

ANNUAL REPORT

FOR THE YEAR ENDED 20TH FEBRUARY, 2006

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

THE UNITED KINGDOM FREIGHT DEMURRAGE AND
DEFENCE ASSOCIATION LIMITED

CONTENTS

	Page
Notice of Meeting	2
Directors	3
Report of the Directors	4
Report of the Independent Auditors	7
Consolidated Income and Expenditure Account	9
Consolidated Balance Sheet	10
Holding Company Balance Sheet	11
Consolidated Cashflow Statement	12
Notes to the Financial Statements	13-21
Managers	22

NOTICE OF MEETING

NOTICE IS HEREBY GIVEN that the Annual General Meeting of the Members will be held in London on 21 September, 2006 at 9.30 a.m. for the following purposes:

to receive and adopt the Directors' Report and Financial Statements for the year ended 20 February, 2006:

to re-elect Directors;

to consider amendments to the Rules of the Association;

to re-appoint the Auditors and authorise the Directors to fix their remuneration; and

to transact any other business.

By Order of the Board

I.R. Jarrett

Secretary

27 April, 2006

Directors

E. André

A. S. Bernard

R. G. Crawford, C.B.E.

P. Decavèle

G. A. Gratsos

M. Hashim

P. C. Laskaridis

M. F. Lykiardopulo

A. D. Manthos

T. J. McClure

S. Palios

P. Pappas

M. G. Pateras

P. J. Vogt (Chairman)

G. Woodford

H. H. Wu (resigned on 28 February, 2006)

REPORT OF THE DIRECTORS

The Directors have pleasure in presenting their Report and the Financial Statements of the Association for the year ended 20 February, 2006.

PRINCIPAL ACTIVITY

The Association carries on the business of mutual insurance of its Members against legal costs and expenses as defined in the Rules of the Association.

Under an agreement dated 19 February, 1999, the Association reinsures 90 per cent of its business with The United Kingdom Defence Insurance Association (Isle of Man) Limited.

The number of ships entered in the Association at the year end on 20 February, 2006 was 2,911 (2,376 owned and 535 chartered), compared with 2,910 ships (2,270 owned and 640 chartered) on 20 February, 2005.

DIRECTORS

The Directors who held office during the year are listed on page 3.

In accordance with the Articles of Association, all the Directors retire at the forthcoming Annual General Meeting to be held on 21 September, 2006 and will be eligible for re-election.

Capt. H. H. Wu resigned as a Director in February 2006.

MEETINGS OF DIRECTORS

The Directors met on five occasions during the year under review, in order to fulfil the general and specific responsibilities entrusted to them by the Members under the Rules and under the Memorandum and Articles of Association. At these meetings the Directors received and discussed written and oral reports and recommendations from the Managers on calls and other policy matters.

As in past years, a substantial portion of each meeting involved the consideration of Members' cases in which the Association's support was requested for court or arbitration proceedings. The Directors considered 40 major cases during the year. Furthermore, as in past years the Managers considered a substantial number of requests for support in proceedings under the authority delegated to them by the Directors. Of all the cases formally considered by the Board or the Managers, 90% received a significant measure of support from the Association, amply illustrating the importance attached by both Board and Managers to the Association being supportive of its Members whenever the circumstances render that possible.

The work of the Association remains substantial with about 2,127 case files open during the past year. However, the Managers continue to advise and support Members who are involved with disputes and are frequently able to help them reach satisfactory terms of settlement without proceedings.

REPORT OF THE DIRECTORS (CONTINUED)

FINANCIAL STATEMENTS

The Consolidated Balance Sheet of the Association and its subsidiary at 20 February, 2006, as set out on page 10, shows the reserves of the Association as £34,126,000 (2005: £32,776,000).

The year ended with a deficit on the technical account of £694,000 (2005: £764,000) and after investment income, exchange gains and taxation, there was a surplus for the year of £384,000 (2005: £275,000).

The reserves at 20 February, 2006, together with calls made on Members after that date, are available, and in the opinion of the Directors are necessary, to meet the Association's outgoings and the legal costs and other expenses of the Association's business.

