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MS Frontier Reinsurance Limited

MS Frontier Reinsurance Limited – “MS Frontier Re”, a Class 3 registered reinsurance company incorporated in Bermuda, specializes in Property Catastrophe Reinsurance business, and aims to provide quality reinsurance support and services to business partners around the world.

MSIG has had a presence in Bermuda since 1997 and launched its Property Catastrophe Reinsurance underwriting in July 2002 with the formation of MS Frontier Re. This has been a key part in establishing geographical portfolio optimization and risk diversification for the group.



Standard & Poor's rating:
AA Very Strong



AM Best rating:
A Excellent

Message from the President & Chief Executive Officer



Yasunori Araga
President & Chief Executive Officer

To our business partners,

I am delighted to report on the activities and performance of MS Frontier Reinsurance Limited for the year ended 31st December 2007.

Whilst we have seen several severe regional natural catastrophe events during 2007, for MS Frontier Re, 2007 was another successful year both in expanding business volume and in producing significant profit, continued from 2006.

Our gross premium income reached \$66.2million, increased from \$45.4million in the previous year. This was despite the increased competition in the marketplace, where we have seen continued downward pricing movements after the hike of 2006. The net income recorded in 2007 of \$68.9million, a jump from \$39.5million in 2006, was achieved through consistent underwriting coupled with steady investment returns which were unaffected by the market turbulence caused by the sub-prime mortgage crisis. Moreover, this excellent business performance was due to close relationships with our clients, brokers and other business partners around the world. I am pleased to say, throughout 2007, MS Frontier Re has enhanced its presence and reputation in the global reinsurance markets as a quality reinsurance company specializing in property catastrophe business.

A combination of modeling and research functions, the launch of our Singapore Representative Office in January 2008 is an important step for the company. This will bring further sophistication and depth to our modeling expertise. MS Frontier Re will aim to achieve consistent growth over the reinsurance cycle with the significant support of the Singapore operation.

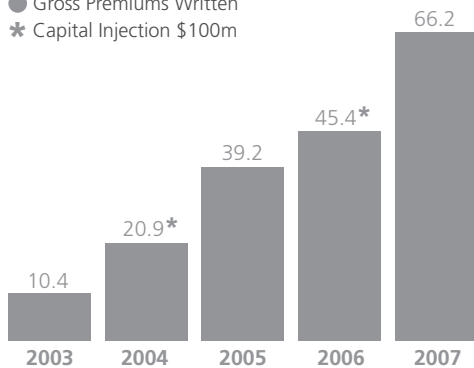
As MS Frontier Re continues to grow, we are also mindful of maintaining the highest standards of compliance and risk management within the company. With the expansion of the Company we have strengthened the various functions of risk management and compliance through internal control projects which utilize various resources from within the Company and also from external sources.

MS Frontier Re has brought highly secured property catastrophe capacity to our valued clients since its launch in 2002. The financial strength of MS Frontier Re is ensured with our healthy balance sheet as well as the credibility associated with being a member company of Mitsui Sumitomo Insurance Group (MSIG). The MSIG network covers 37 countries and 62 cities worldwide, and is regarded as one of the strongest general insurance groups in the world.

“MS Frontier Re – Providing ‘Magnificent Solutions’ to the Reinsurance Industry since 2002.”

Premium Growth
in Millions of US Dollars

- Gross Premiums Written
- * Capital Injection \$100m



In serving our clients in the area of property catastrophe reinsurance with an unchanged philosophy, MS Frontier Re will fulfill our mission to provide geographical portfolio optimization for MSIG. This will ultimately, contribute to the Group's goal of expanding its overseas business.

As we continue to build on our past success, it is our new goal to provide “Magnificent Solutions” to all our customers and business partners. I am extremely grateful for the support they have shown us and look forward to many years of mutual cooperation.

Yasunori Araga
President and Chief Executive Officer

Underwriting Results

“We achieved a significant increase in our gross premium income from \$45.4 million in 2006 to \$66.2 million in 2007, as well as an increase in the number of clients by circa 20%.”

The competition in the reinsurance markets increased during 2007, however with our consistent and clear underwriting philosophy, MS Frontier Re has successfully expanded its property catastrophe reinsurance business over the last couple of years. As the approach to catastrophe modeling and regulations became more standardized and sophisticated in many countries, the demands for higher limits on property catastrophe reinsurance programs and for highly-secured capacity continues to be strong.

