SCOTTISH and YORK 1983 Annual Report

Board of Directors

R. D. ABBOT
R. W. BROUGHTON
S. F. CHAPMAN
I. D. CROFT
W. G. HOLBROOK
ST. CLAIR McCABE
A. D. McEWEN
K. R. THOMSON
J. A. TORY

Officers

R. W. BROUGHTON — *Chairman of the Board and Chief Executive Officer*
W. G. HOLBROOK — *President and Chief Operating Officer*
R. D. ABBOT — *Vice-President and Secretary-Treasurer*
D. A. BOYD — *Vice-President*

Transfer Agent

MONTREAL TRUST COMPANY

Auditors

THORNE RIDDELL

Bankers

THE ROYAL BANK OF CANADA

Executive Office

150 EGLINTON AVENUE EAST, TORONTO, CANADA

SCOTTISH & YORK HOLDINGS LIMITED

To The Shareholders

I am pleased to report that net income for the year ended December 31, 1983 was $6.1 million compared to $5.9 million for 1982. This result was achieved in an unusual and difficult operating environment.

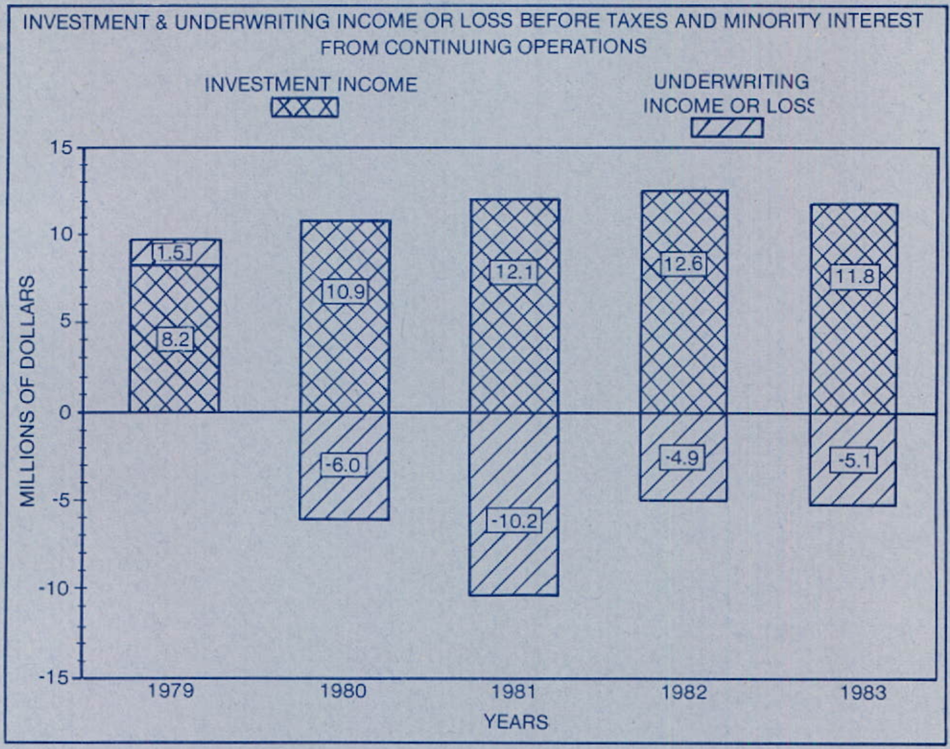
For the past four years the property and casualty insurance industry has had to cope with severe price competition, particularly in commercial lines, resulting from high interest rates and excess capacity in the insurance market place. High interest rates encourage companies to lower rates in order to obtain new premium dollars to invest until claims are paid. So long as high interest rates prevail, investment income earned tends to offset underwriting losses which result from setting premium levels too low. This approach has led insurers to expand their books of what is already unprofitable business and has attracted many new companies into the insurance field. The relaxation of underwriting standards in the former case and lack of underwriting experience in the latter have resulted in escalating claims and underwriting losses.

Many companies are now in a quandry since a unilateral increase in rates will result in an immediate loss of business and cash flow, but a failure to increase rates can only lead to continuing losses.