The Board of Directors has effected a Directors' and Officers' Liability Insurance policy to indemnify the Directors and Officers of the Company against loss arising from any claim against them jointly or severally by reason of any wrongful act in their capacity as Directors or Officers of the Association. The insurance also covers the Association's loss when it is required or permitted to indemnify the Directors or Officers pursuant to common law, statute, or the Articles of Association. The cost of the insurance is met by the Association and is included in net operating expenses.

AUDITORS

RSM Robson Rhodes LLP have expressed their willingness to continue in office, and in accordance with Section 385 of the Companies Act 1985, the Directors will place a resolution before the Annual General Meeting in relation to the re-appointment of Auditors for the ensuing year.

REPORT OF THE DIRECTORS (CONTINUED)

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the Directors to prepare Financial Statements for each financial year which give a true and fair view of the state of affairs of the Association and of the income and expenditure of the Association for that period. In preparing those Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- follow applicable accounting standards; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Association will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Association and to enable them to ensure that the Financial Statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Association and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for ensuring that the Directors' Report is prepared in accordance with company law in England and Wales.

P. J. Vogt

Chairman

27 April, 2006

INDEPENDENT AUDITORS' REPORT

INDEPENDENT AUDITORS' REPORT

TO THE SHAREHOLDERS OF THE UNITED KINGDOM FREIGHT DEMURRAGE AND DEFENCE ASSOCIATION LIMITED

We have audited the financial statements of The United Kingdom Freight Demurrage and Defence Association Limited for the year ended 20 February, 2006 which comprise the Consolidated Income and Expenditure Account, the Consolidated Balance Sheet and the Association's Balance Sheet, the Consolidated Cashflow Statement together with the related notes numbered 1 to 18. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Association's shareholders, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Association's shareholders those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Association and the Association's shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As described in the Statement of Directors' Responsibilities the Association's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Association has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

BASIS OF OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Association's circumstances, consistently applied and adequately disclosed.

INDEPENDENT AUDITORS REPORT (CONTINUED)

BASIS OF OPINION (continued)

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

OPINION

In our opinion the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of affairs of the Association as at 20 February, 2006 and of its surplus for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

RSM Robson Rhodes LLP

Chartered Accountants and Registered Auditors

30 Finsbury Square
London EC2P 2YU
England

27 April, 2006

CONSOLIDATED INCOME AND EXPENDITURE ACCOUNT

For the year ended 20 February 2006

	Note	2006 £'000	2005 £'000
Technical Account			
Gross premiums written		11,769	10,978
Outward reinsurance premiums	3	(7,196)	(6,733)
		4,573	4,245
Gross claims paid	4	(9,666)	(9,248)
Reinsurers' share		6,817	6,629
		(2,849)	(2,619)
Gross change in provision for claims	16	(966)	(2,406)
Reinsurers' share		869	2,165
		(97)	(241)
Net incurred claims		(2,946)	(2,860)
Net operating expenses	5	(2,321)	(2,149)
Balance on the technical account		(694)	(764)
Non Technical Account			
Balance on the technical account		(694)	(764)
Investment income	8	140	46
Unrealised gain on investments		62	2
Exchange gains		927	1,007
Surplus on ordinary activities before tax		435	291
Tax on ordinary activities	14	(51)	(16)
Surplus on ordinary activities after tax		384	275

All activities represent continuing activities. There are no recognised gains or losses other than the result for the year.

CONSOLIDATED BALANCE SHEET

20 February 2006

	Note	2006 £'000	2005 £'000
Assets			
Investments			
Other financial investments	10	564	934
Debtors			
Debtors arising out of direct insurance operations	12	1,441	2,131
Other debtors		69	102
Cash at bank		3,281	1,523
Reinsurers' share of technical provisions			
Claims outstanding		29,110	28,240
Accrued interest		–	2
Total assets		34,465	32,932
Liabilities and Reserves			
Surplus of reserves		1,782	1,398
Technical provisions			
Claims outstanding	16	32,344	31,378
		34,126	32,776
Creditors			
Creditors in respect of direct insurance operations	13	38	34
Creditors in respect of reinsurance operations		45	–
Other creditors including tax and social security	13	256	122
		339	156
Total liabilities and reserves		34,465	32,932

