



SCOTTISH and YORK
1980
Annual Report

HOWARD ROSS LIBRARY
OF MANAGEMENT
MAY 27 1981
MCGILL UNIVERSITY

Board of Directors

R. D. ABBOT
R. W. BROUGHTON
S. F. CHAPMAN
K. H. DOYLE
W. G. HOLBROOK
M. LANDIS
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*
S. F. CHAPMAN — *Vice-President — Finance*
J. A. TORY — *Vice-President*
D. A. BOYD — *Vice-President*

Transfer Agent

MONTREAL TRUST COMPANY

Auditors

THORNE RIDDELL & CO.

Bankers

THE ROYAL BANK OF CANADA

Executive Office

155 UNIVERSITY AVENUE, TORONTO, CANADA

SCOTTISH & YORK HOLDINGS LIMITED

To The Shareholders

The year 1980 posed a dilemma for most property-casualty insurers in North America. Preliminary figures indicate that the industry experienced the second worst underwriting loss ever while at the same time setting a new record for investment income.

Considering the difficult operating environment encountered throughout the year the overall results of your Company for 1980 were satisfactory. Substantial growth in revenue was achieved with gross written premiums increasing by 30.8% from \$134,727,478 to \$176,336,067 while net premiums rose 16.3% from \$82,682,297 to \$96,142,936. Investment income was also at a record level at \$20,864,187 up from the previous high of \$14,429,687 reached in 1979. Intense competition coupled with continued inflationary pressures contributed to an underwriting loss of \$9,432,933 compared to an underwriting profit of \$1,075,424 for the previous year. As a result, net income declined to \$7,163,678 or 90¢ per common share in 1980 compared to \$10,362,235 or \$1.30 per common share in 1979.

Two dividend increases were approved by the Directors of your Company during 1980. Total dividends paid during the year amounted to \$2,400,000 or 30¢ per common share, up 25% from a year earlier.

A number of corporate developments have taken place during the past twelve months. The income tax assessment against your Company's wholly owned Bahamian reinsurance subsidiary, Victoria Insurance Company Limited, was finally settled. The basis of settlement was payment of the tax and accrued interest for the year 1968 amounting in total to \$520,000. Revenue Canada has abandoned its appeal to the Federal Court with respect to the years 1969 and 1970. This settlement has been reflected in the 1980 financial statements as a prior year adjustment and did not affect earnings for 1980.

In May, 1980 ground was broken for our new United States Home Office building located on U.S. Route 1 near Princeton, New Jersey. This building, which will be ready for occupancy by late this summer, is approximately 120,000 square feet in size. It will enable us to consolidate our Home Office and North Eastern Region operations which are presently spread over four locations, and will provide adequate room for future growth.

On April 6th, 1981 it was announced that Scottish & York International Insurance, Inc., our 80% owned United States subsidiary, had reached agreement in principle to acquire Tri-American Corporation. Tri-American is an Ohio Corporation whose shares are traded in the over-the-counter market and quoted on the NASDAQ. Its executive offices are located in Pepper Pike, (Cleveland) Ohio. It is principally engaged in writing non-standard risk automobile policies at surcharged rates through its wholly-owned subsidiary, Globe American Casualty Company.

The value of the transaction, which contemplates acquisition of 100% of Tri-American through a tender offer followed by a cash merger, will be approximately \$12,000,000 U.S., all of which will be provided from internally generated funds. On April 16th, 1981 Scottish & York International Insurance commenced a tender offer for all the outstanding shares of Tri-American. This offer is conditional on not less than 390,000 shares being tendered in addition to the shares in respect of which an option has been obtained from management and their associates. If the above minimum number of shares is tendered we will be in a position to acquire over 51% of the outstanding shares, including shares reserved for issuance on exercise of outstanding warrants and employee options. The offer is scheduled to expire May 14th, 1981 unless extended.