While commercial property and liability business was severly underpriced in 1983, changes in the reinsurance marketplace which appeared late last year could have a favourable impact on commercial rate levels later this year. Personal lines, which were not subject to the severe rate pressure, continued to be profitable in 1983 and we will be seeking additional market penetration in 1984.

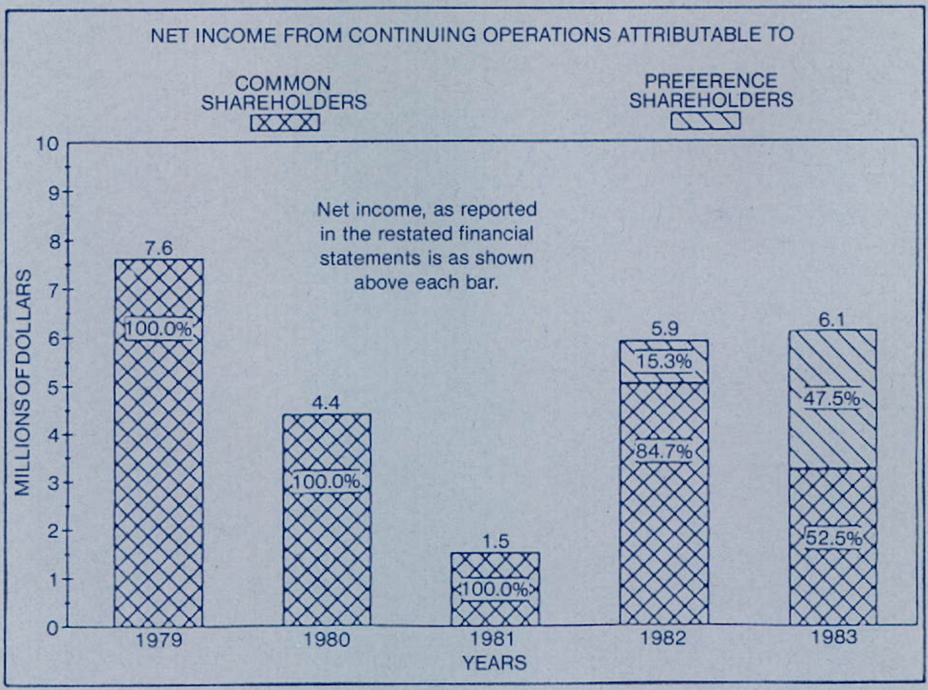
In 1983, Scottish & York's overall underwriting results deteriorated slightly from the previous year due primarily to adverse development in the fourth quarter on a particular professional liability pool and on reinsurance assumed in Canada. Corrective action has been taken by discontinuance of the former and a drastic reduction of our volume of the latter.

In common with other property/casualty insurance companies, investment income has become the main source of our profits and for the past four years has been the only source. In 1983 interest rates fell from their staggering heights of 1982, with the result that our overall investment income fell, even though invested assets grew. The five year history of our underwriting income or loss and of investment income (before taxes and minority interest) is as follows:



The preference shares issued in September of 1982 to The Standard St. Lawrence Company Limited entitle the holder to dividends at the rate of one-half the prime rate charged by The Royal Bank of Canada plus 1%. The company has elected to pay such dividends in the form of additional preference shares. Since the shares were only outstanding for a single quarter in 1982, the dollar equivalent of the stock dividends amounted to approximately $897,000, while for the full year 1983 the amount was $2.9 million. Although such dividends require a transfer from the Retained Earnings/Deficit account to the Capital Stock account, no outflow of cash is suffered by the company.

The net income from continuing operations of the company for each of the past five years, and the portion attributable to the common shareholders is as shown on the following chart:



It is our belief that adherence to credible underwriting standards resulting in a return to profitable underwriting is essential and best serves the long term interests of both our policyholders and shareholders. Our efforts in 1984 will be directed toward an improved underwriting result.

On behalf of the Board of Directors, I would like to express our thanks to our many clients for their continued support and to our staff for their dedication and hard work.

For the Board of Directors

R.W. Broughton

R.W. BROUGHTON
Chairman of the Board and
Chief Executive Officer.

