign exchange translation are included in the Income and Expenditure Account under "Gains / Losses on Exchange", and
- the gains and losses arising on revaluation are included in the Income and Expenditure Account under "Unrealised gains on investments".

As a result of the change in accounting policy, the impact on the current year has been to increase the "Gains on exchange" by US$1,462,000. The comparative figures have been restated as follows:

(a) Income and Expenditure Account:

	Gains on Exchange US$000	Unrealised gains on investments US$000	Surplus for the financial year US$000
20 February 2003 (as previously reported)	9,349	5,543	10,435
Prior year adjustment	746	1,420	2,166
20 February 2003 (as restated)	10,095	6,963	12,601

(b) Balance Sheet:

	Income and Expenditure Account US$000	Revaluation Reserve US$000	Foreign Exchange Reserve US$000
20 February 2003 (as previously reported)	(52,137)	1,823	–
Adoption of new accounting policy at 21 February 2002	(343)	(403)	746
Effect in the year ended 20 February 2003	2,166	(1,420)	(746)
20 February 2003 (as restated)	(50,314)	–	–

Calls and premiums

Calls and premiums, less returns and bad and doubtful debts, are credited to the consolidated income and expenditure account as and when notified to Members.

Reinsurance premiums

Reinsurance premiums, less returns, are debited to the consolidated income and expenditure account in the financial year as and when charged to the Association, together with a provision for the future costs of existing reinsurance policies.

Claims and related expenses

Claims and related expenses, which include the Association's share of other clubs' pool claims, are charged to the combined income and expenditure account on an incurred basis.

Full provision is made for outstanding claims which are based upon the Association's best estimate of the ultimate likely cost of individual claims notified but not paid at the balance sheet date. Provision is also made for claims incurred but not reported (IBNRs) based on statistical methods. Both the individual estimates and the IBNR methodology are reviewed on a regular basis. Although based on information currently available, the ultimate liability of the claims provisions may, as a result of subsequent information and events, prove to be less than or in excess of the amount provided. Provision for the cost of claims handling is included within the IBNRs.

The same basis is applied for all open and closed policy years.

Reinsurance recoveries

Reinsurance recoveries are accrued to match relevant claims.

Investment income

Investment income is recognised on a receivable basis. Variances in unrealised gains and losses are included in the combined income and expenditure account in the period in which they arise. Investment income is allocated in full to the technical account to reflect the mutual status of the Association.

Pension costs

The regular cost of providing retirement pensions is charged to the consolidated income and expenditure account over the employees' service lives on the basis of a constant percentage of earnings. Variations from regular cost, arising from periodic actuarial valuations, are allocated over the expected remaining service lives of current employees on the basis of a constant percentage of current and estimated future earnings.

Taxation

UK Corporation Tax is provided on relevant investment income.

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 that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a non-discounted basis.

Allocation to policy years and the contingency fund

Calls and premiums net of brokerage costs, reinsurance premiums payable, claims and reinsurance recoveries are allocated to the policy years to which they relate. Investment income, gains and losses on sales of investments and exchange gains and losses are allocated on the basis of cash inflows and outflows to and from the relevant policy year or the contingency fund. Investment and administration expenses are allocated to the policy year in which they arise.

Policy years are kept open for no longer than four years. Any surplus or deficit remaining at the closure of a policy year is transferred to or from the contingency fund.

Allocation of costs across the Classes

Costs that are directly attributable to a class are allocated to that class. Other costs are allocated according to time allocation and premium income.

Revaluation

The freehold property is revalued every three years with the surplus or deficit on book value being transferred to the income and expenditure account.

Foreign exchange

All exchange differences are included in the income and expenditure account.

Investments

All investments are stated in the balance sheet at their mid-market value on the balance sheet date.

The freehold property is stated at current value. Depreciation is not provided on the property as it is the company's policy to maintain the building to its previous standard of performance. Consequently the Directors consider the useful life of the property to be long and the residual value high such that there is no significant annual depreciation charge. The Directors annually review the carrying value of the property for impairment and obtain an independent valuation on a triennial basis.

NOTES TO THE ACCOUNTS

(CONTINUED)

Tangible fixed assets and depreciation

Depreciation is provided on all tangible fixed assets at rates calculated to write down the assets to the estimated residual values over the course of their anticipated working lives.

The rates and bases of depreciation used for assets held in the UK are as follows:

Computer Equipment	20% per annum straight line method.
Motor Vehicles	25% per annum reducing balance method.
Office Equipment and Fittings	20% per annum straight line method.

