# ATTACHMENT E

## Best's Key Ratings of
## American Guarantee and Liability Insurance Company

## Best's Rating and Report Updates for American Guarantee and Liability Ins Co

**Best's Rating of A (Excellent)**
**Financial Size Category of XV ($2 billion or more)**

**Rating Category (Excellent):** Assigned to companies that have, in our opinion, an excellent ability to meet their ongoing obligations to policyholders. The **Financial Size Category** is assigned to all companies and reflects their size based on their capital, surplus and conditional reserve funds in millions of U.S. dollars.

The objective of **Best's rating system** is to provide an opinion of an insurer's financial strength and ability to meet ongoing obligations to policyholders. Our opinions are derived from the evaluation of a company's balance sheet strength, operating performance and business profile as compared to Best's quantitative and qualitative standards.View our **Best's Rating System and Procedures** for more information.

While Best's Ratings reflect our **opinion** of a company's financial strength and ability to meet its ongoing obligations to policyholders, they are **not a warranty**, nor are they a recommendation of a specific policy form, contract, rate or claim practice. View our **entire notice** for complete details.

***Note:** The above information reflects the most recent Best's Rating for this company, which may have been released subsequent to the creation of the following Best's Company Report.

**Best's Company Reports** provide detailed business overview, extensive financial data and analytical commentary, product and geographic information, company history, as well as the rationale supporting the financial strength rating assigned by A.M. Best. These reports are updated on a regular basis based on input and analysis performed throughout the year.

**Best Company Report Revision Date - 07/22/2005 ***

The **Report Revision Date *** represents the last significant material change made to this report. Other non-material changes may have been made to this report subsequent to this date, but are not reflected in the report revision date. The Best Company Report below was created based on the following dates.

| Rating and Commentary [1] | Financial [2] | General Information [3] |
|---|---|---|
| **Best's Rating: 09/14/2004** | **Time Period: 1st Quarter - 2005** | **Corporate Structure: N/A** |
| **Rating Rationale: 09/14/2004** | **Last Updated: 07/20/2005** | **States Licensed: 11/14/2001** |
| **Report Commentary : 07/22/2005** | **Status: Quality Cross Checked** | **Officers and Directors: 04/07/2005** |

***Note:** The **Rating and Commentary** [1]date outlines the most recent updates to the Company's Rating, Rationale,and Report Commentary for key rating and business changes. Report commentary may include significant changes to Business Review, Financial Performance/Earnings, Capitalization, Investment/Liquidity, or Reinsurance sections of the report. The **Financial** [2] date reflects the current status of the financial tables found within the body of the Company Report, including whether the data has was loaded as received or had been run through our quality control cross-check process. The **General Information** [3]date covers key areas that may have changed such as corpororate structure, states licensed or officers and directors.

## Best's Company Report for American Guarantee and Liability Ins Co

**Group Affiliation: Zurich Financial Services Group**

# AMERICAN GUARANTEE AND LIABILITY INSURANCE

# COMPANY

**New York, New York, United States**
**1400 American Lane, Schaumburg, Illinois, United States 60196-1056**
**Web: http://www.zurichna.com/**

**Tel:** 847-605-6000 **Fax:** 847-605-6011
**AMB#:** 02562 **NAIC#:** 26247
**FEIN#:** 36-6071400

Report Revision Date: 07/22/2005

# BEST'S RATING

Based on our opinion of the consolidated Financial Strength of the property/casualty members of Zurich Financial Services Group, which operate under a group structure, each group member is assigned a Best's Rating of A (Excellent). The company is assigned the Financial Size Category of Class XV, which is the Financial Size Category of the group.

# RATING RATIONALE

The following text is derived from the report of Zurich Financial Services Group.

**Rating Rationale:** The rating of Zurich Financial Services Group (ZFS) reflects the company's overall improvement in operating performance, excellent business position in selected core markets (Switzerland, Germany, Italy, Spain, United Kingdom and North America), despite slower growth, and excellent consolidated risk-based capitalisation. The main offsetting factor continues to be the potential for further reserve strengthening and the continuing reliance on the management fee income from the Farmers P&C Group towards overall ZFS earnings. The stable outlook reflects A.M. Best's opinion that future non-life earnings, at this stage in the underwriting cycle, are unlikely to be supportive of a higher rating level.

Improving operating performance -- In line with A.M. Best's expectations, earnings improved in the first half of 2004 to USD 1.4 billion from USD 0.8 billion in the first half of 2003. ZFS's strict implementation of its aggressive global profit and risk-based capital improvement programmes focused on reducing costs and enhancing efficiency (underwriting and claims management) and by disposing of non-core subsidiaries that did not meet ZFS's profitability targets. The effect of the profit improvement programme is likely to continue to be reflected in 2004 and 2005, allowing ZFS to improve on the 2003 operating consolidated return on equity (ROE) of 12%. Reported half-year consolidated combined ratio fell by 2.1 percentage points to 96.7%, and it is likely to be maintained at year-end 2004 as ZFS continues to benefit from disciplined underwriting and its focus on operational efficiency. Increased frequency and severity from catastrophe losses could, however, negatively impact 2004 earnings.

Excellent business position -- ZFS has a leading profile as a general insurer in its selected core markets (Switzerland, Germany, Italy, Spain, United Kingdom and North America). Due to some softening of premium rates, A.M. Best expects modest consolidated non-life premium growth in 2004 and 2005 following strong growth in 2003 (22%). Consolidated life premium is likely to decrease by 5%-10% in 2004 as ZFS has reduced its exposure to underperforming life business.

Excellent consolidated risk-based capitalisation -- A.M. Best expects retained earnings to further improve ZFS's level of risk-adjusted capitalisation, despite rising interest rates that are likely to negatively affect the prospects for unrealised gains at the level achieved during 2003. Capitalisation improved during 2003, although net income was impacted by reserve strengthening of approximately USD 1.9 billion, of which USD 0.8 billion related North America Corporate and USD 0.7 billion related to Bermuda-based Centre Solutions Ltd. A.M. Best remains concerned about potential for further reserve strengthening.

