

**EVEREST REINSURANCE (BERMUDA), LTD.**

(a wholly owned subsidiary of Everest Re Group, Ltd.)

**GAAP Financial Statements**

**For the Years Ended December 31, 2008 and 2007**

EVEREST REINSURANCE (BERMUDA), LTD.  
BALANCE SHEETS

	December 31,	
	2008	2007
(Dollars in thousands, except par value per share)		
<b>ASSETS:</b>		
Fixed maturities - available for sale, at market value (amortized cost: 2008, \$4,546,643; 2007, \$3,713,873)	\$ 4,593,307	\$ 3,680,000
Equity securities - available for sale, at market value (cost: 2008, \$14,900; 2007, \$14,482)	16,884	14,797
Equity securities - available for sale, at fair value	13	612,670
Short-term investments	704,279	645,218
Other invested assets (cost: 2008, \$283,420; 2007, \$210,135)	283,420	210,135
Cash	57,954	70,178
Total investments and cash	<u>5,655,857</u>	<u>5,232,998</u>
Accrued investment income	58,161	51,877
Premiums receivable	489,339	465,970
Reinsurance receivables - unaffiliated	19,279	21,471
Reinsurance receivables - affiliated	264,201	278,209
Funds held - reinsureds	232,361	249,537
Deferred acquisition costs	147,781	148,147
Prepaid reinsurance premiums	17,520	22,372
Deferred tax asset	-	696
Other assets	6,089	1,291
<b>TOTAL ASSETS</b>	<u>\$ 6,890,588</u>	<u>\$ 6,472,568</u>
<b>LIABILITIES:</b>		
Reserve for losses and loss adjustment expenses	\$ 3,726,700	\$ 3,079,102
Future policy benefit reserve	66,172	78,417
Unearned premium reserve	499,948	508,672
Funds held under reinsurance treaties	48,600	53,589
Losses in course of payment	111,945	116,264
Other net payable to reinsurers	35,106	47,176
Current income taxes payable	50,229	36,020
Equity index put options, fair value	60,552	39,653
Deferred gain on retroactive reinsurance	37,070	-
Deposit accounting liability	19,745	19,216
Other liabilities	11,875	3,062
Total liabilities	<u>4,667,942</u>	<u>3,981,171</u>
Commitments and Contingencies (Note 13)		
<b>SHAREHOLDER'S EQUITY:</b>		
Common shares, par value: \$1.00; 1.25 million shares authorized, issued and outstanding (2008 and 2007)	1,250	1,250
Additional paid-in capital	1,325,834	1,325,399
Accumulated other comprehensive (loss) income, net of deferred income tax expense of \$47.2 million at 2008 and benefit of \$0.7 million at 2007	(128,456)	5,776
Retained earnings	1,024,018	1,158,972
Total shareholder's equity	<u>2,222,646</u>	<u>2,491,397</u>
<b>TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY</b>	<u>\$ 6,890,588</u>	<u>\$ 6,472,568</u>

The accompanying notes are an integral part of the consolidated financial statements.

EVEREST REINSURANCE (BERMUDA), LTD.  
 STATEMENTS OF OPERATIONS AND COMPREHENSIVE (LOSS) INCOME

(Dollars in thousands)	December 31,	
	2008	2007
<b>REVENUES:</b>		
Premiums earned	\$ 1,563,740	\$ 1,551,753
Net investment income	171,280	238,295
Net realized capital (losses) gains	(304,945)	12,743
Net derivative expense	(20,900)	(2,124)
Other (expense) income	(105,211)	26,716
Total revenues	<u>1,303,964</u>	<u>1,827,383</u>
<b>CLAIMS AND EXPENSES:</b>		
Incurred losses and loss adjustment expenses	806,211	920,000
Commission, brokerage, taxes and fees	457,857	416,164
Other underwriting expenses	23,717	20,440
Total claims and expenses	<u>1,287,785</u>	<u>1,356,604</u>
<b>INCOME BEFORE TAXES</b>	16,179	470,779
Income tax expense	<u>31,133</u>	<u>43,607</u>
<b>NET (LOSS) INCOME</b>	<u>\$ (14,954)</u>	<u>\$ 427,172</u>
Other comprehensive (loss) income, net of tax	<u>(134,232)</u>	<u>27,351</u>
<b>COMPREHENSIVE (LOSS) INCOME</b>	<u>\$ (149,186)</u>	<u>\$ 454,523</u>

The accompanying notes are an integral part of the consolidated financial statements.

EVEREST REINSURANCE (BERMUDA), LTD.  
STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY

	December 31,	
	2008	2007
<small>(Dollars in thousands, except share amounts)</small>		
<b>COMMON SHARES (shares outstanding):</b>		
Balance, beginning of period	1,250,000	1,250,000
Balance, end of period	<u>1,250,000</u>	<u>1,250,000</u>
<b>COMMON SHARES (par value):</b>		
Balance, beginning of period	\$ 1,250	\$ 1,250
Balance, end of period	<u>1,250</u>	<u>1,250</u>
<b>ADDITIONAL PAID-IN CAPITAL:</b>		
Balance, beginning of period	1,325,399	1,325,015
Share-based compensation plans	435	384
Balance, end of period	<u>1,325,834</u>	<u>1,325,399</u>
<b>ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME, NET OF DEFERRED INCOME TAXES:</b>		
Balance, beginning of period	5,776	5,881
Cumulative effect to adopt FAS. 159, net of tax	-	(27,456)
Net (decrease) increase during the period	<u>(134,232)</u>	<u>27,351</u>
Balance, end of period	<u>(128,456)</u>	<u>5,776</u>
<b>RETAINED EARNINGS:</b>		
Balance, beginning of period	1,158,972	704,344
Cumulative effect to adopt FAS. 159, net of tax	-	27,456
Net (loss) income	(14,954)	427,172
Dividends paid	<u>(120,000)</u>	<u>-</u>
Balance, end of period	<u>1,024,018</u>	<u>1,158,972</u>
<b>TOTAL SHAREHOLDER'S EQUITY, END OF PERIOD</b>	<u>\$ 2,222,646</u>	<u>\$ 2,491,397</u>

The accompanying notes are an integral part of the consolidated financial statements.