During 2007, MS Frontier Re encountered numerous business opportunities in North America, Europe, Asia, Oceania and other wider regions. As a result, we have achieved a significant increase in our gross premium income from \$45.4 million in 2006 to \$66.2 million in 2007, as well as an increase in the number of clients by circa 20%. MS Frontier Re has continued to expand its business relationships with top insurers in many catastrophe prone countries.

By maintaining our disciplined underwriting approach we did not incur any catastrophe losses during the year ended 31st December, 2007. The majority of the incurred loss of \$0.8 million during 2007 was as a result of adverse development of losses which occurred in 2005, which we do not expect to develop materially in the future.

Portfolio Management

Portfolio management is a key function for MS Frontier Re. We have implemented a sophisticated portfolio management methodology, which ensures that risk accumulation is accurately monitored and controlled. Underwriters are always fully aware of the impact to our portfolio before making a decision to accept new or renewal business. Our conservative approach to portfolio management enables us to serve our global clients on a long term basis.

Revenue Segmentation by Region



- Americas 58%
- Europe 30%
- Asia 6%
- Oceania 6%

Underwriting Team



Singapore Operation

“Singapore is the centre of a growing Asia Pacific Reinsurance market and has excellent infrastructure and human resources which MS Frontier Re can capitalize on.”

MS Frontier Re has recognized that as a reinsurer which writes business globally it needs to establish centers of operations in key areas across the Globe.

In 2007 it was decided that we would establish our first overseas office in Singapore to help MS Frontier Re as part of our continued growth. The end result was the successful launch of the Singapore Representative office in January 2008.

Singapore is the center of a growing Asia Pacific Reinsurance market and has excellent infrastructure and human resources which MS Frontier Re can capitalize on. MS Frontier Re wanted to create a center of excellence to perform the many facets of the complex catastrophe modeling which is the cornerstone of our business model. Therefore we have recruited a world class team of modeling experts headed up by Shiro Ozawa to establish a strong knowledge base for the future. We view this as an

important step to providing professional research, independent from our underwriting activity, to ensure proper decision making for the Company.

Additionally our team in Singapore perform marketing research in the Asia Pacific Region to explore the possibilities for property catastrophe reinsurance in this growing market.

This is the first step in gaining a firm foothold in the key Asian markets where we believe there are great opportunities for growth in the future.

The Singapore Representative office is linked real time to our head office in Bermuda and all systems are synchronized and backed up so that at any one time we have fully operational systems should there be a failure in one office.

This important backup feature also provides MS Frontier Re with a clear solution to long term business continuity in an uncertain world.

Role of the Singapore Representative office



Singapore Team



From top to bottom left to right:
Shiro Ozawa, Vice President and Singapore Representative, Mayank Dubey, Andeline Neo, Shitalkumar Khandar, Wendy Pok.

Financial and Investment Highlights

“The company has grown its Shareholders equity through internal growth and strategic capital injections from some \$106m in 2003 to \$394m at the end of 2007.”

In support of our underwriting results MS Frontier Re has invested its capital prudently in the capital markets in a manner that both safeguards the assets of the company and generates a reasonable return.

Returns from investments, including Catastrophe bonds, for 2007 totaled \$20.7m (2006 - \$10.9m).

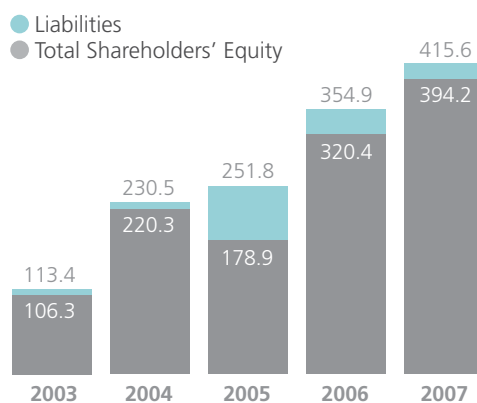
This has helped to generate net income for the year of \$68.9m (2006 - \$39.5m).