**Best's Rating: A g** **Outlook: Stable**

# FIVE YEAR RATING HISTORY

| Date | Best's Rating |
|---|---|
| 09/14/04 | A g |
| 06/10/04 | A g |
| 09/03/03 | A g |
| 05/30/03 | A g |
| 12/18/02 | A g |
| 09/06/02 | A gu |
| 03/22/02 | A+ g |
| 09/27/01 | A+ gu |
| 11/17/00 | A+ g |

# KEY FINANCIAL INDICATORS

| | Statutory Data ($000) | | |
|---|---|---|---|
| Period Ending | Direct Premiums Written | Net Premiums Written | Pretax Operating Income |
| 2000 | 447,902 | ... | 7,802 |
| 2001 | 724,331 | ... | 8,262 |
| 2002 | 1,008,748 | ... | 7,913 |
| 2003 | 1,231,899 | ... | 3,785 |
| 2004 | 1,312,783 | ... | 4,306 |
| | | | |
| 03/2004 | 293,388 | ... | 851 |
| 03/2005 | 292,452 | ... | 1,253 |

| | Statutory Data ($000) | | |
|---|---|---|---|
| Period Ending | Net Income | Total Admitted Assets | Policy-holders' Surplus |
| 2000 | 7,881 | 146,532 | 146,399 |
| 2001 | 7,125 | 151,153 | 150,655 |
| 2002 | 11,751 | 88,403 | 87,662 |
| 2003 | 4,984 | 93,987 | 93,729 |
| 2004 | 4,570 | 213,770 | 128,140 |

| | | | |
|---|---|---|---|
| 03/2004 | 839 | 94,926 | 94,568 |
| 03/2005 | 1,353 | 337,687 | 129,896 |

| | Profitability | | | Leverage | | | Liquidity | |
|---|---|---|---|---|---|---|---|---|
| Period Ending | Comb. Ratio | Inv. Yield (%) | Pretax ROR (%) | NA Inv Lev | NPW to PHS | Net Lev | Overall Liq (%) | Oper. Cash-flow (%) |
| 2000 | ... | 5.3 | ... | 4.5 | ... | 0.0 | 999.9 | 732.8 |
| 2001 | ... | 5.5 | ... | 3.5 | ... | 0.0 | 999.9 | ... |
| 2002 | ... | 6.9 | ... | 6.9 | ... | 0.0 | 999.9 | ... |
| 2003 | ... | 4.3 | ... | 6.7 | ... | 0.0 | 999.9 | ... |
| 2004 | ... | 3.9 | ... | 5.3 | ... | 0.7 | 249.6 | 152.9 |
| 5-Yr Avg | ... | 5.2 | 0.0 | ... | ... | ... | ... | ... |
| 03/2004 | ... | XX | ... | XX | ... | ... | 999.9 | ... |
| 03/2005 | ... | XX | ... | XX | ... | 1.6 | 162.5 | -99.9 |

(*) Data reflected within all tables of this report has been compiled from the company-filed statutory statement. Within several financial tables of this report, this company is compared against the Commercial Casualty Composite.

# BUSINESS REVIEW

The following text is derived from the report of Zurich U.S.

Zurich U.S. is the U.S.-based insurance operation of Zurich Financial Services Group ("ZFS"), Switzerland. ZFS offers a full array of property / casualty, life insurance, reinsurance and asset management services principally in the U.S., UK and Switzerland. The consolidated operations of Zurich U.S. contribute approximately 50% of the worldwide property / casualty premiums of ZFS and are integral to their international insurance strategy.

Overall, Zurich U.S. operations include eighteen insurance subsidiaries, including Universal Underwriters INs. Co. and its wholly owned subsidiary, Universal Underwriters Ins. Co. of Texas (both of which are slated for sale later in 2005), that provide a complete array of property / casualty products. Property / casualty products are offered by sixteen companies through a network of agents and brokers, memberships in underwriting associations and syndicates. Property / casualty underwriting activities target the writing of standard commercial, specialty commercial, fidelity and surety business. Zurich U.S. ranks among the top 20 largest U.S. property / casualty insurance groups, with $7.2 billion in net premiums supported by $4.9 billion in surplus at year-end 2004.

At December 31, 2004, the property / casualty operations of Zurich U.S. primarily consist of an eighteen-member pool led by Zurich American Insurance Company. Under the pooling agreement, each member's transactions included in income or loss resulting from underwriting operations as well as related asset and liability accounts are distributed 100% to Zurich American Insurance Company and 0% to the other pool members. The remaining seventeen pool members consist of: American Guarantee & Liability Insurance Company; American Zurich Insurance Company; Assurance Company of America; Colonial American Casualty and Surety; Maine Bonding and Casualty Company; Maryland Casualty Company; Maryland Insurance Company; National Standard Insurance Company; Northern Insurance Company of New York; Valiant Insurance Company;

Steadfast Insurance Company; Empire Fire and Marine Insurance Company; Empire Indemnity Insurance Company; Zurich American Insurance Company of Illinois; Fidelity & Deposit Company of Maryland, Universal Underwriters Insurance Company and Universal Underwriters of Texas Insurance Company. A former affiliate, Mountbatten Surety Company, was sold during the first quarter of 2003. Another affiliate, Maryland Lloyds Insurance Company, was dissolved in late 2004.

Central to Zurich U.S.'s business strategy are its customer-focused business units (BUs), including a dedicated service business unit. The customer-focused BUs operate through independent agents and brokers that have access to Zurich's products and services through a nationwide network of seven regional offices and 63 branch offices. The BUs include: Corporate Customer, Middle Markets, Small Business, Specialties, Construction, Global Energy, Surety and Financial Enterprises, Empire, and Universal. The service BU unifies the Zurich U.S. approach to managing claims, managed care, risk engineering, information technology and marketing and provides support to all its commercial business units.