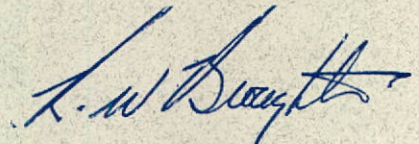
We are very excited about this proposed acquisition. Tri-American has an established and profitable track record in a class of business in which we are not presently engaged and could provide new marketing outlets for our other products lines in the United States.

The improvements to our data processing system in the United States referred to in our annual report for last year are substantially in place and operating satisfactorily. We have recently made commitments to bring our Canadian operations onto a combined "on line" and "batch" data system which, when fully operational in 1982, should greatly enhance our ability to respond to our clients' needs in a more efficient manner. It is our view that the substantial investment in terms of human and financial resources now being made in improving our data processing systems in both Canada and the United States and in acquiring our own office building in the United States will have a very stabilizing effect on overhead as we continue to grow.

It appears that the malaise suffered by the general insurance industry will continue for at least the balance of this year. The effects of inflation and overcapacity will make it difficult for us to achieve an underwriting profit. However, curtailment of certain unprofitable lines during 1980 coupled with rate increases in others early this year should have a positive effect on our underwriting results for 1981. Gross written premiums are expected to exceed \$200,000,000 reflecting our increased market penetration and expanded marketing facilities. Investment income, at current rates of return, should show continued improvement.

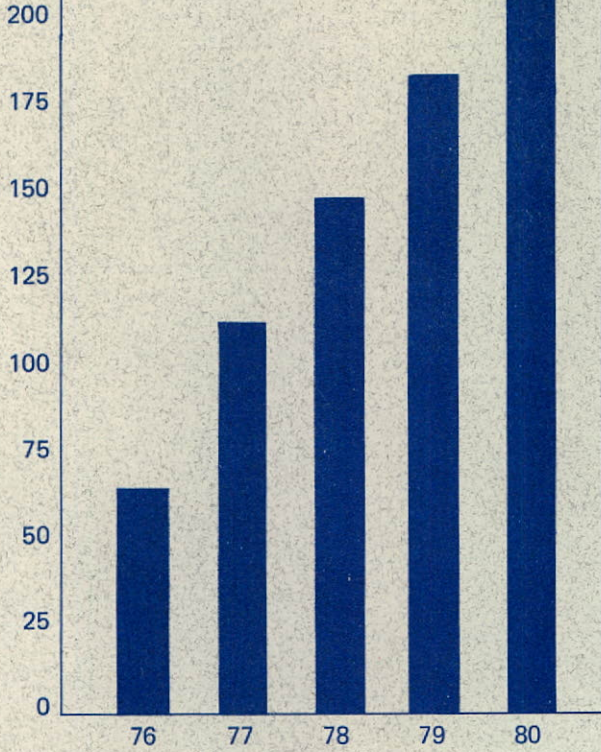
On behalf of the Board I would like to express our thanks to all our employees for their many accomplishments in 1980. Their skill and dedication in a year of many challenges was most gratifying.

For the Board of Directors

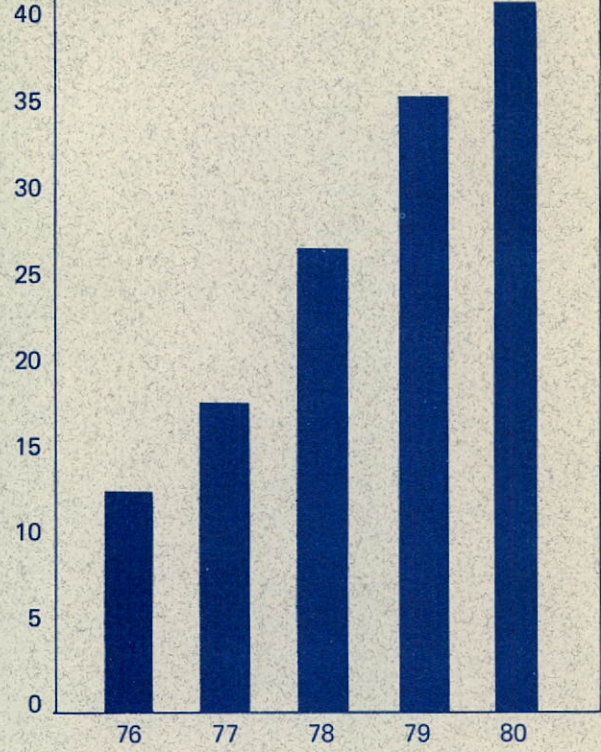
A handwritten signature in dark ink, appearing to read "R.W. Broughton", with a stylized flourish at the end.