Fixed assets held in Hong Kong are depreciated at a rate of 20% per annum (previously 50% per annum) using the straight line method.

Fixed assets held in Greece are depreciated at a rate of 20% per annum using the straight line method.

Foreign currencies

Foreign currency assets and liabilities are translated into US Dollars at the rates of exchange ruling at the balance sheet date. Income and expenditure are translated at a monthly average rate of exchange. Exchange differences arising on the retranslation of accounts into US Dollars are included in the income and expenditure account.

The principal rates of exchange ruling at the balance sheet date were as follows:

	2004			2003
United Kingdom	£0.535	=	US$1	(£0.627)
Euro	€0.795	=	US$1	(€0.924)
Japan	YEN108.855	=	US$1	(YEN118.430)

2. GROSS PREMIUMS WRITTEN

	2004 US$000's	2003 US$000's
Gross premiums charged	156,446	147,106
Change in provision for future calls	–	(14,003)
	156,446	133,103

3. REINSURANCE PREMIUMS

	2004 US$000's	2003 US$000's
Market	16,777	14,931
International Group	14,423	8,680
War Risks Group	486	239
	31,686	23,850

4. GROSS CLAIMS PAID

	2004 US$000's	2003 US$000's
Members' claims	84,452	78,691
Newcastle P&I Association reinsurance	–	5,079
Other P&I Clubs' pool claims	9,534	5,773
Claims handling costs	11,886	8,658
	105,872	98,201

5. CHANGE IN THE PROVISION FOR GROSS CLAIMS

	2004 US$000's	2003 US$000's
Members	61,795	52,057
Newcastle P&I Association reinsurance	–	(40,712)
Pooling agreement	2,368	8,979
	64,163	20,324

6. NET OPERATING EXPENSES

	2004 US$000's	2003 US$000's
Brokerage	9,631	8,847
Acquisition costs	4,967	3,645
Administration expenses		
Gross	14,967	12,327
Merger expenses	–	24
Amount recharged to Marine Shipping Mutual Insurance Company Limited	(1,318)	(1,105)
Claims handling costs	(11,886)	(8,658)
	1,763	2,588
Net operating expenses	16,361	15,080

In accordance with Schedule 3 of the International Group Agreement 1999 we are required to disclose the Average Expense Ratio for the Association's P&I business for the five years ended 20 February 2004. The Ratio of 10.0% (2003 – 9.3%) has been calculated in accordance with the Schedule and the guidelines issued by the International Group and is consistent with the relevant Financial Statements.

7. INVESTMENT INCOME

	2004 US$000's	2003 US$000's
Income from listed investments	10,887	11,971
Bank and other interest receivable	165	207
Realised losses	(6,887)	(9,570)
	4,165	2,608

NOTES TO THE ACCOUNTS

(CONTINUED)

8. TAX

	2004 US$000's	2003 US$000's
Corporation tax on investment income at 30% (2003 – 30%)	1,152	642
Adjustment in respect of prior years	–	(16)
Charge for the year	1,152	626

There is no provided or unprovided deferred tax at 20 February 2004 (2003 – nil).

Given the Association's mutual status, taxation is only payable on the UK investment return.

9. OTHER FINANCIAL INVESTMENTS

A policy of holding high quality, low risk marketable investments which provide a spread of currencies and a structured range of maturity dates has been adopted in consultation with merchant bank advisers.

The investments principally consist of listed fixed interest and government securities and equities.

Choice of currency is an important consideration, particularly in the current volatile market conditions and, whilst it is not possible to exactly match assets and liabilities in the various currencies, in order to reduce the effects of currency fluctuations, funds are held in those currencies in which future material settlements are expected to be made.

	2004 US$000's	2003 US$000's
Market Value		
Shares and other variable-yield securities	109,991	65,656
Fixed income securities	277,709	277,039
Unrealised gain / (loss) on forward exchange contracts	215	(255)
Deposits with credit institutions	23,769	6,579
	411,684	349,019
Cost		
Shares and other variable-yield securities	81,993	83,582
Fixed income securities	274,042	265,711
Deposits with credit institutions	23,769	6,579
	379,804	355,872

10. DEBTORS ARISING OUT OF DIRECT INSURANCE OPERATIONS

US$17.112m of mutual premium does not become due for payment until November 2004.