Corporate Customer serves large corporate and commercial businesses with global and domestic solutions in three major areas: property, casualty, and group captives.

Middle Markets offers package solutions and program solutions to meet the needs of the medium-sized commercial enterprise. Target segments include manufacturing, services (including hospitality) and public entities. Middle Markets also offers programs for groups and associations and provides a full array of financial institution bonds, professional liability and property-casualty solutions.

Small Business provides a comprehensive, customized coverage portfolio of property, liability, commercial auto, umbrella and, in some locations, workers compensation. It provides solutions for small businesses in the retail, wholesale, service, office, institutional, and manufacturing fields.

Specialties offers coverages for emerging, potentially volatile and unique third-party liability exposures. These include the professional liability risks of group services providers such as architects and engineers, healthcare organizations, financial institutions, environmental contractors, and information technology firms, along with a wide range of specialty liability coverages, such as management, environmental, excess and umbrella, products, volatile general and political risk insurance and accident and health, specialty health and disability programs. Liability solutions are also provided for the healthcare, environmental, financial and rail industries.

Construction specializes in providing product, service and risk financing solutions for project owners, construction managers, contractors and subcontractors. In addition to all standard property-casualty coverages, this industry-focused business unit also provides a number of specialized products, including surety business. Surety serves the needs of construction project owners, construction contractors and subcontractors and governmental entities, non-profit organizations and commercial enterprises in most industries with a wide array of contract, commercial and environmental surety bond products.

Global Energy specializes in providing comprehensive risk solutions, risk engineering services and claims support tailored to the individual needs of oil and gas, petrochemical, natural resources, mining and power generation customers worldwide. The unit also provides a full range of marine products and services in the United States and London, including ocean cargo protection, hull, liabilities and other marine-related solutions.

Empire Fire and Marine provides specialized insurance and financial solutions to small and midsized commercial markets, distributing its products to auto rental, independent auto dealer, recreational vehicle and contractors' equipment businesses. Its nationwide network of managing general agents target markets such as long-haul trucking, ambulance and tow truck companies as well as general liability classes including tanning salons and security guard companies.

Zurich U.S. also includes the operations of Universal Underwriters Insurance Group, ("UUIG"). Universal became a member of the pool as of January 1, 2002. Universal Underwriters Group specializes in providing insurance and financial services to franchised auto, truck, equipment and motorcycle dealerships and automotive-related businesses. Universal offers a wide range of commercial insurance-related products and services including property-casualty insurance, workers compensation, risk management services, business life insurance, vehicle service contracts, credit life and disability insurance, GAP insurance, sub prime financing services and income development programs. As mentioned above, this group is expected to be sold to an outside investor group later in 2005.

**Affiliations:** American Insurance Association, Insurance Services Office, National Council on Compensation Insurance and Surety Association of America.

### 2004 BUSINESS PRODUCTION AND PROFITABILITY ($000)

| Product Line | Premiums Written Direct | Premiums Written Net | % of Total NPW | Pure Loss Ratio | Loss & LAE Reserves |
|---|---|---|---|---|---|
| Comm'l Auto Liab | 53,020 | ... | ... | ... | ... |
| Prod Liab Occur | 140,402 | ... | ... | ... | ... |
| Oth Liab Cl-Made | 149,212 | ... | ... | ... | ... |
| Oth Liab Occur | 533,020 | ... | ... | ... | ... |
| Workers' Comp | 104,708 | ... | ... | ... | ... |
| Com'l MultiPeril | 34,301 | ... | ... | ... | ... |
| Allied Lines | 121,187 | ... | ... | ... | ... |
| Fire | 115,842 | ... | ... | ... | ... |
| All Other | 61,091 | ... | ... | ... | ... |
| Totals | 1,312,783 | ... | ... | ... | ... |

**Major 2004 Direct Premium Writings By State ($000):** California, $ 157,760 (12.0%); Texas, $ 137,499 (10.5%); New York, $ 95,046 (7.2%); New Jersey, $ 83,406 (6.4%); Connecticut, $ 75,548 (5.8%); Florida, $ 74,949 (5.7%); 45 other jurisdictions, $ 685,407 (52.2%); Aggregate Alien, $ 3,167 (0.2%).

# FINANCIAL PERFORMANCE

The following text is derived from the report of Zurich U.S.

Operating performance has generated subpar returns on both revenue and surplus, on both a five-year and ten-year basis. The poor results have been due to adverse loss reserve development, subpar underwriting returns and, during the 2000 - 2002 period, realized and unrealized capital losses on the group's equity investments. Benefiting from significantly improved market conditions since late 2000, the group has implemented strong rate increases, tighter underwriting controls and standards, and significant cost savings initiatives. Furthermore, Zurich U.S. benefited during 2003 from a strong equity market which allowed the group to record nearly $360 million in capital gains, nearly two-thirds of which represented unrealized capital appreciation. Net investment earnings on Zurich's sizable fixed-income portfolio continued to lag behind underwriting and "other" losses over the past five years. Like its commercial casualty peers, investment yields have eroded over the years due to the low interest rate environment in conjunction with an abbreviated duration on the investment portfolio.