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

ASSETS
(MILLIONS)

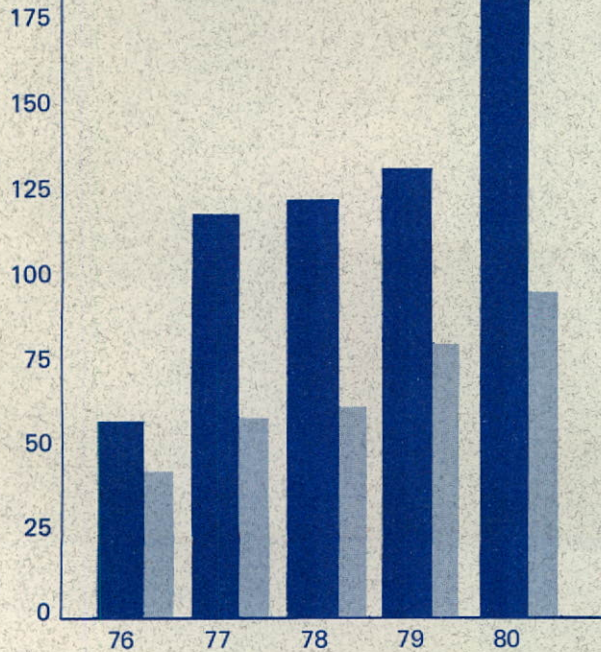


EQUITY
(MILLIONS)

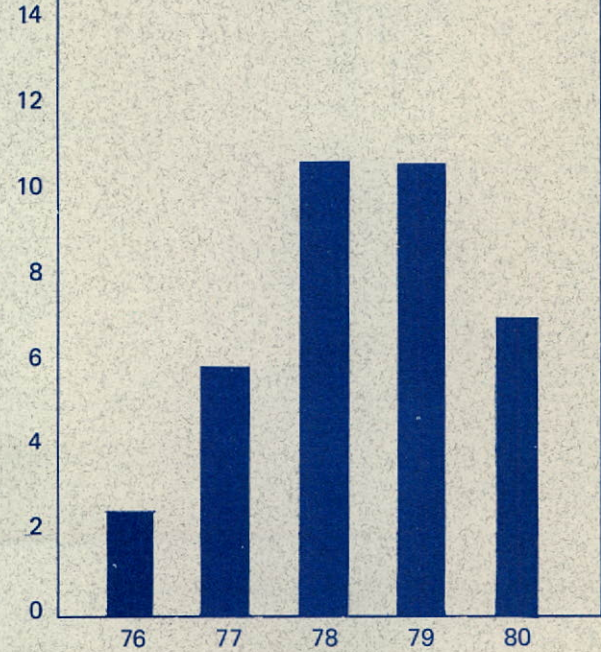


PREMIUMS WRITTEN
(MILLIONS)

GROSS 
NET 



NET INCOME
(MILLIONS)



SCOTTISH & YORK HOLDINGS LIMITED

(Incorporated under the laws of Ontario)

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1980

ASSETS

	<u>1980</u>	<u>1979</u>
Cash	\$ 4,036,525	\$ 2,036,796
Marketable securities (note 1)		
Term deposits	27,015,775	18,687,174
Bonds (market value 1980, \$92,190,101; 1979, \$87,004,228)	105,746,746	94,288,446
Stocks (market value 1980, \$27,212,846; 1979, \$23,098,603)	25,968,077	21,937,773
Accrued interest on bonds and term deposits	3,024,309	2,167,244
Accounts and notes receivable	42,828,923	44,268,808
Property and equipment (note 2)	5,646,419	920,523
Premium paid on acquisition of shares of subsidiary companies, net of amortization of \$300,944; 1979, \$229,725	1,537,000	1,371,919
	<u>\$215,803,774</u>	<u>\$185,678,683</u>