SCOTTISH & YORK HOLDINGS LIMITED
(Incorporated under the laws of Ontario)

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1983

ASSETS

	1983	1982
Cash	$ 307,694	$ 3,056,665
Marketable securities		
Term deposits	42,611,902	48,868,459
Bonds (market value 1983, $38,242,578; 1982, $29,035,719)	41,267,865	32,382,220
Stocks (market value 1983, $7,601,879; 1982, $7,585,414)	7,922,786	9,254,112
Accrued interest on bonds and term deposits	2,849,122	2,429,183
Accounts receivable	38,952,744	33,050,602
Notes receivable (note 3)	4,685,166	2,157,773
Income taxes recoverable	241,700	636,375
Fixed assets (note 5)	867,373	545,209
Marketing agreement, net of amortization	630,000	665,000
	$140,336,352	$133,045,598

Approved by the Board

W.G. HOLBROOK, Director
R.D. ABBOT, Director

LIABILITIES

	1983	1982
Accounts payable and accrued liabilities	$ 15,636,350	$ 18,931,624
Provision for outstanding claims	69,147,198	63,101,171
Income and premium taxes payable	1,145,788	4,227,085
Deferred revenue	19,721,691	18,083,773
Interest of minority shareholders (note 7)	8,450	132,546
	105,659,477	104,476,199

SHAREHOLDERS' EQUITY

Capital stock (note 8)		
Authorized		
6,000,000 Class A floating rate preference shares		
250,000 Class B floating rate preference shares		
50,000,000 Common shares		
Issued		
4,200,000 Class A preference shares	42,000,000	42,000,000
34,545 Class B preference shares	3,454,500	
8,000,000 Common shares	3,701,000	3,701,000
Deficit	(14,478,625)	(17,131,601)
	34,676,875	28,569,399
	$140,336,352	$133,045,598

Commitments (note 9)

SCOTTISH & YORK HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF INCOME
YEAR ENDED DECEMBER 31, 1983

	1983	1982
Net premiums written and other income (note 11)	$71,333,071	$ 87,229,186
Underwriting loss	$(5,061,178)	$ (4,905,776)
Investment income	11,779,127	12,560,103
Income before undernoted items	6,717,949	7,654,327
Income taxes	593,312	1,741,125
	6,124,637	5,913,202
Interest of minority common shareholders of subsidiary companies (note 7)	16,700	43,787
Income from continuing operations	6,107,937	5,869,415
Losses from operations no longer consolidated (note 2)		(49,751,400)
NET INCOME (LOSS)	6,107,937	(43,881,985)
Dividends on preference shares (note 8)	2,921,602	896,700
EARNINGS (LOSS) ATTRIBUTABLE TO COMMON SHAREHOLDERS	$ 3,186,335	$ (44,778,685)
EARNINGS (LOSS) PER SHARE		
Earnings per common share from continuing operations	$ .40	$ .62
Earnings (loss) per common share	$ .40	$ (5.60)

CONSOLIDATED STATEMENT OF RETAINED EARNINGS (DEFICIT)
YEAR ENDED DECEMBER 31, 1983

	1983	1982
RETAINED EARNINGS (DEFICIT) AT BEGINNING OF YEAR	$(17,131,601)	$26,750,384
Net income (loss)	6,107,937	(43,881,985)
Dividends (note 8)	(3,454,961)	
DEFICIT AT END OF YEAR	$ 14,478,625	$17,131,601

SCOTTISH & YORK HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
YEAR ENDED DECEMBER 31, 1983

	1983	1982
CASH PROVIDED		
Income from continuing operations	$ 6,107,937	$ 5,869,415
Items not involving cash		
Depreciation and amortization	213,596	222,765
Amortization of marketing agreement	35,000	35,000
Interest of minority common shareholders of subsidiary companies		43,787
Increase in deferred revenue	1,637,918	2,443,548
Increase in provision for outstanding claims	6,046,027	2,539,435
Increase (decrease) in accounts payable and accrued liabilities	(3,295,274)	9,818,517
Increase (decrease) in income and premium taxes payable, net	(2,686,622)	2,763,338
Decrease (increase) in accounts and notes receivable	(6,322,081)	8,946,560
Cash provided from continuing operations	1,736,501	32,682,365
Proceeds from sale of fixed assets	16,770	
Proceeds from issuance of preference shares	8,450	42,000,000
Sale of marketable securities, net		
Stocks	1,331,326	1,411,973
Bonds		1,390,526
Decrease in term deposits	6,256,557	
	9,349,604	77,484,864
CASH APPLIED		
Investment in Scottish & York Inc.		46,860,286
Purchase of marketable securities, net – bonds	8,885,645	
Purchase of minority interest in common shares	132,546	
Increase in term deposits		25,851,537
Acquisition of subsidiary		2,591,000
Increase in notes receivable	2,527,393	
Purchase of fixed assets, net	552,530	336,795
Dividends on preference shares relating to fractional shares	461	
Marketing agreement		700,000
	12,098,575	76,339,618
INCREASE (DECREASE) IN CASH	(2,748,971)	1,145,246
CASH AT BEGINNING OF YEAR	3,056,665	1,911,419
CASH AT END OF YEAR	$ 307,694	$ 3,056,665