Underwriting results, although in line with peers, have been hampered by a series of significant reserve strengthening actions, elevated catastrophe losses and prolonged competitive market conditions in the Zurich US targeted business classes. Sizable reserve additions for prior year losses were recorded in each of the past four calendar years, including more than $2.0 billion in 2004, nearly $1.0 billion in 2003, approximately $725 million in 2002 and close to $400 million in 2001. The recent reserve development was primarily impacted by the general liability line while the 2003 development came from its workers' compensation, other liability, and medical malpractice lines. The 2002 reserving action was concentrated on the medical malpractice, commercial multiple peril, auto liability and other liability lines. In addition, underwriting results in 2004 were negatively impacted by four hurricanes which hit the Southeast coast of the United States during the third quarter. In 2001, Zurich U.S. realized approximately $130 million of net losses attributable to the September 11th terrorist attacks, primarily in property lines. To date, there has been $138.1 million of net losses and LAE incurred as a result of the attacks. Historically, the group's underwriting results were also impacted by a higher expense base. In response, Zurich U.S. management implemented a formal expense reduction program including "shared services" among business units resulting in operational restructuring and reduced headcount. Although the group incurred a restructuring charge at the time, significant expense savings are being realized annually resulting in a substantial downward trend in underwriting expenses. Partially as a result of these initiatives as well as the strong growth in net premium volume, primarily due to rate increases, the group's expense ratio has improved considerably in recent years and is now several points better than its industry peers.

Going forward the group's exposure to adverse loss development from prior accident years relating to casualty classes of business may continue to be an earnings drag on Zurich U.S.'s operating results. As a result, and partially due to softening market conditions, A.M. Best does not anticipate strong underwriting results in the medium term; notwithstanding improved accident year earnings in more recent accident years.

## PROFITABILITY ANALYSIS

| | Company | | | | Industry Composite | | | |
|---|---|---|---|---|---|---|---|---|
| Period Ending | Pretax ROR (%) | Return on PHS(%) | Comb. Ratio | Oper. Ratio | Pretax ROR (%) | Return on PHS(%) | Comb. Ratio | Oper. Ratio |
| 2000 | ... | 5.5 | ... | ... | 8.0 | 2.4 | 109.6 | 91.6 |
| 2001 | ... | 2.8 | ... | ... | -4.1 | -6.3 | 118.7 | 104.1 |
| 2002 | ... | 10.7 | ... | ... | 1.8 | -4.2 | 108.4 | 95.9 |
| 2003 | ... | 6.0 | ... | ... | 5.1 | 12.8 | 104.2 | 92.2 |
| 2004 | ... | 4.8 | ... | ... | 7.7 | 13.0 | 102.2 | 91.0 |
| 5-Yr Avg | 0.0 | 5.8 | ... | ... | 3.9 | 4.1 | 107.9 | 94.6 |
| 03/2004 | ... | XX | ... | ... | XX | XX | XX | XX |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 03/2005 | ... | XX | ... | ... | XX | XX | XX | XX |

## UNDERWRITING EXPERIENCE

| Year | Net Undrw Income ($000) | Loss Ratios Pure Loss | LAE | Loss & LAE | Expense Ratios Net Comm | Other Exp. | Total Exp. | Div. Pol. | Comb Ratio |
|---|---|---|---|---|---|---|---|---|---|
| 2000 | 452 | ... | ... | ... | ... | ... | ... | ... | ... |
| 2001 | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| 2002 | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| 2003 | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| 2004 | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| 5-Yr Avg | ... | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | ... |
| 03/2004 | ... | ... | ... | ... | XX | XX | ... | ... | ... |
| 03/2005 | ... | ... | ... | ... | XX | XX | ... | ... | ... |

## INVESTMENT INCOME ANALYSIS ($000)

| Year | Company Net Inv Income | Company Realized Capital Gains | Unrealized Capital Gains |
|---|---|---|---|
| 2000 | 7,350 | 55 | ... |
| 2001 | 7,884 | -1,058 | -2,900 |
| 2002 | 7,913 | 3,838 | 996 |
| 2003 | 3,785 | 1,280 | 436 |
| 2004 | 4,306 | 277 | 788 |
| 03/2004 | 851 | 90 | ... |
| 03/2005 | 1,253 | -40 | 403 |

| Year | Company Inv Inc Growth (%) | Company Inv Yield (%) | Company Total Return (%) | Industry Composite Inv Inc Growth (%) | Industry Composite Inv Yield (%) |
|---|---|---|---|---|---|
| 2000 | -41.2 | 5.3 | 5.3 | 7.7 | 6.0 |
| 2001 | 7.3 | 5.5 | 2.7 | -14.1 | 5.3 |
| 2002 | 0.4 | 6.9 | 11.3 | -0.1 | 5.1 |
| 2003 | -52.2 | 4.3 | 6.3 | 6.0 | 4.9 |
| 2004 | 13.8 | 3.9 | 4.9 | 1.5 | 4.4 |
| 5-Yr Avg | -65.5 | 5.2 | 5.9 | -0.5 | 5.1 |
| 03/2004 | XX | XX | 1.0 | XX | XX |
| 03/2005 | XX | XX | 1.3 | XX | XX |

## INVESTMENT PORTFOLIO ANALYSIS

| Asset Class | 2004 Inv Assets ($000) | % of Invested Assets 2004 | 2003 | Annual % Chg |
|---|---|---|---|---|
| Long-Term bonds | 121,468 | 94.0 | 89.2 | 46.2 |
| Affiliated Investments | 1 | 0.0 | 0.0 | ... |
| Other Inv Assets | 7,808 | 6.0 | 10.8 | -22.4 |
| Total | 129,278 | 100.0 | 100.0 | 38.8 |

## 2004 BOND PORTFOLIO ANALYSIS

| Asset Class | % of Total Bonds | Mkt Val to Stmt Val(%) | Avg. Maturity (Yrs) | Class 1 - 2 (%) | Class 3 - 6 (%) | Struc. Secur. (%) | Struc. Secur. (% of PHS) |
|---|---|---|---|---|---|---|---|
| Governments | 53.7 | 1.5 | 5.4 | 100.0 | ... | ... | ... |
| States, terr & poss | 22.9 | 1.8 | 4.6 | 100.0 | ... | 15.7 | 3.4 |
| Corporates | 23.4 | 1.1 | 5.2 | 100.0 | ... | 52.6 | 11.7 |
| Total all bonds | 100.0 | 1.5 | 5.2 | 100.0 | ... | 15.9 | 15.1 |

# CAPITALIZATION

The following text is derived from the report of Zurich U.S.

