



DECEMBER 5, 2007

CIRCULAR NO. 24/07

TO MEMBERS OF THE ASSOCIATION

Dear Member:

DEVELOPMENT OF OPEN POLICY YEARS

**SETTLEMENT OF THE DECLARATORY JUDGEMENT ACTION CONCERNING
CLOSED YEAR OCCUPATIONAL DISEASE CLAIMS AND THE ENHANCEMENT OF
CLUB SURPLUS**

CLOSURE OF THE 2004 POLICY YEAR

At its recent meeting in Shanghai, in addition to deciding upon premium requirements for the forthcoming policy year (as already reported to Members in Circular No. 23/07 of November 21, 2007), your Board considered a number of other issues relevant to the American Club's funding.

The purpose of this Circular is to inform Members of the decisions which your Board reached in relation to these matters.

Development of open policy years

2004

This year continues to develop in substantial surplus which, although not as large as that which appeared to be emerging some months ago, nevertheless represents a significantly positive contribution to the Club's overall financial position.

Your Board has resolved that this year should be closed as of September 30, 2007 without further call in excess of the original forecast and the surplus allocated to the Club's contingency fund subject to the proviso discussed under the separate heading as to closure below.

The release call margin for the year is now set at zero.

2005

This year continues to develop in respectable surplus. No further call is expected in excess of that already made to date, save to the extent discussed later in this Circular as to surplus enhancement. Current expectations are that 2005 will be capable of closure,



barring unforeseen eventualities, in approximately twelve months from now, without additional calls in excess of those already levied or as described below.

The release call margin for the year is as set out in the summary section below.

2006

This year has unfortunately undergone substantial deterioration over the last twelve months, much of it driven by the unprecedented level of Pool claims experienced by the International Group of P&I Clubs over this period. A large part of the negative development of the Pool emerged during the first half of 2007, as did some deterioration of the Club's retained exposure, although to a more limited degree.

Although there are grounds for cautious optimism that 2006 may improve over time as more investment income is allocated to the year and IBNR is reduced as claims mature, your Board is of the view that it would be sensible to cure this continuing deficit by levying an additional supplementary call of 15% of qualifying advance calls for the year.

This call will fall due for payment in one installment on May 20, 2008. The year will remain open subject to further notice as to closure in due course and subject to the provision for a surplus enhancement call as described below.

The release call margin for the year is as set out in the summary section below.

2007

This policy year is currently exhibiting a deficit of just over \$6 million. Retained claims for the year seem to be tracking those of 2004, although the development of claims within the International Group Pool remains problematic.

At August 20, 2007, the current year looked worse than the 2006 policy year at the same stage i.e. after 6 months' development. While it is possible that Pool claims for 2007 may develop more favorably than present indications suggest, it is only prudent to assume that the ultimate outturn for 2007 will be similar to the levels of exposure sustained in 2006.

Notwithstanding this, and while the investment markets remain fragile, it is hoped that investment earnings may substantially reduce the apparent deficit over time.

Accordingly, your Board is of the view that no further call should be made in regard to this policy year at this point (subject, however, to the surplus enhancement call discussed in the next section), although the position will be closely monitored over the next six to nine months and any change in the ultimate prognosis for the year notified to Members accordingly.



The release call margin for the year is as set out in the summary section below.

Settlement of the Declaratory Judgment Action concerning closed year occupational disease claims and the enhancement of Club surplus

Members will be pleased to learn that a settlement has recently been agreed between the American Club and those parties impleaded as defendants in the Declaratory Judgment Action in regard to pre-1989 closed year occupational disease claims commenced at the end of May, 2004 and notified to Members in Circular No. 14/04 of June 7, 2004.

The settlement benefits all concerned since the compromising of disputed issues results in substantial savings in litigation expenses and avoids the risk of trial.

While the terms of the settlement are confidential, it can nevertheless be said that it provides for limited annual payments to the defendants on a pre-agreed basis. This benefits the Club's current and future Members by optimizing cash flow in settlement of such claims over the years ahead.

The settlement will, however, entail charges to the Club's surplus under the rules of statutory and GAAP accounting. Consequently, and as part of its general desire to increase surplus, your Board has determined to levy a surplus enhancement call of 5% on all open years. This, in parallel with the manner in which claims will be paid in accordance with the settlement, will substantially benefit the Club's future liquidity.

Closure of the 2004 policy year

This has already been mentioned above.

So far as the call for surplus enhancement purposes as mentioned in the prior section is concerned, part of the surplus for the 2004 policy year will be allocated specifically to satisfy the 5% call required on all open policy years and, in addition, a further \$500,000 from the overall surplus will be earmarked as an IBNR allowance for potential occupational disease claims for that year specifically. The effect of this is to obviate the need to charge a further surplus enhancement call for 2004.

Summary

The foregoing can be summarized as follows.

2004

- Year to be closed as of September 30, 2007 without further call.

- 5% surplus enhancement call to be defrayed from overall surplus for the year and allocated as such as part of the transfer to the Club's contingency fund on closure.
- Release call margin reduced to zero.

2005

- Surplus enhancement call of 5% to be levied on all mutual entries, payable on May 20, 2008.
- Release call on mutual entries to be 10% of advance call premium over and above the 5% surplus enhancement call i.e. 15% of advance call overall.

2006

- Further supplementary call of 15% on all mutual entries to be levied to assist in curing deficit for the year, payable on May 20, 2008.
- Additional surplus enhancement call of 5% to be levied on all mutual entries, again to be payable on May 20, 2008.
- Release call on mutual entries to be 10% of advance call premium over and above the supplementary and surplus enhancement calls mentioned above, i.e. 30% of advance call overall.

2007

- Surplus enhancement call of 5% to be made on all mutual entries payable on May 20, 2008.
- Release call on mutual entries to be 25% over and above surplus enhancement call, i.e. 30% of advance call overall.

The future

Your Board has identified the need to improve the American Club's level of capital adequacy as a matter of paramount importance. This remains the Club's greatest priority as it continues to increase its financial strength to meet the challenges of the future. The Club's investment portfolio, subject of course to market risk, is at an all time high. Its five year pure underwriting results – even disregarding additional calls – place the American Club second among the International Group of thirteen and third from the top in combined loss ratio.



The American Club has made admirable progress in consolidating its capabilities to be a leading service provider in the P&I field. Its historical posture in regard to balance sheet funding has, however, challenged the development of free reserves in recent years. The solution is to build a solid capital base. Accordingly, the Club has a clear policy to focus on this issue as a key driver for future success. The settlement of the Declaratory Judgment Action is an important component in the fulfillment of the Club's aims in this respect.

In seeking to build the Club's capital, your Board is aware that price and other cost increases are never welcome. The Club nevertheless counts on the support of Members, business associates and its many other friends in achieving the important financial goals it has set itself for the years ahead.

Yours faithfully,

Joseph E.M. Hughes, Chairman & CEO
Shipowners Claims Bureau, Inc., Managers for
THE AMERICAN CLUB