The total market value of assets invested as at Dec 31, 2007 was \$383.6m (2006 - \$329.7m). The portfolio of investments has been diversified as it has grown but MS Frontier Re has always maintained conservative guidelines with our investment managers in the areas where we wish to invest. This has stood us in good stead as we have avoided any major downturns in recent times such as investments in securities affected by the sub prime credit crisis. We continue to only invest in high quality, liquid securities.

The company has grown its Shareholders' equity through internal growth and strategic capital injections from some \$106m in 2003 to \$394m

in 2007. This carefully planned growth has seen MS Frontier Re mature into a highly profitable member of MSIG and play a key part of the group's future overseas expansion.

Shareholders' Equity and Total Assets
Over the past 5 years
in Millions of US Dollars



5 Year Historical Highlights
in Millions of US Dollars

	2007	2006	2005	2004	2003
Net Premium Written	66.2	45.0	39.4	19.8	8.2
Investment Income*	18.8	10.5	7.3	2.5	1.9
Net Income	68.9	39.5	(40.7)	14.8	4.9
Shareholders' Equity	394.2	320.4	178.9	220.3	106.3

*Excluding Catastrophe Bond Income

2007 Shareholders Equity
(US Dollars)

2007 Net Income
(US Dollars)

394.2m | 68.9m

Finance and
Administration
Team



From top to bottom left to right:
Gary Devery - Controller,
George Masters, Darren Choonucksing,
Virginia Stephens, Gayle Yoshimoto,
Elaine McGlynn

Financial Statements

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying balance sheets of MS Frontier Reinsurance Limited as of December 31, 2007 and 2006 and the related statements of income and comprehensive income, changes in shareholder's equity and cash flows for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of MS Frontier Reinsurance Limited as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.



Chartered Accountants
Hamilton, Bermuda
April 1, 2008

Balance Sheets

December 31, 2007 and 2006 (Expressed in United States Dollars)

	2007	2006
Assets		
Cash and cash equivalents (Note 3)	\$ 7,694,366	\$ 4,532,649
Investments (Note 3)	383,576,638	329,654,850
Accrued interest receivable	5,884,209	4,974,584
Reinsurance balances receivable	14,600,983	12,723,453
Unearned ceded premiums (Note 8)	–	121,493
Funds withheld	25,050	222,618
Deferred acquisition expenses	2,202,550	1,545,570
Prepaid expenses	1,292,191	844,494
Capital assets (Note 6)	311,629	277,890
Total assets	415,587,616	354,897,601
Liabilities		
Outstanding losses and loss expenses (Notes 7 and 8)	3,351,072	21,176,327
Unearned premiums (Note 8)	17,322,003	12,640,228
Reinsurance balances payable (Note 8)	12,251	170,926
Deferred commission income (Note 8)	–	17,009
Accounts payable and accrued expenses (Note 8)	736,141	503,715
Total liabilities	21,421,467	34,508,205
Shareholder's equity		
Share capital (Note 10)	200,000,000	200,000,000
Contributed surplus (Note 10)	100,000,000	100,000,000
Accumulated other comprehensive income	5,514,372	596,272
Retained earnings	88,651,777	19,793,124
Total shareholder's equity	394,166,149	320,389,396
Total liabilities and shareholder's equity	\$ 415,587,616	\$ 354,897,601

See accompanying notes to financial statements

Statements of Income and Comprehensive Income

Years ended December 31, 2007 and 2006 (Expressed in United States Dollars)

	2007	2006
Income		
Premiums assumed (Note 8)	\$ 66,204,673	\$ 45,437,496
Change in unearned premiums	(4,681,775)	(1,982,755)
Premiums earned	61,522,898	43,454,741
Premiums ceded (Notes 5 and 8)	—	(442,544)
Change in unearned ceded premiums	(121,493)	121,493
Ceded premiums earned	(121,493)	(321,051)
Net premiums earned	61,401,405	43,133,690
Catastrophe bond income	1,930,991	351,312
Investment income	18,777,106	10,536,578
Loss on sale of investments (Note 3)	(148,124)	(2,073,674)
Commission income (Note 8)	17,009	41,251
Foreign exchange gain	170,821	1,877,377
Total income	82,149,208	53,866,534
Expenses		
Losses and loss expenses incurred (Notes 7 and 8)	821,941	5,289,387
Acquisition expenses	6,535,883	4,790,237
General and administrative expenses (Note 8)	5,932,731	4,292,011
Total expenses	13,290,555	14,371,635
Net income	68,858,653	39,494,899
Other comprehensive income		
Unrealized holding gains (losses) arising during year	4,769,976	(87,784)
Less: reclassification adjustment for losses included in net income	(148,124)	(2,073,674)
Other comprehensive income	4,918,100	1,985,890
Comprehensive income	\$ 73,776,753	\$ 41,480,789