Given the U.S. operations strategic importance to Zurich Financial Services Group, as explicitly and consistently demonstrated over the years through reinsurance support and capital contributions totaling $3.5 billion since 2001, the U.S. group's current and prospective level of capitalization, on a risk adjusted basis as measured by Best's Capital Adequacy Ratio, is adequate. The group's capitalization reflects the continued substantial capital support provided through surplus notes issued to the U.S. group's parent company as well as sizable reinsurance arrangements with the parent. Nevertheless, Zurich U.S.'s stand-alone capitalization is negatively impacted by elevated (albeit improved) underwriting leverage and significant levels of reinsurance dependence compared to industry peers. Surplus notes totaling $2.0 billion were issued to the group's parent and affiliated companies over the past two years as well as a cash capital contribution of $1.3 billion from the parent company in 2004. Relative to its rating level, the financial leverage of surplus notes is high at 41% of total capital and surplus. While a portion of the notes are generally payable over three to four year terms, beginning with a $453 million note due in 2006, the majority of the notes are held in perpetuity. Repayment terms are generally flexible and require prior approval by state insurance regulators. Reinsurance dependence is somewhat tempered as approximately 30% of the group's recoverables are with Zurich Financial Services affiliates.

Following a sizable decline in reported capital between 1999 and 2001 (mostly during 2000), the group's surplus position has improved in more recent years, principally due to the cessation of shareholder dividends after 2000 and capital support provided by the parent in each of the past four years. A particularly strong 40% gain to surplus in 2003 was due to improved earnings and a capital contribution of $350 million. Surplus growth of 34% during 2004 was solely due to the $2.26 billion contribution made at year-end that more than offset the $1.0 billion operating loss. A.M. Best believes that capitalization will remain supportive of the current rating level, however, it is subject to further uncertainty as unfavorable reserve development trends have severely impeded internal surplus growth.

## CAPITAL GENERATION ANALYSIS ($000)

| | Source of Surplus Growth | | |
|---|---|---|---|
| Year | Pretax Operating Income | Total Inv. Gains | Net Contrib. Capital |
| 2000 | 7,802 | 55 | ... |
| 2001 | 8,262 | -3,958 | ... |
| 2002 | 7,913 | 4,835 | -74,998 |
| 2003 | 3,785 | 1,717 | ... |
| 2004 | 4,306 | 1,065 | 30,000 |
| 5-Yr Total | 32,069 | 3,713 | -44,998 |
| 03/2004 | 851 | 90 | ... |
| 03/2005 | 1,253 | 363 | ... |

| | Source of Surplus Growth | | |
|---|---|---|---|
| Year | Other, Net of Tax | Change in PHS | PHS Growth (%) |
| 2000 | 24 | 7,881 | 5.7 |
| 2001 | -49 | 4,256 | 2.9 |
| 2002 | -743 | -62,993 | -41.8 |
| 2003 | 565 | 6,067 | 6.9 |
| 2004 | -961 | 34,411 | 36.7 |
| 5-Yr Total | -1,163 | -10,379 | ... |
| 03/2004 | -101 | 839 | 0.9 |
| 03/2005 | 140 | 1,756 | 1.4 |

## QUALITY OF SURPLUS ($000)

| | | % of PHS | | | Dividend Requirements | | |
|---|---|---|---|---|---|---|---|
| Year | Year-End PHS | Cap Stk/ Contrib. Cap. | Other | Un-assigned Surplus | Stock-holder Divs | Div to POI (%) | Div to Net Inc. (%) |
| 2000 | 146,399 | 151.8 | ... | -51.8 | ... | ... | ... |
| 2001 | 150,655 | 147.5 | ... | -47.5 | ... | ... | ... |
| 2002 | 87,662 | 168.0 | ... | -68.0 | ... | ... | ... |
| 2003 | 93,729 | 157.1 | ... | -57.1 | ... | ... | ... |
| 2004 | 128,140 | 138.3 | ... | -38.3 | ... | ... | ... |
| 03/2004 | 94,568 | 155.7 | ... | -55.7 | ... | ... | ... |
| 03/2005 | 129,896 | 136.5 | ... | -36.5 | ... | ... | ... |

## LEVERAGE ANALYSIS

| | Company | | | | Industry Composite | | | |
|---|---|---|---|---|---|---|---|---|
| Year | NPW to PHS | Reserves to PHS | Net Lev | Gross Lev | NPW to PHS | Reserves to PHS | Net Lev | Gross Lev |
| 2000 | ... | ... | 0.0 | 5.9 | 1.0 | 1.7 | 3.5 | 4.9 |
| 2001 | ... | ... | 0.0 | 5.9 | 1.2 | 1.9 | 4.2 | 5.9 |
| 2002 | ... | ... | 0.0 | 9.7 | 1.4 | 2.0 | 4.6 | 6.6 |
| 2003 | ... | ... | 0.0 | 10.3 | 1.3 | 1.9 | 4.3 | 6.1 |
| 2004 | ... | ... | 0.7 | 9.4 | 1.2 | 1.8 | 4.0 | 5.5 |
| | | | | | | | | |
| 03/2004 | ... | ... | ... | XX | XX | XX | XX | XX |
| 03/2005 | ... | ... | 1.6 | XX | XX | XX | XX | XX |