The financial statements set out on pages 9 to 21 were approved by the Board of Directors on 27 April, 2006 and have been signed on its behalf by:

DIRECTORS

P. J. Vogt (Chairman)

T. J. McClure

MANAGERS

J. R. Morris

HOLDING COMPANY BALANCE SHEET

20 February 2006

	Note	2006 £'000	2005 £'000
Assets			
Investments			
Shares in group undertakings	11	50	50
Other financial investments	10	564	934
Debtors			
Debtors arising out of direct insurance operations	12	1,441	2,131
Other debtors		19	52
Due from subsidiary		5	5
Cash at bank		3,281	1,523
Reinsurers' share of technical provisions			
Claims outstanding		29,110	28,240
Accrued interest			
		–	2
Total assets		34,470	32,937
Liabilities and Reserves			
Surplus of reserves		1,792	1,408
Technical provisions			
Claims outstanding – gross amount	16	32,344	31,378
		34,136	32,786
Creditors			
Creditors arising out of direct insurance operations	13	38	34
Creditors arising out of reinsurance operations		45	–
Other creditors including tax and social security	13	251	117
		334	151
Total liabilities and reserves		34,470	32,937

The financial statements set out on pages 9 to 21 were approved by the Board of Directors on 27 April, 2006 and have been signed on its behalf by:

DIRECTORS

P. J. Vogt (Chairman)

T. J. McClure

MANAGERS

J. R. Morris

CONSOLIDATED CASHFLOW STATEMENT

For the year ended 20 February 2006

	Note	2006 £'000	2005 £'000
OPERATING ACTIVITIES			
Premiums received		11,691	11,035
Claims paid net of reinsurers' share		(756)	(660)
Reinsurance premiums paid		(7,151)	(6,733)
Other operating cash payments		(3,512)	(5,490)
<hr/>			
Net cashflow from operating activities		272	(1,848)
Interest received and exchange gains		1,070	1,053
Taxation		(16)	(2)
<hr/>			
	15	1,326	(797)
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CASHFLOW STATEMENT

	2006 £'000	2005 £'000
Balance on technical account	(694)	(764)
(Decrease)/increase in gross provision for claims	97	241
Decrease/(increase) in debtors	726	(1,340)
(Decrease)/increase in creditors	143	15
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Net cashflow from operating activities	272	(1,848)
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NOTES TO THE FINANCIAL STATEMENTS

For the year ended 20 February 2006

1 Constitution

The Association is incorporated in England as a company limited by guarantee and not having a share capital.

In the event of the company's liquidation the net assets of the Association are to be distributed in proportion to the amount of contributions paid by Members during the preceding six years.

2 Accounting Policies

(a) Accounting disclosures

These Financial Statements have been prepared under the provisions of Section 255 of, and Schedule 9A to, the Companies Act 1985, and comply with applicable accounting standards. The Financial Statements are prepared on an annual basis under the historical cost convention as modified by the revaluation of investments and comply with all material recommendations of the Statement of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers in December 2005.

(b) Foreign currencies

Foreign currency assets and liabilities (except the cost of investment) are translated into sterling at the rates of exchange ruling at the balance sheet date. The resulting difference is treated as unrealised.

Revenue transactions are translated into sterling at the rate applicable for the date on which they took place.

Differences between closing exchange rates and the rates applying to outstanding forward currency contracts are also recognised. All exchange gains/losses whether realised or unrealised have been included in the Income and Expenditure Account for the year.

(c) Gross premiums written

Calls and premiums include calls less return premiums and the change in provisions for bad and doubtful debts. These calls and premiums are the total receivable for the whole period of cover provided by the contracts incepting during the accounting period together with any adjustments in respect of prior accounting periods. There are no unearned premiums.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

2 Accounting Policies (continued)

(d) Claims

These are the legal costs and expenses of the Members covered by the Association. They include all claims incurred during the year, whether paid, estimated or unreported together with internal claims management costs and future claims management costs and adjustments for claims outstanding from previous years.