See accompanying notes to financial statements

Statements of Changes in Shareholder's Equity

Years ended December 31, 2007 and 2006 (Expressed in United States Dollars)

	2007	2006
Share capital		
Balance at beginning and end of year	\$ 200,000,000	\$ 200,000,000
Contributed surplus		
Balance at beginning of year	100,000,000	–
Additional contribution in year	–	100,000,000
Balance at end of year	100,000,000	100,000,000
Accumulated other comprehensive income		
Balance at beginning of year	596,272	(1,389,618)
Movement in year	4,918,100	1,985,890
Balance at end of year	5,514,372	596,272
Retained earnings		
Balance at beginning of year	19,793,124	(19,701,775)
Net income	68,858,653	39,494,899
Balance at end of year	88,651,777	19,793,124
Total shareholder's equity	\$ 394,166,149	\$ 320,389,396

See accompanying notes to financial statements

Statements of Cash Flows

Years ended December 31, 2007 and 2006 (Expressed in United States Dollars)

	2007	2006
Cash flows from operating activities		
Net income	\$ 68,858,653	\$ 39,494,899
Adjustments to reconcile net income to net cash provided by (used by) operating activities:		
Amortization of investments	(1,204,559)	161,297
Amortization of capital assets	87,653	73,437
Loss on sale of investments	148,124	2,073,674
Loss on sale of capital assets	13,522	3,212
Accrued interest receivable	(909,625)	(2,806,039)
Reinsurance balances receivable	(1,877,530)	(2,735,928)
Unearned ceded premium	121,493	(121,493)
Funds withheld	197,568	(25,343)
Deferred acquisition expenses	(656,980)	(324,942)
Prepaid expenses	(447,697)	45,011
Outstanding losses and loss expenses	(17,825,255)	(40,846,679)
Unearned premiums	4,681,775	1,982,755
Reinsurance balances payable	(158,675)	170,926
Deferred commission income	(17,009)	17,009
Accounts payable and accrued expenses	232,426	322,211
Cash provided by (used by) operating activities	51,243,884	(2,515,993)
Cash flows from investing activities		
Purchase of investments	(141,934,399)	(404,712,328)
Proceeds from sale of investments	93,987,146	260,399,445
Purchase of capital assets	(134,914)	(113,915)
Proceeds from sale of capital assets	-	2,000
Cash used by investing activities	(48,082,167)	(144,424,798)
Cash flows from financing activities		
Proceeds from contribution of surplus	-	100,000,000
Cash provided by financing activities	-	100,000,000
Net increase (decrease) in cash and cash equivalents	3,161,717	(46,940,791)
Cash and cash equivalents at beginning of year	4,532,649	51,473,440
Cash and cash equivalents at end of year	\$ 7,694,366	\$ 4,532,649

See accompanying notes to financial statements

Notes to Financial Statements

December 31, 2007 and 2006

1. General

MS Frontier Reinsurance Limited (the "Company") was incorporated under the laws of Bermuda on September 9, 1997 and is licenced as a Class 3 and Long Term reinsurer under the Insurance Act, 1978 of Bermuda and related regulations to write all classes of property and casualty business.

The Company participates in various excess of loss property catastrophe reinsurance contracts. Property catastrophe reinsurance covers unpredictable events such as hurricanes, windstorms, hailstorms, earthquakes, fires, industrial explosions, freezes, floods and other man-made or natural disasters. Because the Company has large aggregate exposure to these risks, the Company expects that its claims experience will be characterized by relatively low frequency and high severity claims. The occurrence of claims from catastrophic events is likely to result in substantial volatility in the Company's financial results for any particular period. The Company endeavours to manage its exposures to catastrophic events by limiting the amount of its exposure in each geographic zone.