11. CONTINGENCY FUND

Protecting & Indemnity Class

	2004 US$000's	2004 US$000's	2003 US$000's	2003 US$000's
Balance at 20 February 2003		141,482		135,125
The transfer from the Income and Expenditure account comprises:				
Allocation of realised investment gains / losses and income	6,892		7,222	
Surplus / (Deficit) transferred from closed policy years	3,430		(841)	
Merger costs transferred from Income and Expenditure account	–		(24)	
		10,322		6,357
Balance at 20 February 2004		151,804		141,482

The contingency fund was established on 12 October 1983 in order to maintain call stability.

Freight, Demurrage & Defence Class

	2004 US$000's	2004 US$000's	2003 US$000's	2003 US$000's
Balance at 20 February 2003		8,426		5,551
The transfer from the Income and Expenditure account comprises:				
Allocation of realised investment gains / losses and income	2,143		1,082	
Surplus transferred from closed policy years	1,701		1,793	
		3,844		2,875
Balance at 20 February 2004		12,270		8,426

The contingency fund was established on 23 September 1994 in order to maintain call stability.

12. DESIGNATED RESERVES

Given the increases in recent years of pool retentions and the participation of International Group Clubs, by way of coinsurance, in the Group market reinsurance contract, all members of the International Group of P&I Clubs have entered into arrangements (under an agreement dated 20 February 1996) whereby each Club has provided letters of credit in favour of the Bermuda Trust Company. Such letters of credit can only be drawn upon in the event that the Association fails to meet a call upon it in relation to its obligations under the Pooling Agreement. The Association has lodged US$11,883,506 (2003 – US$10,912,593) in relation to its participation in the arrangement.

13. OTHER GUARANTEES

In the normal course of business, the Association has provided letters of credit and guarantees. These are secured by investments lodged with the Association amounting to US$4.1 million (2003 - US$2.5 million).

COMBINED P&I CLASS POLICY YEAR STATEMENT

	Closed Years	2001/ 2002	2002/ 2003	2003/ 2004	Claims Handling Reserve	Contingency Fund	Unrealised Gains and Foreign Exchange	Total
	US$000's	US$000's	US$000's	US$000's	US$000's	US$000's	US$000's	US$000's
Calls								
Advance & Fixed Premium								
Invoiced in Prior Years		73,198	115,342	–	–	–	–	188,540
Invoiced in Current Year		(110)	(278)	137,520	–	–	–	137,132
		73,088	115,064	137,520	–	–	–	325,672
Release & Supplementary		18,994	1,279	370	–	–	–	20,643
		92,082	116,343	137,890	–	–	–	346,315
Reinsurance Premiums		(18,596)	(23,877)	(31,406)	–	–	–	(73,879)
		73,486	92,466	106,484	–	–	–	272,436
Investment income, gains on sales of investments, and exchange movements		2,900	3,769	1,611	–	81,379	34,067	123,726
Transfers		–	–	–	–	73,490	–	73,490
		76,386	96,235	108,095	–	154,869	34,067	469,652
Members' & Pool Claims		(36,626)	(43,227)	(22,251)	–	–	–	(102,104)
Expenses & Tax		(11,672)	(13,972)	(16,698)	–	(3,065)	–	(45,407)
Surplus Available on Closed Years	91,422	–	–	–	–	–	–	91,422
Balances Available for Outstanding Claims	91,422	28,088	39,036	69,146	–	151,804	34,067	413,563
Outstanding Claims	(121,779)	(29,124)	(77,543)	(138,401)	(11,000)	–	–	(377,847)
Reinsurance Recoveries	30,357	1,165	18,223	35,849	–	–	–	85,594
	(91,422)	(27,959)	(59,320)	(102,552)	(11,000)	–	–	(292,253)
Surplus / (Deficit) at 20 February 2004	**–**	**129**	**(20,284)**	**(33,406)**	**(11,000)**	**151,804**	**34,067**	**121,310**
Surplus / (Deficit) at 20 February 2003	(10,190)	(8,894)	(18,303)	–	(8,000)	141,482	(6,160)	89,935

NOTES TO THE COMBINED P&I CLASS POLICY YEAR STATEMENT

1. The Combined P&I Class Policy Year Statement ("the Statement") is based on the combined policy year results of the Association and NoE(Bermuda) ("the Companies"). The Statement aggregates the policy year statements of the Companies and eliminates the effect of the reinsurance transaction by which the Association reinsures 90% of its P&I risks and accumulated outstanding claims with NoE(Bermuda). The Companies have accounted for the reinsurance transaction in their respective accounts for the period ended 20 February 2004.
2. Investment income, gains and losses on sales of investments and exchange movements are allocated to policy years and the Contingency Fund on the basis of cash inflows and outflows to and from the relevant policy year / Contingency Fund. Unrealised gains are not allocated to policy years until such time as gains and losses are realised. The foreign exchange gain on the freehold building is included in unrealised gains and foreign exchange.
3. Calls are net of brokerage.
4. Supplementary call forecasts are as per the Directors' Report.
5. Expenses and tax charged to open policy years are as follows:

	2001/2002 US$000's	2002/2003 US$000's	2003/2004 US$000's
General and administrative expenses	10,634	12,123	14,224
Merger costs transferred to Contingency Fund	(193)	(24)	-
Investment expenses	1,231	1,361	1,398
Taxation	-	512	1,076
	11,672	13,972	16,698

6. Estimated outstanding claims are net of expected reinsurance recoveries from the International Group of P&I Clubs, as reported at 20 February 2004 with the addition of appropriate amounts in each policy year for incurred but not reported (IBNR) claims.
7. A deficit on any open policy year will be funded by expected future investment income and, if necessary, a transfer from the Contingency Fund or by making supplementary calls.
8. Future investment income has not been included in the statement and claims have not been discounted.
9. Transfers are made from the Contingency Fund to meet exceptional items and to maintain call stability. The surplus on closed years has been transferred to the Contingency Fund.
10. The approximate yield of a 10% supplementary call on the open policy years is:

2001/02	US$6.1 million
2002/03	US$10.1 million
2003/04	US$12.4 million

COMBINED FD&D CLASS POLICY YEAR STATEMENT

	Closed Years US$000's	2001/ 2002 US$000's	2002/ 2003 US$000's	2003/ 2004 US$000's	Claims Handling Reserve US$000's	Contingency Fund US$000's	Unrealised Gains US$000's	Total US$000's
Calls								
Advance & Fixed Premium								
Invoiced in Prior Years		7,361	8,019	–	–	–	–	15,380
Invoiced in Current Year		(20)	(33)	8,496	–	–	–	8,443
		7,341	7,986	8,496	–	–	–	23,823
Release & Supplementary		164	106	21	–	–	–	291
		7,505	8,092	8,517	–	–	–	24,114
Reinsurance Premiums		(518)	(503)	(578)	–	–	–	(1,599)
		6,987	7,589	7,939	–	–	–	22,515
Investment income, gains on sales of investments, and exchange movements		1,088	822	219	–	5,167	39	7,335
Transfers		–	–	–	–	7,103	–	7,103
		8,075	8,411	8,158	–	12,270	39	36,953
Claims		(1,438)	(1,004)	(494)	–	–	–	(2,936)
Expenses & Tax		(2,355)	(2,860)	(4,399)	–	–	–	(9,614)
Surplus Available on Closed Years	4,506	–	–	–	–	–	–	4,506
Balances Available for Outstanding Claims	4,506	4,282	4,547	3,265	–	12,270	39	28,909
Outstanding Claims	(4,587)	(1,824)	(3,704)	(5,372)	(5,000)	–	–	(20,487)
Reinsurance Recoveries	81	–	–	–	–	–	–	81
	(4,506)	(1,824)	(3,704)	(5,372)	(5,000)	–	–	(20,406)
Surplus / (Deficit) at 20 February 2004	**–**	**2,458**	**843**	**(2,107)**	**(5,000)**	**12,270**	**39**	**8,503**
Surplus / (Deficit) at 20 February 2003	759	1,008	(409)	–	(4,000)	8,426	1,048	6,832