A forecast of unreported claims is based on the estimated ultimate cost of claims arising out of events which have occurred before the end of the accounting period but have not yet been reported. These future claims are based on the Managers' best estimate of unreported claims on each policy year. The estimates are calculated by comparing the pattern of claims payments in current policy years with earlier policy years, and then projecting the likely outcome of the more recent years.

Whilst the Directors consider that the gross provisions for claims and the related reinsurance recoveries are fairly stated on the basis of information currently available, the ultimate liability will vary as a result of subsequent information and events and may result in significant adjustments to the amount provided. Any differences between the provisions and subsequent settlements are dealt with in the technical accounts of later years.

(e) Investments

Investments purchased in foreign currencies are translated into sterling on the date of purchase. The market value of foreign currency investments is translated at the rate of exchange ruling at the balance sheet date. The investment in the Subsidiary is carried at cost in the Holding Company Balance Sheet.

(f) Investment income

This comprises income received during the year adjusted in respect of interest receivable at the year end, and profits and losses on the sale of investments and gains and losses on closed forward currency contracts.

The unrealised gains and losses on the movement in the market value of the investments are included in the non-technical account. No transfer is made of the investment returns from the non-technical account to the technical account, as this is not considered appropriate.

(g) Consolidation

As the Financial Statements are in consolidated form, the Association is exempt from the requirement to present an Income and Expenditure Account for the holding company.

(h) The payment of taxation is deferred or accelerated because of timing differences between the treatment of certain items for accounting and taxation purposes. Full provision for deferred taxation is made under the liability method, without discounting, on all timing differences that have arisen, but not reversed by the balance sheet date, unless such provision is not permitted by Financial Reporting Standard 19.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2005

3 Outward Reinsurance Premiums

		2006 £'000	2005 £'000
Excess loss premium		310	259
90% quota share premium 2005/6		9,957	9,348
		10,267	9,607
Agreed discount		(3,071)	(2,874)
		7,196	6,733

4 Gross Claims Paid

	Note	2006 £'000	2005 £'000
Legal costs and expenses		7,574	7,365
Management fee in respect of claims handling	6	2,092	1,883
		9,666	9,248

5 Net Operating Expenses

	Note	2006 £'000	2005 £'000
Management fee	6	1,395	1,255
Directors' remuneration		93	91
Auditors' remuneration	8		
Audit fees for holding company		22	22
Tax and other consultancy services		2	2
Brokerage		396	332
Other expenses		413	447
		2,321	2,149

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

6 Management Fee

The fee covers the Managers' costs of providing offices, staff and administration. It is fixed by the Directors in accordance with the Rules. No loan has been made to the Managers and none is contemplated. The Association itself had no employees throughout the year.

The management fee is apportioned across three functions which are included in the accounts as follows:

	Note	2006 £'000	2005 £'000
Acquisition costs		1,114	1,002
Other		281	253
Management fees in Net Operating Expenses	5	1,395	1,255
Claims handling	4	2,092	1,883
		3,487	3,138

7 Directors' Fees

	2006 £	2005 £
Aggregate emoluments	93	92

Pension contributions are not made in respect of any of the Directors.

8 Investment Income

	2006 £'000	2005 £'000
Bank deposits	103	40
Interest on bonds and UCITS	37	6
	140	46

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

9 Rates of Exchange

	2006	2005
Year end rates of exchange were:		
Equivalent to £1 sterling US dollar	1.7406	1.8944

10 Investments

	Market Value		Cost	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Fixed interest securities	–	342	–	400
UCITS	564	592	559	592
	564	934	559	92

	2006	2005
Cash and interest bearing securities repayable:		
within one year	100%	100%
one to three years	–	–
	100%	100%

11 Investments

	Holding Company	
	2006 £'000	2005 £'000
Shares in group undertakings at cost	50	50

The Association owns 100% of the issued share capital of United Kingdom Defence Reinsurance Association Ltd., a company that is incorporated in Bermuda. This company does not trade.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

12 Debtors

	2006 £'000	2005 £'000
Arising out of direct insurance operations:		
Contributions	282	199
Recoverable deductibles	68	69
Due from quota share reinsurer	1,091	1,863
	1,441	2,131

13 Creditors

	The Group		Holding Company	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Arising out of direct insurance: operations				
Members	38	34	38	34
	38	34	38	34
Other creditors:				
Accrued expenses	113	60	113	60
Corporation tax payable	51	16	51	16
Other	92	46	87	41
	256	122	251	117

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

14 Taxation

This relates to the holding company and is in respect of United Kingdom corporation tax on its assessable investment income and gains at current rates of taxation.