In prior years the Company participated in various quota share pools covering risks such as fire, property and other man-made or natural disasters and provided excess of loss coverage of cargo, windstorm and property risks of its ultimate parent company. This business has been in run-off since 2002.

2. Summary of significant accounting policies

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The following are the significant accounting policies adopted by the Company:

(a) Premiums assumed and ceded, acquisition expenses and commission income

Premiums assumed are recorded on the accruals basis and are included in income on a pro-rated basis over the period of underlying coverage with the unearned portion deferred in the balance sheet. Reinsurance premiums are similarly pro-rated over the period of coverage with the unearned portion deferred in the balance sheet as unearned ceded premiums. Premium estimates on certain policies are made using the latest information available to management. Adjustments to estimates are recorded in the period in which they are determined. Reinstatement premiums are recognized in accordance with the provisions of the reinsurance contracts. Reinstatement premiums are accrued at the time losses are incurred and, where coverage of the original contract is reinstated under pre-defined contract terms, are earned pro-rata over the reinstated coverage period.

Acquisition expenses and income, mainly commissions and brokerage, related to unearned premiums and unearned ceded premiums are deferred and amortized to income over the periods in which the premiums are earned. The method followed in determining the deferred acquisition expenses limits the amount of the deferral to its realizable value by giving consideration to losses and loss expenses expected to be incurred as premiums are earned.

Notes to Financial Statements

December 31, 2007 and 2006

2. Summary of significant accounting policies (continued)

(b) Outstanding losses and loss expenses

Losses and loss expenses are recorded when advised by the ceding insurance companies. Outstanding losses represent management's estimate of the amount of reported losses and loss expenses based on reports received from the ceding insurance companies plus a provision for losses incurred but not reported ("IBNR"). The IBNR provision is estimated by management based on reports from industry sources, including initial estimates of aggregate industry losses, individual loss estimates received from ceding companies and brokers, output from commercially available catastrophe loss models and actuarial analysis using historical data available to the Company on the business assumed together with industry data.

Given the inherent nature of major catastrophic events, considerable uncertainty underlies the assumptions and associated estimated reserve for losses and loss expenses. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments, if any, are reflected in income in the period in which they are determined. Due to the inherent uncertainty in estimating the liability for losses and loss expenses, there can be no assurance that the ultimate liability will not be settled for a significantly greater or lesser amount than that recorded. Based on the current assumptions used management believes that the Company's recorded amount is a reasonable estimate of the ultimate cost of losses incurred to the balance sheet date.

Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities.

(c) Profit commissions

Certain policies include terms and conditions which may result in the payment of profit commissions. Estimates of profit commissions are continually reviewed based on the underwriting experience to date, and as adjustments become necessary, such adjustments are reflected in current operations. Profit commissions are accrued to the balance sheet date, and included within accounts payable and accrued expenses.

(d) Investments

All investments are classified as available-for-sale securities under the provisions of Statement of Financial Accounting Standards No. ("SFAS") 115, "Accounting for Certain Investments in Debt and Equity Securities". Unrealized gains and losses are included within accumulated other comprehensive income as a separate component of shareholder's equity in the balance sheet. Fair values for fixed maturity securities are based on quoted market prices. Fair values for catastrophe bonds are based on independent broker quotes.

Notes to Financial Statements

December 31, 2007 and 2006

2. Summary of significant accounting policies (continued)

Realized gains and losses are derived using the specific identification method for determining the cost of securities sold. A decline in the market value of any security below cost that is deemed other than temporary is charged to earnings resulting in the establishment of a new cost basis for the security.

The Company's assessment of decline in value deemed to be other-than-temporary includes judgement as to the financial position and future prospects of the entity that issued the security. If that judgement changes in the future, the Company may ultimately record a realised loss after originally concluding that the decline in value was temporary. Factors which management consider in evaluating other-than-temporary declines in value include the extent of decline, the length of time the security is below cost, the Company's intent and ability to hold the security, the future prospects of the issuer and other qualitative and quantitative factors.

(e) Investment income and catastrophe bond income

Investment income is accrued to the balance sheet date, and includes the amortization of premium or discount on the Company's investments in marketable securities purchased at amounts different from their par value.

Catastrophe bond income is accrued to the balance sheet date and relates to the risk premium in excess of LIBOR on each catastrophe bond held.