Current BCAR: 144.5

## PREMIUM COMPOSITION & GROWTH ANALYSIS

| Period | DPW | | GPW | |
|---|---|---|---|---|
| Ending | ($000) | (% Chg) | ($000) | (% Chg) |
| 2000 | 447,902 | 6.9 | 501,012 | 3.3 |
| 2001 | 724,331 | 61.7 | 737,597 | 47.2 |
| 2002 | 1,008,748 | 39.3 | 1,033,741 | 40.1 |
| 2003 | 1,231,899 | 22.1 | 1,271,588 | 23.0 |
| 2004 | 1,312,783 | 6.6 | 1,328,061 | 4.4 |
| | | | | |
| 5-Yr CAGR | ... | 25.7 | ... | 22.3 |
| 5-Yr Change | ... | 213.3 | ... | 173.7 |
| | | | | |
| 03/2004 | 293,388 | 17.2 | 298,775 | 14.4 |
| 03/2005 | 292,452 | -0.3 | 296,573 | -0.7 |

| Period | NPW | | NPE | |
|---|---|---|---|---|
| Ending | ($000) | (% Chg) | ($000) | (% Chg) |
| 2000 | ... | 100.0 | ... | ... |
| 2001 | ... | ... | ... | ... |
| 2002 | ... | ... | ... | ... |
| 2003 | ... | ... | ... | ... |
| 2004 | ... | ... | ... | ... |
| | | | | |
| 5-Yr CAGR | ... | -99.9 | ... | 0.0 |
| 5-Yr Change | ... | 100.0 | ... | 0.0 |
| | | | | |
| 03/2004 | ... | ... | ... | ... |
| 03/2005 | ... | ... | ... | ... |

**Reserve Quality:** Loss reserves have proved deficient by relatively wide margins in each of the past four calendar years with most accident years being adversely affected. Particularly hard hit have been the 1997 through 2002 accident years, most often which coincided with the worst of the soft-market years. There was another sizable reserve charge of $2.0 billion recorded in 2004, the bulk of which related to accident years 2002 and prior, and was driven by construction defect claims (general liability) and, to a lesser extent, to workers' compensation claims. Both lines of business are generating more severe losses then were originally anticipated in ultimate loss reserve estimates.

Based on Footnote 33 data, Zurich U.S. reported $226 million and $163 million of net asbestos and environmental reserves, respectively, at year-end 2004. The group's asbestos and environmental - exposed business generally relates to pre-1986 general liability policies written on a primary and excess basis. A&E reserves constitute a modest 3% of the group's overall loss reserve base. Zurich U.S.'s three-year survival ratio (reserves-to-average paid losses) of 7.5 times compares unfavorably to Best's undiscounted industry benchmark survival ratio of 20 times. The group increased its net A&E reserve position by approximately $23 million and $43 million in 2004 and 2003, respectively. The group has maintained a centralized facility to handle its A&E claims for fifteen years. A sizable staff of professionals is dedicated to oversight and management of A&E claims. Resolution strategies include policy buy-outs with indemnification, site releases, structured contingent settlement with caps and proactive declaratory judgment litigation. These actions have served to accelerate loss payments, thus negatively impacting reported survival ratios. Nevertheless, A.M. Best remains somewhat concerned over the overall level of both A&E and core loss reserve adequacy.

**Reinsurance Utilization:** Relative to many of its peers, Zurich U.S. utilizes a significant and growing amount of reinsurance with roughly half of its gross premium income ceded under its current reinsurance programs. Approximately two-thirds of the group's ceded premiums is ceded to non-affiliated companies with the remainder ceded to Zurich affiliates. Non-affiliated reinsurance purchases are made using a highly structured methodology to provide capacity to the group. Zurich's dependence on reinsurance is very high with unaffiliated recoverables equal to 2.6 times surplus, more than the commercial casualty industry norm. The group maintains a risk management approach that limits its gross loss from a 250-year catastrophe event to approximately 33% of surplus for hurricane and earthquake perils. The group's strong reinsurance program limits the net probable maximum loss to less than 6% of surplus.

## CEDED REINSURANCE ANALYSIS ($000)

| | Company | | | | Industry Composite | | |
|---|---|---|---|---|---|---|---|
| Year | Ceded Reins Total | Business Retention (%) | Rein Rec to PHS (%) | Ceded Reins to PHS (%) | Business Retention (%) | Rein Rec to PHS (%) | Ceded Reins to PHS(%) |
| 2000 | 865,801 | ... | 405.3 | 591.4 | 74.0 | 95.6 | 138.9 |
| 2001 | 885,998 | ... | 430.8 | 588.1 | 70.6 | 129.2 | 178.5 |
| 2002 | 852,444 | ... | 694.9 | 972.4 | 71.4 | 139.4 | 195.8 |
| 2003 | 968,146 | ... | 718.1 | 999.9 | 72.4 | 122.9 | 175.0 |
| 2004 | 1,119,876 | ... | 648.9 | 874.0 | 76.3 | 108.2 | 147.8 |

## 2004 REINSURANCE RECOVERABLES ($000)

| | Paid & Unpaid Losses | IBNR | Unearned Premiums | Other Recov* | Total Reins Recov |
|---|---|---|---|---|---|
| US Affiliates | 500,441 | 913,795 | 432,525 | 5,525 | 1,852,287 |
| Foreign Affiliates | 23,865 | 53,714 | 17,128 | ... | 94,706 |
| US Insurers | 202,825 | 395,200 | 88,952 | -79 | 686,899 |
| Pools/Associations | 6,038 | 13 | 8 | ... | 6,058 |
| Other Non-US | 18,674 | 25,496 | 5,177 | -5,445 | 43,901 |

| | | | | | |
|---|---|---|---|---|---|
| Total (ex US Affils) | 251,402 | 474,423 | 111,265 | -5,524 | 831,564 |
| Grand Total | 751,840 | 1,388,218 | 543,791 | ... | 2,683,850 |

* Includes Commissions less Funds Withheld

### INVESTMENT LEVERAGE ANALYSIS (% OF PHS)

| | Company | | | | | | Industry Composite | |
|---|---|---|---|---|---|---|---|---|
| Year | Class 3-6 Bonds | Real Estate/ Mtg. | Other Invested Assets | Common Stocks | Non-Affl Inv. Lev. | Affil Inv. | Class 3-6 Bonds | Common Stocks |
| 2000 | ... | ... | 4.5 | ... | 4.5 | 0.0 | 7.6 | 26.7 |
| 2001 | ... | ... | 3.4 | 0.0 | 3.5 | 0.0 | 10.5 | 24.1 |
| 2002 | ... | ... | 6.8 | 0.0 | 6.9 | 0.0 | 10.4 | 18.0 |
| 2003 | ... | ... | 6.7 | ... | 6.7 | 0.0 | 8.6 | 19.4 |
| 2004 | ... | ... | 5.3 | ... | 5.3 | 0.0 | 6.7 | 19.1 |

# LIQUIDITY

The following text is derived from the report of Zurich U.S.