NOTES TO THE COMBINED FD&D CLASS POLICY YEAR STATEMENT

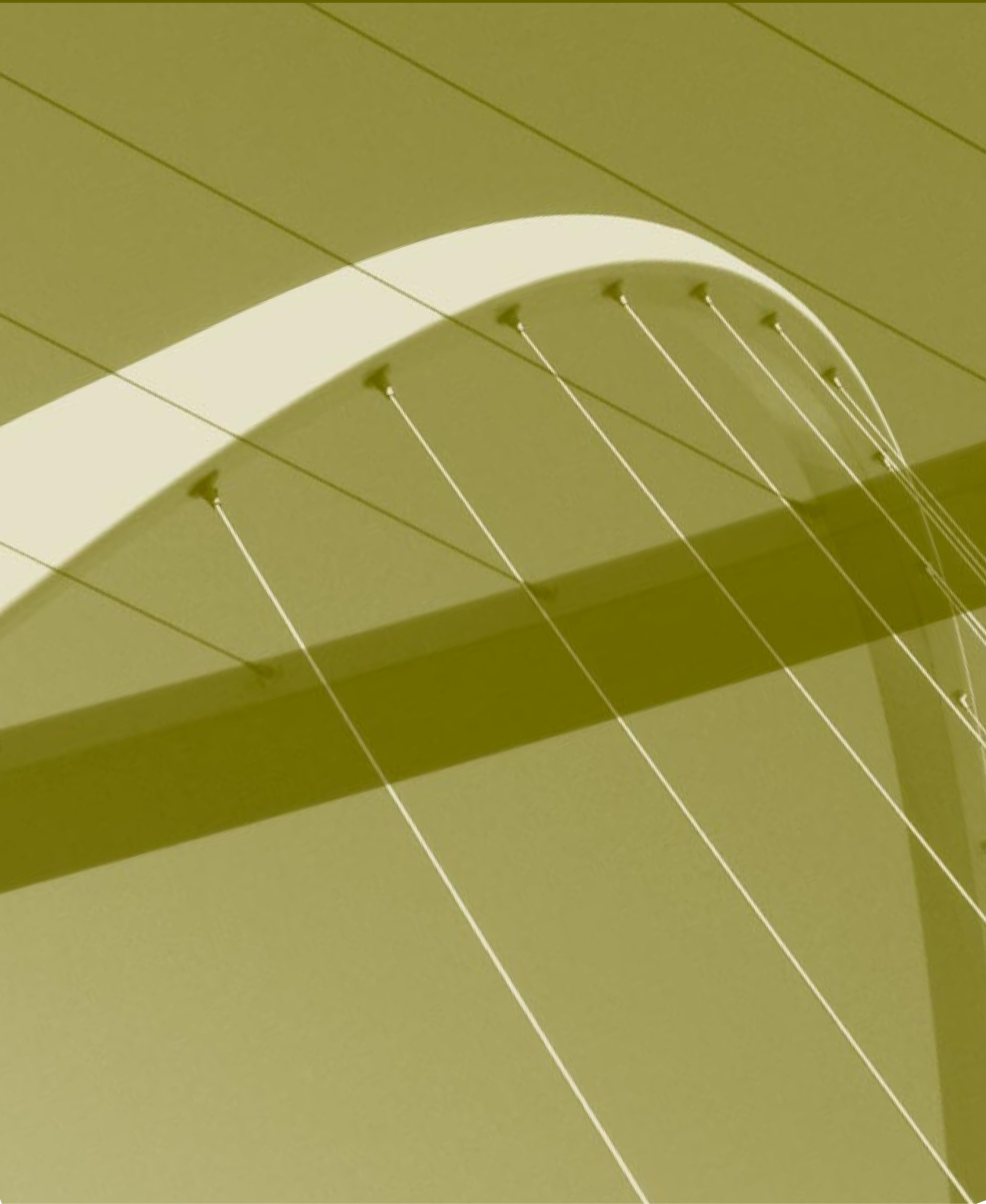
1. The Combined FD&D Class Policy Year Statement ("the Statement") is based on the combined policy year results of the Association and NoE(Bermuda) ("the Companies"). The Statement aggregates the policy year statements of the Companies and eliminates the effect of the reinsurance transaction by which the Association reinsures 90% of its FD&D risks and accumulated outstanding claims with NoE(Bermuda). The Companies have accounted for the reinsurance transaction in their respective accounts for the period ended 20 February 2004.
2. Investment income, gains and losses on sales of investments and exchange movements are allocated to policy years and the Contingency Fund on the basis of the average balance available for outstanding claims of the relevant policy year / Contingency Fund. Unrealised gains are not allocated to policy years until such time as gains and losses are realised.
3. Calls are net of brokerage.
4. Supplementary call forecasts are as per the Directors' Report.
5. Expenses and tax charged to open policy years are as follows:

	2001/2002 US$000's	2002/2003 US$000's	2003/2004 US$000's
General and administrative expenses	2,296	2,652	4,239
Investment expenses	59	89	106
Taxation	-	119	54
	2,355	2,860	4,399

6. Estimated outstanding claims include appropriate amounts in each policy year for incurred but not reported (IBNR) claims.
7. A deficit on any open policy year will be funded by expected future investment income and, if necessary, a transfer from the Contingency Fund or by making supplementary calls.
8. Future investment income has not been included in the statement and claims have not been discounted.
9. Transfers are made from the Contingency Fund to meet exceptional items and to maintain call stability. The surplus on closed years has been transferred to the Contingency Fund.
10. The approximate yield of a 10% supplementary call on the open policy years is:

2001/02	US$0.5 million
2002/03	US$0.6 million
2003/04	US$0.6 million

NOTES



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