(f) Amortization of capital assets

Amortization of capital assets is computed using the declining balance method at rates estimated to amortize their cost over their estimated useful lives. The following rates are used:

Furniture and fixtures	10-20%
Computer equipment	33%
Office equipment	20%
Motor vehicles	20%

(g) Translation of foreign currencies

Foreign currency assets and liabilities considered monetary items are translated at exchange rates in effect at the balance sheet date. Foreign currency revenues and expenses are translated at the transaction date exchange rates. Exchange gains and losses are included in the determination of net income.

(h) Cash and cash equivalents

For purposes of the statements of cash flows the Company considers all time deposits with an original maturity of ninety days or less as equivalent to cash.

Notes to Financial Statements

December 31, 2007 and 2006

3. Cash and investments

(a) Cash and cash equivalents are held at a European branch of a Japanese bank and two banks in Bermuda. The Company's management evaluates the financial strength and stability of these institutions on a periodic basis.

The bankers of the Company's parent issued letters of credit in the amount of \$2,552,500 (2006 - \$17,330,478) in favor of US ceding companies. The Company's parent has pledged assets of a similar amount as security for these letters of credit.

(b) The amortized cost and fair value of investments in marketable securities classified as available-for-sale are as follows:

	Amortized cost	Unrealized gains	Unrealized losses less than 12 months	Unrealized losses greater than 12 months	Fair value
December 31, 2007					
U.S. government and government agency	\$ 32,514,578	\$ 322,633	\$ -	\$ -	\$ 32,837,211
U.S. corporate securities	268,048,448	4,189,236	(321,589)	(186,561)	271,729,534
EU government and government agency	17,772,383	704,122	-	-	18,476,505
Catastrophe bonds	40,174,200	572,398	(50,550)	-	40,696,048
Other corporate securities	19,552,657	284,683	-	-	19,837,340
	\$378,062,266	\$ 6,073,072	\$ (372,139)	\$ (186,561)	\$383,576,638
December 31, 2006					
U.S. government and government agency	\$ 58,010,517	\$ 36,168	\$ (49,166)	\$ -	\$ 57,997,519
U.S. corporate securities	175,301,874	742,611	(182,053)	(131,386)	175,731,046
EU government and government agency	17,643,675	186,905	-	-	17,830,580
EU corporate securities	4,476,613	2,281	(3,648)	(41)	4,475,205
Catastrophe bonds	22,500,000	31,300	(50,825)	-	22,480,475
Other corporate securities	51,125,899	98,032	(67,652)	(16,254)	51,140,025
	\$329,058,578	\$ 1,097,297	\$ (353,344)	\$ (147,681)	\$329,654,850

Notes to Financial Statements

December 31, 2007 and 2006

3. Cash and investments (continued)

Unrealized losses on investments held at December 31, 2007 and 2006 comprise an accumulation of relatively small unrealized losses on a security by security basis caused by general interest rate movements rather than credit events. There are no amounts in respect of declines in the value of individual securities considered to be other than temporary included in gross unrealized losses on fixed maturity investments for the years ended December 31, 2007 and 2006.

The Company's management has evaluated the Company's investments in marketable securities for exposure to sub prime mortgages and structured credit products. The Company does not invest in asset-backed or mortgage-backed securities and therefore the Company has insignificant direct exposure to sub prime mortgages.

- (c) For investments in marketable securities held on December 31, 2007 the maturity distribution is as follows:

	Amortized cost	Fair value
Within one year	\$ 79,932,259	\$ 80,025,630
From one to five years	293,225,578	298,687,604
From five to ten years	4,904,429	4,863,404
	<u>\$ 378,062,266</u>	<u>\$ 383,576,638</u>

- (d) During the year, proceeds from the sale of investments amounted to \$93,987,146 (2006 - \$260,399,445) and the Company realized gains of \$228,104 and losses of \$376,228 (2006 - gains of \$68 and losses of \$2,073,742) on those sales.

With the exception of catastrophe bonds, the investments held at December 31, 2007 have all been assigned a credit rating of BBB+ or better by Standard & Poor's. In accordance with the Company's investment guidelines, with the exception of U.S. government and government agency securities, no more than 10% of the investment portfolio may be invested in any one issuer. The largest holding in corporate securities represents 6.6% (2006 - 4.7%) of the total investment portfolio.