While current liquidity ratios are significantly lower than the group's commercial casualty peers, both underwriting and operating cash flows have been growing quickly and remain strong. These cash flows have significantly improved since 2001, benefiting from increased market rates and the group's high profile in the market. Underwriting cash flow has been boosted over the period primarily due to reduced loss and expense payments coupled with a moderate increase in premium collections. Zurich U.S. maintains a high-quality fixed income portfolio, including tax exempt municipal, U.S. government, high-quality corporate bonds and mortgage-backed securities, with an average bond maturity of under six years at year-end 2004. Invested assets represent 68% of total assets, which is lower than many of its commercial lines peer companies. In addition, the group maintains relatively sizable long-term receivables associated with its retrospectively rated business. Zurich U.S. has also decreased the size of its equity portfolio bringing it in line with industry peers.

### LIQUIDITY ANALYSIS

| | Company | | | | Industry Composite | | | |
|---|---|---|---|---|---|---|---|---|
| Year | Quick Liq (%) | Current Liq (%) | Overall Liq (%) | Gross Agents Bal to PHS(%) | Quick Liq (%) | Current Liq (%) | Overall Liq (%) | Gross Agents Bal to PHS(%) |
| 2000 | 19.1 | 226.1 | 999.9 | ... | 25.1 | 108.6 | 142.2 | 18.4 |
| 2001 | 8.3 | 191.5 | 999.9 | ... | 22.8 | 101.1 | 135.6 | 18.1 |
| 2002 | 37.5 | 173.3 | 999.9 | ... | 24.0 | 98.9 | 133.1 | 18.8 |
| 2003 | 63.1 | 152.8 | 999.9 | ... | 26.1 | 102.3 | 134.5 | 14.9 |
| 2004 | 116.8 | 243.1 | 249.6 | -0.4 | 24.0 | 105.8 | 136.4 | 14.0 |
| 03/2004 | XX | 999.9 | 999.9 | ... | XX | XX | XX | XX |
| 03/2005 | XX | 62.8 | 162.5 | 0.5 | XX | XX | XX | XX |

## CASH FLOW ANALYSIS ($000)

| | | Company | | | | Industry Composite | |
|---|---|---|---|---|---|---|---|
| Year | Underw Cash Flow | Oper Cash Flow | Net Cash Flow | Underw Cash Flow(%) | Oper Cash Flow(%) | Underw Cash Flow(%) | Oper Cash Flow(%) |
| 2000 | 452 | 7,599 | 3,123 | ... | 732.8 | 86.4 | 101.4 |
| 2001 | ... | 9,259 | -2,788 | ... | ... | 87.6 | 103.2 |
| 2002 | ... | 10,695 | 303 | ... | ... | 102.6 | 114.8 |
| 2003 | ... | 4,887 | -499 | ... | ... | 113.2 | 123.7 |
| 2004 | 26,314 | 31,051 | -2,917 | 144.9 | 152.9 | 121.2 | 130.6 |
| 03/2004 | ... | 1,051 | -2,902 | ... | ... | XX | XX |
| 03/2005 | 122,751 | 123,918 | -22 | -99.9 | -99.9 | XX | XX |

# HISTORY

This company was organized under the laws of New York as an affiliate of the United States Branch of the Zurich Insurance Company. It commenced business on September 6, 1939.

The Zurich Fire Insurance Company of New York, a former member of the Zurich Group, was merged into the company at the close of business on December 31, 1952.

Administrative offices were moved in early 1980 from Chicago to Schaumburg, Illinois.

Capital stock of $5,000,027 consists of 6,636 common shares at $753.47 par value each. All authorized shares are outstanding.

The company is a member of the Zurich U.S. pool.

# MANAGEMENT

The company is owned by Zurich American Insurance Company. Zurich American is owned by Zurich Holding Company of America, Inc. which is, in turn, owned by the Zurich Financial Services Group.

All of the outstanding capital stock passed to Zurich American Insurance Company in December, 1998 (as a surplus contribution) from its parent, Zurich Holding Company of America, Inc. Prior to October 31, 1981, direct stock ownership had resided with the former U.S. Branch of Zurich Insurance Company, Switzerland.

The management of this company also directs the affairs of Zurich American Insurance Company.

**Officers:** Chief Executive Officer, Axel Lehmann; President, Thomas A. Bradley; Executive Vice President and Secretary, David A. Bowers; Executive Vice President and Treasurer, David A. Levinson; Executive Vice Presidents, E. Randall Clouser, J. Peter Connors, James D. Engel, Robert M. Fishman, Craig J. Fundum, Donna L. Galer, Barry J. Gilway, Donald J. Hurzeler, John A. Kelm, Michael D. Markman, Nancy D. Mueller, Frank A. Patalano, Steve Rand, David J. Saul, Raymond C.

Thomas, Dianne Whidden.

**Directors:** David A. Bowers, Thomas A. Bradley, James D. Engel, Donna L. Galer, Barry J. Gilway, Donald J. Hurzeler, John A. Kelm, Axel Lehmann (Chairman), James W. March, Michael D. Markman, Nancy D. Mueller, Juliet G. Nash, Frank A. Patalano.