Approved by the Board

W. G. HOLBROOK, Director

R. D. ABBOT, Director

LIABILITIES

	<u>1980</u>	<u>1979</u>
Notes payable (note 3)	\$ 21,679,407	\$ 16,082,000
Accounts payable and accrued liabilities	13,613,967	16,898,386
Provision for outstanding claims	104,148,719	86,055,494
Income and premium taxes payable	2,706,386	2,795,360
Deferred revenue	27,978,296	24,373,278
Obligations under capital leases (note 2)	870,492	
Interest of minority common shareholders of subsidiary companies	4,320,740	3,752,076
	<u>175,318,007</u>	<u>149,956,594</u>

SHAREHOLDERS' EQUITY

Capital Stock		
Authorized		
10,000 First preference shares, par value \$50 each, issuable in series		
12,000,000 Common shares without par value		
Issued		
8,000,000 Common shares	3,701,000	3,701,000
Retained earnings	36,784,767	32,021,089
	<u>40,485,767</u>	<u>35,722,089</u>
	<u>\$215,803,774</u>	<u>\$185,678,683</u>

Contingent liabilities and contractual
commitments (note 4)
Subsequent event (note 8)

SCOTTISH & YORK HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF INCOME

YEAR ENDED DECEMBER 31, 1980

	<u>1980</u>	<u>1979</u>
Gross premiums written and other income	\$197,200,254	\$149,157,165
Underwriting profit (loss)	\$ (9,432,933)	\$ 1,075,424
Investment income	20,864,187	14,429,687
	<u>11,431,254</u>	<u>15,505,111</u>
Interest on notes payable	1,961,287	1,275,986
Income before undernoted items	9,469,967	14,229,125
Income taxes	1,465,056	3,028,003
Income before minority interest	8,004,911	11,201,122
Interest of minority common shareholders of subsidiary companies	841,233	838,887
NET INCOME	<u>\$ 7,163,678</u>	<u>\$ 10,362,235</u>
Earnings per share	<u>\$.90</u>	<u>\$ 1.30</u>

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

YEAR ENDED DECEMBER 31, 1980

	<u>1980</u>	<u>1979</u>
BALANCE AT BEGINNING OF YEAR		
As previously reported	\$ 32,541,089	\$ 24,098,854
Adjustment of prior years' income taxes (note 4(a)) ...	520,000	520,000
As restated	<u>32,021,089</u>	<u>23,578,854</u>
Net income	7,163,678	10,362,235
	<u>39,184,767</u>	<u>33,941,089</u>
Dividends on common shares	2,400,000	1,920,000
BALANCE AT END OF YEAR	<u>\$ 36,784,767</u>	<u>\$ 32,021,089</u>

SCOTTISH & YORK HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION YEAR ENDED DECEMBER 31, 1980

	<u>1980</u>	<u>1979</u>
RESOURCES PROVIDED		
Operations (as outlined below)	\$27,367,580	\$14,547,093
Decrease in term deposits		3,772,350
Proceeds from notes payable	19,047,807	6,101,308
Obligations under capital leases	870,492	
Decrease in cash		294,867
	<u>\$47,285,879</u>	<u>\$24,715,618</u>
RESOURCES APPLIED		
Increase in cash	\$ 1,999,729	
Increase in term deposits	8,328,601	
Purchase of marketable securities, net		
Bonds	11,458,300	\$ 9,194,932
Stocks	4,030,304	11,514,345
Notes payable	13,450,400	1,134,500
Purchase of property and equipment, net	5,020,703	505,515
Increase in premium paid on acquisition of shares of subsidiary companies (note 1(a))	236,299	113,319
Dividends on common shares	2,400,000	1,920,000
Net change in other assets and liabilities	361,543	333,007
	<u>\$47,285,879</u>	<u>\$24,715,618</u>
Operations		
Net income	\$ 7,163,678	\$10,362,235
Items not involving cash		
Depreciation	294,807	164,600
Amortization of premium paid on acquisition of shares of subsidiary companies (note 1(e))	71,218	43,992
Interest of minority common shareholders of subsidiary companies	841,233	838,887
Increase in deferred revenue	3,605,018	2,997,870
Increase in provision for outstanding claims	18,093,225	30,413,863
Decrease in accounts payable and accrued liabilities	(3,284,419)	(15,011,255)
(Increase) decrease in accounts and notes receivable and accrued interest	582,820	(15,263,099)
Resources provided from operations	<u>\$27,367,580</u>	<u>\$14,547,093</u>