- (e) The Company holds investments in catastrophe bonds with a fair value of \$40,696,048 at December 31, 2007, comprised of fourteen catastrophe bonds with Standard and Poor's ratings ranging from BB to BB+ and maturities ranging from 2008 to 2011. The issuers of these securities have used the proceeds raised to collateralize certain catastrophe reinsurance obligations, specifically chosen to complement the Company's overall underwriting risk profile. The investment in these securities is therefore at risk of loss, in whole or in part, if a covered catastrophe occurs.

Notes to Financial Statements

December 31, 2007 and 2006

4. Fair value of financial instruments

The carrying amount of cash and cash equivalents approximates fair value because of the short maturity of those instruments. Investments are carried at fair value based on quoted market prices, or in the case of catastrophe bonds, the fair value is based on independent broker quotes. The fair value of other assets and liabilities, consisting of accrued interest receivable, reinsurance balances receivable, funds withheld, reinsurance balances payable, accounts payable and accrued expenses approximates their carrying value due to their relative short term nature.

The estimates of fair value of other assets and liabilities are subjective in nature and are not necessarily indicative of the amounts that the Company would actually realize in a current market exchange. However, any differences would not be expected to be material. Certain instruments such as deferred acquisition expenses, prepaid expenses, outstanding losses and loss expenses, unearned premiums, unearned ceded premiums and deferred commission income are excluded from fair value disclosure. Thus the total fair value amounts cannot be aggregated to determine the underlying economic value of the Company.

5. Reinsurance

Reinsurance contracts do not relieve the Company from its obligations to policyholders. Failure of the reinsurer to honor its obligations could result in losses to the Company; consequently, allowances are established for amounts deemed uncollectible. The Company regularly evaluates the financial condition of its reinsurer. At December 31, 2007 and 2006, no recoveries are due from the Company's reinsurer. All ceded reinsurance has been placed with the parent company, Mitsui Sumitomo Insurance Company Limited. Mitsui Sumitomo Insurance Company Limited has a credit rating of AA (2006 - AA-) from Standard & Poor's. No new premiums have been ceded since 2004 and ceded premiums recorded are adjustments to prior year premium estimates (Note 8).

6. Capital assets

Capital assets consist of the following:

			2007	2006
	Cost	Accumulated amortization	Net book value	Net book value
Furniture and fixtures	\$ 269,786	\$ 84,686	\$ 185,100	\$ 188,603
Motor vehicles	148,806	87,520	61,286	49,244
Computers	51,602	35,680	15,922	29,917
Office Equipment	57,945	8,624	49,321	10,126
	\$ 528,139	\$ 216,510	\$ 311,629	\$ 277,890

Notes to Financial Statements

December 31, 2007 and 2006

7. Outstanding losses and loss expenses

The summary of changes in outstanding losses and loss expenses at December 31, 2007 and 2006 are as follows:

	2007	2006
Balance at beginning of year	\$ 21,176,327	\$ 62,023,006
Incurred related to:		
Prior years	803,479	4,344,791
Foreign exchange loss on outstanding losses and loss expenses	18,462	944,596
Total loss and loss expenses incurred	821,941	5,289,387
Paid related to:		
Prior years	18,647,196	46,136,066
Total paid losses	18,647,196	46,136,066
Balance at end of year	\$ 3,351,072	\$ 21,176,327

As a result of changes in estimates of insured events for prior years, the liability for unpaid losses and loss expenses increased by \$803,479 (2006 - \$4,344,791), due primarily to adverse development in claims associated with MSI Liability Excess of Loss Underlayer and Hurricane Katrina in the United States of America.

For certain catastrophic events there are considerable uncertainties underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Reserves are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments could require a material change in the amount estimated. The uncertainty surrounding reserves for property catastrophe exposures arises from problems such as policy coverage issues, multiple events affecting one geographic area and the impact on claims adjusting by ceding companies. These issues can cause significant delays to the timing of notification of changes to loss estimates reported by ceding companies.