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEAR ENDED DECEMBER 31, 1983

1. ACCOUNTING POLICIES

The consolidated financial statements have been prepared in conformity with generally accepted accounting principles and with respect to the subsidiary insurance companies differ in some respects from statutory accounting practices followed in the preparation of financial statements submitted to regulatory authorities.

(a) Basis of consolidation

The consolidated financial statements include all subsidiary companies, after reflecting the events described in note 2 and note 7:

Canada
- Scottish & York Insurance Co. Limited
- Central Canada Insurance Service Limited
- Victoria Insurance Company of Canada
- Eaton Bay Insurance Company

Bermuda
- Scottish International Insurance Co. Ltd.

Netherlands
- Scottish & York B.V.

Netherlands Antilles
- Scottish & York N.V.

As at December 31, 1983, all of these subsidiaries are 100% owned.

(b) Translation into Canadian Dollars

The accounts of subsidiary companies have been translated into Canadian dollars on the following basis:

(i) assets and liabilities of a monetary nature at the rate of exchange prevailing at December 31,

(ii) all other assets and liabilities at the rate of exchange prevailing at the date the assets were acquired or the liabilities incurred,

(iii) income and expenses at the average rate for the year.

Foreign currency gains and losses are included in income when realized.

(c) Marketable securities

(i) Term deposits are recorded at cost.

(ii) Bonds are recorded at cost.
Interest income is recorded on an accrual basis.

(iii) Stocks are recorded at cost.
Dividend income is recorded on a cash received basis.

(iv) Gains and losses on disposal of investments are included in investment income.

(d) Fixed assets

Fixed assets are recorded at cost, less accumulated depreciation and amortization. Fixed assets are depreciated over their useful lives on the following basis:

Data processing equipment and computer software are depreciated on a straight line basis over a maximum of 5 years.

Automobiles are depreciated at the rate of 30% reducing balance basis.

Furniture and fixtures are depreciated at the rate of 20% reducing balance basis.

Leasehold improvements are amortized on a straight line basis over a maximum of 5 years.

(e) Marketing agreement

The company is amortizing the marketing agreement with Eaton Bay Financial Services Limited over twenty years from 1982, the date of acquisition.

(f) Deferred Revenue

(i) Policy acquisition costs, net of reinsurance allowances, are deferred and amortized over the terms of the related policies.

For the years 1983 and 1982 deferred commission income exceeds deferred acquisition costs. Accordingly, the net credit balance is included in deferred revenue.

(ii) Premium income is deferred until it is earned. The basis for taking premiums into income is prescribed by the regulating authorities under which the companies operate.

(g) Provision for outstanding insurance claims

The liabilities for outstanding insurance claims and related adjustment expenses are determined using case basis evaluations plus a provision for unreported claims and are estimates of the ultimate net cost of all insurance claims incurred through December 31, 1983.

Since the provisions are necessarily based on estimates of future trends in claim severity and frequency and other factors, which could vary as the claims are settled, the ultimate liability may be more or less than the estimated amounts. These liabilities have been stated net of reinsurance recoverable from other companies. Although it is not possible to measure the degree of variability inherent in such estimates, management believes that the liabilities for insurance claims and related adjustment expenses are adequate. The estimates are continually reviewed and, as adjustments to these liabilities become necessary, they are reflected in current operations.