SCOTTISH & YORK HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEAR ENDED DECEMBER 31, 1980

1. ACCOUNTING POLICIES

The consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles which conform in all material respects with International Accounting Standards, and as 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) Principles of Consolidation

The consolidated financial statements include all the subsidiary companies, which are:

	Percentage ownership
Canada	
Scottish & York Insurance Co. Limited	97.92
Central Canada Insurance Service Limited	100
Victoria Insurance Company of Canada	99.1
Scottish & York (Nova Scotia) Limited	100
United States	
Scottish & York, Inc.	100
Lincoln Insurance Company	80
Lincoln Management Corporation	80
Guarantee Insurance Company	80
Scottish & York Management Company	80
Scottish & York International Insurance, Inc.	80
Scottish & York Reinsurance Management Corp.	80
Scottish & York Finance Company	80
Scottish & York Insurance Services Inc.	80
Scottish & York Realty Inc.	80
Bahamas	
Victoria Insurance Company Limited	100
Netherlands	
Scottish & York B. V.	100
Netherlands Antilles	
Scottish & York N. V.	100

Under an agreement dated June 27, 1975, among Scottish & York Holdings Limited, International Insurance Holdings Corporation, Scottish & York, Inc. and Scottish & York Reinsurance Management Corp. relating to the July 1, 1975 acquisition of the 80% interest in the U.S. subsidiaries, provision is made whereby additional consideration may be payable depending on the level of future profits of the U.S. subsidiaries. The purchase agreement also provides for adjustments in respect of uncollected accounts receivable, undisclosed liabilities and unreflected assets at that date.

As a result of the application of these covenants of the purchase agreement a provision for additional purchase consideration amounting to \$236,299 for the current year and \$1,272,073 from inception of the agreement has been paid or accrued in the accounts.

(b) Translation into Canadian Dollars

The accounts of the subsidiary companies in the United States, the Bahamas and the Netherlands 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.
- (iv) 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 or amortized 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) Property and Equipment

Property and equipment are recorded at cost, less accumulated depreciation.

Office and automotive equipment are depreciated over their estimated useful lives at varying rates ranging from 12-1/2% straight line basis to 30% reducing balance basis.

Leasehold improvements are amortized on a straight line basis over a maximum of 6 years.

Amortization of equipment under capital leases is computed using the straight line method with useful lives ranging from 5 to 8 years.

(e) Premium Paid on Acquisition of Shares of U.S. Subsidiary Companies

The Company amortizes such premium over forty years from date of acquisition.

(f) Deferred Revenue

- (i) Deferred commission income and policy acquisition costs.

Policy acquisition costs, net of reinsurance allowances, are deferred and amortized over the terms of the related policies. For the years 1980 and 1979 deferred commission income exceeded deferred acquisition costs. Accordingly, the net credit balance is included in deferred revenue.

- (ii) Deferred premium income

Premium income is deferred until it is earned. The basis for taking premiums into income is in accord with policies prescribed by the regulating organizations under which the companies operate.

(g) Provision for Outstanding Claims

The liabilities for losses and claims and related adjustment expenses are determined using case basis evaluations plus a provision for unreported claims and represent estimates of the ultimate net cost of all losses and claims incurred through December 31, 1980. Since the provisions are necessarily based on estimates of future trends in claim severity and frequency and other factors, which could vary as the losses 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 losses 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.