Notes to Financial Statements

December 31, 2007 and 2006

8. Related party transactions

The Company provides certain higher layer property catastrophe excess of loss coverage for its ultimate parent and other affiliated companies. Premiums assumed from the parent or affiliates amounted to \$2,615,027 (2006 - \$2,368,064), and were undertaken on normal commercial rates. Other balance sheet and income statement items associated with these policies include the following:

	2007	2006
Unearned premiums	\$ 577,703	\$ 491,478
Outstanding losses and loss expenses	300,000	3,108
Losses and loss expenses incurred	(296,892)	(138,715)

In prior years, the Company had entered into a retrocession agreement with its parent company, whereby the Company ceded to its parent a portion of certain high layer property catastrophe risks. During 2007 and 2006, the Company did not have premiums ceded to the parent company, however due to premium adjustments on related assumed contracts, the Company had ceded premium adjustments of \$Nil (2006 - positive ceded income of \$442,544). Other balance sheet and income statement items associated with these ceded policies include the following:

	2007	2006
Reinsurance balances payable	\$ (12,251)	\$ (127,249)
Unearned ceded premium	–	121,493
Deferred commission income	–	17,009
Commission income	17,009	41,251

The Company has appointed a company related through common control as an investment manager. The Company pays fees for investment management services based on the month end market value of the total investment portfolio. The fees are based on standard market rates and are included in general and administrative expenses. The fees incurred for the above services were \$354,962 (2006 - \$270,927). At December 31, 2007 fees of \$57,148 (2006 - \$18,000) are included in accounts payable and accrued expenses.

Notes to Financial Statements

December 31, 2007 and 2006

9. Commitment

The Company has entered into an agreement to lease office space for \$28,210 per month until the lease expires on June 30, 2011.

10. Share capital and contributed surplus

The Company's share capital comprises 200,000,000 authorized, issued and fully paid shares of \$1 par value each.

On November 13, 2006 a cash injection of \$100,000,000 was made to the contributed surplus of the Company by its parent, Mitsui Sumitomo Insurance Company Limited.

11. Statutory requirements

The Company is required by its licence to maintain capital and surplus greater than a minimum statutory amount determined as the greater of a percentage of outstanding losses or a given fraction of net written premiums. At December 31, 2007 the Company is required to maintain a minimum statutory capital and surplus of \$10,230,701. Actual statutory capital and surplus is \$390,359,779.

Actual statutory capital and surplus, as determined using statutory accounting principles, is as follows:

Total shareholder's equity	\$ 394,166,149
Less non-admitted assets:	
Deferred acquisition expenses	2,202,550
Prepaid expenses	1,292,191
Capital assets	311,629
Statutory capital and surplus	<u>\$ 390,359,779</u>

The Company is also required to maintain a minimum liquidity ratio whereby the value of its relevant assets are not less than 75% of the amount of its relevant liabilities. Relevant assets include cash and cash equivalents, investments, accrued interest receivable, reinsurance balances receivable and funds withheld. Certain categories of assets do not qualify as relevant assets under the statute. The relevant liabilities are total general business insurance reserves and total other liabilities, less sundry liabilities.

At December 31, 2007 the Company was required to maintain relevant assets of \$16,066,101. At that date relevant assets were \$411,781,246 and the minimum liquidity ratio was therefore met.

Notes to Financial Statements

December 31, 2007 and 2006

12. Taxation

Under current Bermuda law the Company is not required to pay any taxes in Bermuda on either income or capital gains. The Company has received an undertaking from the Minister of Finance in Bermuda that in the event of any such taxes being imposed the Company will be exempted from taxation until the year 2016.

In July 2006, the FASB issued FIN 48, which clarifies the criteria for recognition and measurement of income tax benefits in accordance with SFAS 109, "Accounting for Income Taxes". Under FIN 48, evaluation of income tax benefits is a two-step process. First, income tax benefits can be recognized in financial statements for a tax position only if it is considered "more likely than not," as defined in SFAS 5, "Accounting for Contingencies", of being sustained on audit based solely on the technical merits of the income tax position. Second, if the recognition criteria are met, the amount of income tax benefits to be recognized is measured based on the largest income tax benefit that is more than 50 percent likely to be realized on ultimate resolution of the tax position. FIN 48 is effective on January 1, 2007, and any amounts to be recorded upon implementation will result in a one-time adjustment to beginning retained earnings as a cumulative effect of a change in accounting principle. The Company adopted FIN 48 on January 1, 2007 and it has not had any effect on the Company's financial position or result of operations.