The tax charge for the year is made up as follows:

	2006 £'000	2005 £'000
Corporation tax at 19% (2005 – 19%)	51	16
Prior year adjustment	–	–
Total current tax	51	16

The current taxation charge for the year is different from the standard rate of corporation tax for companies of this size in the UK (19%). The differences are explained below:

	2006 £'000	2005 £'000
Surplus/(deficit) on ordinary activities before taxation	435	291
Theoretical tax of UK corporation tax of 19% (2005: 19%)		
Effects of:	83	55
Balance on technical account	132	145
Non taxable exchange gains	(164)	(184)
Prior year adjustment	–	–
Actual current tax charge	51	16

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

15 Cashflow Statement

Movement in cash, deposits and investments	At 20/02/2005 £'000	Cashflow £'000	Change in market value £'000	At 20/02/2006 £'000
Cash at bank	1,523	1,758	–	3,281
Other financial investments	934	(432)	62	564
	2,457	1,326	62	3,845

16 Claims Outstanding

	2006 £'000	2005 £'000
Claims outstanding at end of year	32,344	31,378
Claims outstanding at beginning of year	31,378	28,972
Decrease/(increase) in gross provision for claims	(966)	(2,406)

The nature of the business makes it very difficult to predict the likely outcome of any particular case and to estimate the cost of future claims. The estimates for known outstanding claims are based on the best estimates and judgement of the Managers of the likely cost of individual cases, and the extent of the Association's current commitment to the cost of these cases. These estimates are as accurate as possible given the details of the cases and taking into account all the current information. The estimates are reviewed regularly.

The movement on incurred claims for prior policy years was a release of £3,460,000 (2005: £1,823,000 deterioration).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 20 February 2006

17 Contingent Liabilities

A number of guarantees have been given in respect of legal costs relating to cases involving Members, where the Association is already committed to the costs of the cases.

The Association has entered into forward currency contracts to sell US Dollars 10,000,000 for sterling, during 2006 and 2007, which protect part of its US Dollar income against exchange rate fluctuations.

18 Related Party Disclosures

The Association has no share capital and is controlled by the Members who are also the insureds. The subsequent insurance transactions are consequently deemed to be between related parties but these are the only transactions between the Association and the Members.

All of the Directors are current representatives of Member companies and other than the insurance, which is arranged on an arm's length basis, and Member interests of these companies, the Directors have no financial interests in the Association.

The Association reinsures with the United Kingdom Defence Insurance Association (Isle of Man) Limited (UKDIA(IOM)) on a 90% quota share basis. None of the Directors of the Association are Directors of UKDIA(IOM).

MANAGERS

THOMAS MILLER DEFENCE LIMITED

J. R. Morris (Chairman)

R. A. Bettinson

D. J. Evans

A. T. Jenkinson

N. G. Long

S. L. Murphy

P. M. Sessions

N. Staff

M. R. White

SECRETARY

I. R. Jarrett

REGISTERED OFFICE

International House,
26 Creechurch Lane,
London, EC3A 5BA
Telephone: 020 7283 4646
Fax: 020 7204 2131

REGISTERED NUMBER

00501877 England

SUBSIDIARY COMPANY

UNITED KINGDOM DEFENCE REINSURANCE ASSOCIATION LTD.

REGISTERED OFFICE AND BUSINESS ADDRESS OF THE SUBSIDIARY

Windsor Place, 18, Queen Street,
P.O. Box 665,
Hamilton HMCX, Bermuda.
Telephone: Hamilton 2-4724