(h) Recognition of Income

A subsidiary company, Scottish & York Reinsurance Management Corp. manages a number of reinsurance arrangements for which it receives management fees based upon earned premiums. The fee income is recognized simultaneously with the recognition of earned premiums by the reinsurers.

2. PROPERTY AND EQUIPMENT

	<u>1980</u>	<u>1979</u>
Land	\$ 411,604	
Land improvements	389,511	
Construction in progress	2,339,528	
Leasehold improvements	201,914	\$ 148,005
Office equipment	1,113,109	1,017,615
Computer software	765,843	
Automotive equipment	130,536	111,336
Equipment under capital leases	921,790	
	<u>6,273,835</u>	<u>1,276,956</u>
Less accumulated depreciation and amortization	627,416	356,433
	<u>\$5,646,419</u>	<u>\$ 920,523</u>

Depreciation and amortization charged to income was \$294,807 and \$164,600 in 1980 and 1979 respectively.

Equipment includes the following equipment under capital leases at December 31, 1980:

Office equipment	\$ 563,488
Data processing equipment	<u>358,302</u>
	921,790
Less accumulated amortization	<u>57,325</u>
	<u>\$ 864,465</u>

The following is a schedule of future minimum lease payments for equipment under capital leases together with the present value of the minimum lease payments as at December 31, 1980.

Year ended December 31,	
1981	\$ 254,500
1982	254,500
1983	254,500
1984	254,500
1985	<u>153,450</u>
Total minimum lease payments	1,171,450
Less amount representing interest at 18%	<u>300,958</u>
Present value of minimum lease payments	<u>\$ 870,492</u>

3. NOTES PAYABLE

	<u>1980</u>		<u>1979</u>	
	<u>Due within one year</u>	<u>Due after one year</u>	<u>Due within one year</u>	<u>Due after one year</u>
Note payable to bank, interest at U.S. prime plus 1-1/2% (U.S. \$1,750,000)	\$ 2,089,150		\$ 584,800	\$2,631,600
Note payable to bank, interest at U.S. prime plus 1% (U.S. \$5,500,000)		\$6,565,900		
Demand note payable to bank, secured by assignment of notes receivable, interest at U.S. prime plus 1-1/2% (U.S. \$1,410,000)	1,683,257			
Note payable to bank, interest at 20.75% due April 16, 1981 (U.S. \$9,500,000)	11,341,100			
Note payable to bank, bearing interest at 11-5/8% (U.S. \$5,000,000)			5,848,000	
Demand note payable to bank, bearing interest at U.S. prime plus 1% (U.S. \$1,000,000)			1,169,600	
Note payable to bank, bearing interest at 15-3/4% (U.S. \$5,000,000)			<u>5,848,000</u>	
	<u>15,113,507</u>	<u>6,565,900</u>	<u>13,450,400</u>	<u>2,631,600</u>
Total		<u>\$21,679,407</u>		<u>\$16,082,000</u>

The U.S. \$5,500,000 note due after one year as of December 31, 1980 is payable in instalments of U.S. \$1,750,000 due on January 31, 1982 and 1983 with a final payment of U.S. \$2,000,000 due on January 31, 1984.

In February, 1981 U.S. \$3,000,000 in additional working capital financing was obtained. The note payable to the bank is due on April 15, 1981 with interest at 16%.

4. CONTINGENT LIABILITIES AND CONTRACTUAL COMMITMENTS

- (a) The company has obtained a settlement of Federal income taxes assessed against its wholly owned subsidiary company, Victoria Insurance Company Limited, for the years 1968, 1969, 1970. Taxes and interest payable of \$520,000 under the settlement are included in income and premium taxes payable and are reported as an adjustment of prior years' income taxes.

The company has deposited its share investment in subsidiary companies Scottish & York Insurance Co. Limited and Victoria Insurance Company of Canada with The Royal Bank of Canada to be held as security until payment of the settlement has been made.