2. INVESTMENT IN SCOTTISH & YORK, INC.

During the year, Scottish & York, Inc. ("S&YI"), formerly a wholly owned U.S. subsidiary, reorganized its share capital in a manner which transferred voting control of S&YI to The Standard St. Lawrence Company Limited ("Standard St. Lawrence"), the company's major shareholder. The company continues to hold indirectly through Scottish & York B.V. all of the 100 issued common shares of S&YI and to hold directly the preferred shares of S&YI which were acquired in 1982 at a cost of approximately $42,000,000. These investments were written down to a nil value in 1982.

Standard St. Lawrence subscribed for 400 voting redeemable preferred shares of S&YI at a price of 1¢ each. These shares are entitled to three votes each at meetings of shareholders and are redeemable by S&YI at a price equal to the amount paid up thereon. The common shareholders of S&YI have the right under the share conditions attaching to the reorganized share capital of S&YI to require such redemption to be made at any time. At present, all of the common shares are held by Scottish & York B.V., a wholly owned subsidiary of the company.

In addition, S&YI authorized a new class of non-voting redeemable and retractable preference shares which are entitled to cumulative dividends at a rate equal to the U.S. prime rate from time to time. On redemption or retraction the holder is entitled to the amount paid up on each share plus accrued but unpaid dividends. These shares are issued when additional capital is required by S&YI or its subsidiaries and such shares are subscribed for by Standard St. Lawrence. The parties have entered into an agreement under which Scottish & York B.V. will agree not to cause the redemption of the voting preferred shares unless all of these preference shares have been redeemed by S&YI or acquired by the company. At December 31, 1983, 18,600 of such shares had been issued at a price of U.S. $1,000 per share.

The agreement also requires the continued involvement of officers of Scottish & York Holdings Limited in the supervision of the operations of S&YI.

As a result of the foregoing, the company no longer consolidates the financial statements of the companies in the S&YI group.

For 1982, losses related to the S&YI group were accounted for on the equity basis.

3. NOTES RECEIVABLE

Prior to the reorganization of the capital stock of Scottish and York Inc. (S&YI) referred to in note 2, the company had made non-interest bearing advances to S&YI. The company is of the opinion that these amounts will be repaid in due course.

4. ACQUISITION OF SUBSIDIARY

Effective January 5, 1982 the company acquired for cash 100% of the outstanding shares of Eaton Bay Insurance Company.

The transaction was accounted for on the purchase method with the results of operations included in these financial statements from the date of acquisition.

The purchase agreement provides that to the extent that loss development on claims arising prior to January 1, 1982 exceeds the claims reserves established at that date, the company will be indemnified. To December 31, 1983 the company has been reimbursed in the amount of $1.3 million.

In addition the purchase agreement requires the company to make payments equal to one-half of the amount by which Eaton Bay Insurance Company's future income taxes are reduced by non-capital losses which under the terms of the agreement include timing differences attributable to loss provisions incurred prior to December 31, 1981. As at December 31, 1981, the potential tax benefit of the loss carry forward amounted to approximately $2.4 million.

5. FIXED ASSETS

	1983	1982
Leasehold improvements	$ 101,956	$ 96,766
Furniture and fixtures	320,659	331,955
Data processing equipment and software	811,102	365,458
Automotive equipment	131,947	103,180
	1,365,664	897,359
Less accumulated depreciation and amortization	498,291	352,150
	$ 867,373	$545,209

Depreciation and amortization charged to income was $213,596 and $222,765 in 1983 and 1982, respectively.

6. INCOME TAXES

At December 31, 1983 the company has the following losses available to reduce future years' income for tax purposes, the effect of which has not been recorded in the accounts:

Available until 1986	$ 674,000
Available until 1987	58,000
Available until 1988	277,000
	$1,009,000

In addition $4.8 million relating to loss provisions and deferred revenue recorded in these accounts are available to reduce future years' taxable income.

7. MINORITY INTEREST

On August 19, 1983, common shares of Scottish & York Insurance Co. Limited, Victoria Insurance Company of Canada and Eaton Bay Insurance Company held by the directors were purchased by Scottish & York Holdings Limited for $132,546.

Preference shares of the subsidiary companies were issued to directors of the subsidiary companies for cash consideration totalling $8,450.