# REGULATORY

An examination of the financial condition is being made as of December 31, 2003 by the Insurance Department of New York. An annual independent audit of the company is conducted by PricewaterhouseCoopers, LLP. An annual evaluation of reserves for unpaid losses and loss adjustment expenses is made by Nancy D. Mueller, Executive Vice President.

# TERRITORY

The company is licensed in the District of Columbia and all states.

# REINSURANCE PROGRAMS

The following text is derived from the report of Zurich U.S.

Reinsurance facilities are maintained, with excess of loss, surplus and catastrophe contracts protecting all members of the Zurich U.S. pool. For fiscal year 2005, the maximum net exposure on any single loss for the group is $25,000,000 on property risks. On hospital risks with high limits, an additional $200,000,000 may be kept net and unreinsured in limits above $500,000,000, subject to the first $500,000,000 containing twice the risk's EML. On casualty risks the maximum is $15,000,000 which includes participations in voluntary pools that are not subject to the group's casualty reinsurance programs.

Reinsurance agreements with various insurers and reinsurers afford protection to the group above retentions of $25,000,000 per occurrence on workers compensation, $10,000,000 excess of loss per risk on commercial lines property, $12,000,000 excess of loss per occurrence on all commercial casualty and commercial umbrella covers. On global property risks the maximum net exposure is $25,000,000 per risk.

Catastrophe reinsurance provides coverage for 95% of net losses above $175,000,000 up to $825,000,000 per occurrence for the Zurich U.S. pool.

# BALANCE SHEET ($000)

| ADMITTED ASSETS | 12/31/2004 | 12/31/2003 | 2004 % | 2003 % |
|---|---|---|---|---|
| Bonds | 121,468 | 83,075 | 56.8 | 88.4 |
| Cash & short-term invest | 89 | 3,005 | 0.0 | 3.2 |
| Other non-affil inv asset | 6,727 | 6,293 | 3.1 | 6.7 |
| Investments in affiliates | 1 | 1 | 0.0 | 0.0 |
| Total invested assets | 128,285 | 92,375 | 60.0 | 98.3 |

| | | | | |
|---|---|---|---|---|
| Premium balances | -561 | ... | -0.3 | ... |
| Accrued interest | 992 | 757 | 0.5 | 0.8 |
| All other assets | 85,053 | 855 | 39.8 | 0.9 |
| Total assets | 213,770 | 93,987 | 100.0 | 100.0 |

| LIABILITIES & SURPLUS | 12/31/2004 | 12/31/2003 | 2004 % | 2003 % |
|---|---|---|---|---|
| All other liabilities | 85,630 | 258 | 40.1 | 0.3 |
| Total liabilities | 85,630 | 258 | 40.1 | 0.3 |
| Capital & assigned surplus | 177,270 | 147,270 | 82.9 | 156.7 |
| Unassigned surplus | -49,131 | -53,541 | -23.0 | -57.0 |
| Total policyholders' surplus | 128,140 | 93,729 | 59.9 | 99.7 |
| Total liabilities & surplus | 213,770 | 93,987 | 100.0 | 100.0 |

# SUMMARY OF 2004 OPERATIONS ($000)

| STATEMENT OF INCOME | 12/31/2004 | FUNDS PROVIDED FROM OPERATIONS | 12/31/2004 |
|---|---|---|---|
| Premiums earned | ... | Premiums collected | 84,964 |
| Losses incurred | ... | Benefit & loss related pmts | 58,650 |
| Net underwriting income | ... | Undrw cash flow | 26,314 |
| Net investment income | 4,306 | Investment income | 4,737 |
| Pre-tax oper income | 4,306 | Pre-tax cash operations | 31,051 |
| Realized capital gains | 277 | | |
| Income taxes incurred | 13 | Income taxes pd (recov) | ... |
| Net income | 4,570 | Net oper cash flow | 31,051 |

## INTERIM BALANCE SHEET

| ADMITTED ASSETS | 03/31/2005 | | |
|---|---|---|---|
| Cash & short term invest | 66 | ... | ... |
| Bonds | 122,186 | ... | ... |
| Other investments | 7,019 | ... | ... |
| Total investments | 129,272 | | |
| Premium balances | 703 | ... | ... |
| Reinsurance funds | 56,937 | ... | ... |
| Accrued interest | 1,274 | ... | ... |
| All other assets | 149,501 | ... | ... |
| Total assets | 337,687 | | |

| LIABILITIES & SURPLUS | 03/31/2005 |
|---|---|

| | | | |
|---|---|---|---|
| All other liabilities | 207,791 | ... | ... |
| Total liabilities | 207,791 | | |
| Capital & assigned surp | 177,270 | ... | ... |
| Unassigned surplus | -47,375 | ... | ... |
| Policyholders' surplus | 129,896 | | |
| Total liabilities & surplus | 337,687 | | |

## INTERIM INCOME STATEMENT

| | Period Ended 3/31/2005 | Period Ended 3/31/2004 | Increase/ Decrease |
|---|---|---|---|
| Net investment income | 1,253 | 851 | 402 |
| Pre-tax operating income | 1,253 | 851 | 402 |
| Realized capital gains | -40 | 90 | -130 |
| Income taxes incurred | -140 | 101 | -241 |
| Net income | 1,353 | 839 | 513 |

## INTERIM CASH FLOW

| | Period Ended 3/31/2005 | Period Ended 3/31/2004 | Increase/ Decrease |
|---|---|---|---|
| Premiums collected | 121,038 | ... | 121,038 |
| Benefit & loss related pmts | -1,713 | ... | -1,713 |
| Underwriting cash flow | 122,751 | ... | 122,751 |
| Investment income | 1,165 | 1,051 | 114 |
| Pre-tax cash operations | 123,916 | 1,051 | 122,864 |
| Income taxes pd (recov) | -2 | ... | -2 |
| Net oper cash flow | 123,918 | 1,051 | 122,867 |