- (b) The company leases certain office space under lease agreements expiring in various years through 1985. The following is a schedule of future minimum lease payments for the leases with initial or remaining terms in excess of one year as of December 31, 1980:

Year ending December 31

1981	\$ 626,383
1982	364,249
1983	253,832
1984	163,708
1985	44,938
	<u>\$1,453,110</u>

Rental expense of \$750,911 was charged to income in 1980.

- (c) A United States subsidiary has under construction an office building to be used primarily for United States operations. Construction costs are estimated at U.S. \$8,000,000.

U.S. \$8,000,000 will be obtained through a lending bank under the auspices of the New Jersey Economic Development Authority. Financing terms will include a first mortgage lien on acquired land and related improvements with amounts payable monthly over a 30 year term plus interest at 50% of U.S. prime plus 2-1/2%.

5. INFORMATION BY GEOGRAPHIC AREA

In the opinion of management, the company operates solely in the casualty and property insurance industry.

The company conducts business in three geographic areas which are Canada, United States and the Bahamas and other.

	1980		
	<u>Assets</u>	<u>Revenue</u>	<u>Net Income</u>
	(000 omitted)		
Canada	\$ 44,436	\$ 67,887	\$1,315,182
United States	125,619	104,962	3,136,197
Bahamas and other	45,749	24,742	2,712,299
	215,804	197,591	7,163,678
Inter-area eliminations		391	
	<u>\$215,804</u>	<u>\$197,200</u>	<u>\$7,163,678</u>

6. RELATED PARTY TRANSACTIONS

The company has loaned to certain directors, non-interest bearing loans totalling \$176,000. The loans are repayable in equal monthly instalments over 25 years. The company has taken mortgages on real property as security for these loans.

A subsidiary company has loaned a shareholder company affiliated with a director \$730,600 in anticipation of dividends to be declared and paid by subsidiary company.

7. OTHER STATUTORY INFORMATION

	<u>1980</u>	<u>1979</u>
Direct remuneration of directors and senior officers (as defined by The Business Corporations Act)	\$498,276	\$394,425
Depreciation and amortization of property and equipment	\$294,807	\$164,600
Amortization of premium paid on acquisition of shares	\$ 71,218	\$ 43,992

8. SUBSEQUENT EVENT

On April 15, 1981, Scottish & York International Insurance, Inc. tendered for all the shares of Tri-American Corporation, the holding company of the Globe American Casualty Company. The tender offer is at U.S. \$11.50 per share and expires May 14, 1981. The consideration anticipated to complete this acquisition, when the results of the tender are known, is approximately U.S. \$12,000,000 which is to be funded from cash or cash equivalents available to Scottish & York International Insurance, Inc. or a subsidiary company.

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, 1980 and the consolidated statements of income, retained earnings 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, 1980 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 13, 1981
April 16, 1981 for note 8

THORNE RIDDELL
Chartered Accountants

SCOTTISH & YORK HOLDINGS GROUP

Five Year Performance Record

YEAR	GROSS PREMIUMS WRITTEN	NET PREMIUMS WRITTEN	DEFERRED REVENUE	INCOME BEFORE TAXES AND MINORITY INTEREST	INCOME TAXES	NET INCOME	EARNINGS PER SHARE	DIVIDENDS PAID PER SHARE
1980	176,336,067	96,142,936	27,978,296	9,469,967	1,465,056	7,163,678	.90¢	30.0¢
1979	134,727,478	82,682,297	24,373,278	14,229,125	3,028,003	10,362,235	\$1.30	24.0¢
1978	125,037,555	60,043,358	21,375,408	15,819,907	4,495,594	10,551,440	\$1.32	20.25¢
1977	116,094,454	58,638,786	19,653,637	11,205,643	4,179,277	6,252,237	78.2¢	10.75¢
1976	56,052,394	41,540,610	13,350,424	4,430,320	1,772,550	2,489,230	31.1¢	3.5¢