8. CAPITAL STOCK

Class A Floating Rate Preference Shares

The holders of Class A preference shares are entitled to receive cumulative dividends at a rate of one-half the prime rate charged by The Royal Bank of Canada plus 1%. Dividends are payable, at the option of the directors, either in cash or by way of stock dividends in Class B shares. These shares are retractable at the holders' option on September 1, 1987 at the price of $10 per share plus accrued and unpaid dividends. The shares are redeemable at the Company's option at a price equal to $10 per share plus accrued and unpaid dividends.

Class B Floating Rate Preference Shares

The holders of Class B preference shares are entitled to receive cumulative dividends at a rate of one-half the prime rate charge by The Royal Bank of Canada plus 1%. These shares are retractable at the holders' option on September 1, 1987 at the price of $100 per share plus accrued and unpaid dividends. The shares are redeemable at the Company's option at a price equal to $100 per share plus accrued and unpaid dividends.

Dividends on preference shares attributable to 1983 have been calculated as follows:

Stock dividends in class B preference shares	$3,454,500
Cash in lieu of fractional shares on stock dividends	461
Dividends paid during year	3,454,961
Dividends accrued to December 31, 1982	(896,700)
Dividends accrued to December 31, 1983	363,341
Dividends on preference shares attributable to 1983	$2,921,602

9. COMMITMENTS

Cash and short-term deposits in the amount of $26,486,658 (1982 – $25,318,717) are assigned as security against letters of credit totalling $25,897,905 (1982–$25,318,717) issued to ceding insurance companies to secure liabilities.

The company leases certain office space under a lease agreement expiring in 1992 with an option to extend this to 2002. The following is a schedule of future minimum lease payments for the lease:

Year ending December 31,	
1984	$ 572,389
1985	597,276
1986	597,276
1987	642,049
1988	776,368
1989 to remainder of lease term	2,911,380
	$6,096,738

10. SEGMENTED INFORMATION

The company operates solely in the property and casualty insurance industry and conducts business in two geographic areas - Canada
- Bermuda and Other.

	1983			1982		
	Canada	Bermuda and Other	Consolidated	Canada	Bermuda and Other	Consolidated
		(000's omitted)			(000's omitted)	
Total assets	$ 78,908	$ 61,428	$140,336	$ 81,034	$ 52,012	$133,046
Revenue	$ 29,866	$ 41,467	$ 71,333	$ 34,740	$ 52,489	$ 87,229
Operating income from continuing operations	$ 1,948	$ 4,269	$ 6,217	$ 266	$ 5,900	$ 6,166
General corporate expenses			109			297
Income from continuing operations			$ 6,108			$ 5,869

11. NET PREMIUMS WRITTEN AND OTHER INCOME

For 1983 the company determined gross revenue on the basis of net retained premiums rather than on gross premiums written.
The 1982 comparative figures have been restated to conform with this method of presentation.

Auditors' Report

To the Shareholders of
Scottish & York Holdings Limited

We have examined the consolidated balance sheet of Scottish & York Holdings Limited as at December 31, 1983 and the consolidated statements of income, retained earnings (deficit) and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1983 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
March 5, 1984

THORNE RIDDELL
Chartered Accountants

SCOTTISH & YORK HOLDINGS GROUP

Five Year Performance Record of Continuing Operations

(SEE NOTE 2 TO THE FINANCIAL STATEMENTS)

YEAR	NET PREMIUMS WRITTEN	DEFERRED REVENUE	INCOME BEFORE TAXES AND MINORITY INTEREST	INCOME TAXES	NET INCOME FROM CONTINUING OPERATIONS	EARNINGS PER SHARE FROM CONTINUING OPERATIONS	DIVIDENDS PAID PER COMMON SHARE
1983	$59,553,944	$19,721,691	$6,717,949	$ 593,312	$6,107,937	*40¢	—
1982	74,669,083	18,083,773	7,654,327	1,741,125	5,869,415	*62¢	—
1981	32,099,641	13,944,225	1,903,696	464,037	1,490,611	19¢	16.0¢
1980	35,953,921	10,516,932	4,920,399	497,894	4,418,609	55¢	30.0¢
1979	34,538,516	10,175,577	9,686,238	2,046,906	7,625,108	95¢	24.0¢

*After giving effect to the accrual of dividends on the Floating Rate Preference Shares