EVEREST REINSURANCE (BERMUDA), LTD.  
STATEMENTS OF CASH FLOWS

	Years Ended December 31,	
	2008	2007
(Dollars in thousands)		
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net (loss) income	\$ (14,954)	\$ 427,172
Adjustments to reconcile net income to net cash provided by operating activities:		
(Increase) decrease in premiums receivable	(65,283)	37,265
Increase in funds held by reinsureds, net	(33,242)	(38,209)
Increase in reinsurance receivables	(63,689)	(56,382)
Increase in deferred tax asset	696	-
Increase in reserve for losses and loss adjustment expenses	255,755	251,404
Decrease in future policy benefit reserve	(12,244)	(22,545)
Increase in unearned premiums	13,168	25,595
Change in equity adjustments in limited partnerships	68,819	(22,663)
Change in other assets and liabilities, net	55,299	9,879
Non-cash deferred gain on loss portfolio transfer	(315)	-
Non-cash compensation expense	435	384
Amortization of bond premium	5,442	(301)
Net realized capital losses (gains)	304,945	(12,743)
Net cash provided by operating activities	<u>514,832</u>	<u>598,856</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from fixed maturities matured/called - available for sale, at market value	437,195	473,602
Proceeds from fixed maturities sold - available for sale, at market value	121,022	230,565
Proceeds from equity securities sold - available for sale, at fair value	572,140	972,703
Proceeds from other invested assets sold	26,927	9,970
Cost of fixed maturities acquired - available for sale, at market value	(1,108,081)	(655,537)
Cost of equity securities acquired - available for sale, at market value	(1,024)	(13,407)
Cost of equity securities acquired - available for sale, at fair value	(178,029)	(1,337,592)
Cost of other invested assets acquired	(168,813)	(57,534)
Net purchases of short-term securities	(40,821)	(184,159)
Net (increase) decrease in unsettled securities transactions	(3,611)	748
Net cash used in investing activities	<u>(343,095)</u>	<u>(560,641)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Dividends paid to shareholder	(120,000)	-
Net cash used in by financing activities	<u>(120,000)</u>	<u>-</u>
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH</b>	<u>(63,961)</u>	<u>(34,816)</u>
Net (decrease) increase in cash	(12,224)	3,399
Cash, beginning of period	70,178	66,779
Cash, end of period	<u>\$ 57,954</u>	<u>\$ 70,178</u>
<b>SUPPLEMENTAL CASH FLOW INFORMATION</b>		
Cash transactions:		
Income taxes paid	\$ 57,622	\$ 33,796

The accompanying notes are an integral part of the financial statements.

**EVEREST REINSURANCE (BERMUDA), LTD.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Years Ended December 31, 2008 and 2007**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. Business and Basis of Presentation.**

Everest Reinsurance (Bermuda) Ltd. (the "Company" or "Bermuda Re"), a Bermuda insurance company and direct wholly owned subsidiary of Everest Re Group, Ltd. ("Group"), is registered as a Class 4 insurer and long-term insurer and underwrites property and casualty reinsurance and insurance and life and annuity business. The Company's UK branch writes property and casualty reinsurance for the United Kingdom and European markets.

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"). All amounts are reported in U.S. dollars.

The preparation of financial statements in conformity with GAAP requires 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. Ultimate actual results could differ, possibly materially, from those estimates.

Certain reclassifications and format changes have been made to prior years' amounts to conform to the 2008 presentation.

**B. Investments.**

Fixed maturity and market value equity security investments are all classified as available for sale. Unrealized appreciation and depreciation, as a result of temporary changes in market value during the period, are reflected in shareholder's equity, net of income taxes in "accumulated other comprehensive income" in the balance sheets. Actively managed equity securities are carried at fair value with fair value re-measurements reflected as net realized capital gains and losses in the statements of operations and comprehensive income. Unrealized losses on fixed maturities, which are deemed other-than-temporary, are charged to net income as net realized capital losses. Short-term investments are stated at cost, which approximates market value. Realized gains or losses on sales of investments are determined on the basis of identified cost. For non-publicly traded securities, market prices are determined through the use of pricing models that evaluate securities relative to the U.S. Treasury yield curve, taking into account the issue type, credit quality and cash flow characteristics of each security. For publicly traded securities, market value is based on quoted market prices or valuation models that use observable market inputs. When a sector of the financial markets is inactive or illiquid, the Company may use its own assumptions about future cash flows and risk-adjusted discount rates to determine fair value. Retrospective adjustments are employed to recalculate the values of asset-backed securities. Each acquisition lot is reviewed to recalculate the effective yield. The recalculated effective yield is used to derive a book value as if the new yield were applied at the time of acquisition. Outstanding principal factors from the time of acquisition to the adjustment date are used to calculate the prepayment history for all applicable securities. Conditional prepayment rates, computed with life to date factor histories and weighted average maturities, are used to effect the calculation of projected and prepayments for pass-through security types. Other invested assets include limited partnerships. Limited partnerships are accounted for under the equity method of accounting, which may be recorded on a monthly or quarterly lag.

**C. Uncollectible Receivable Balances.**

The Company provides reserves for uncollectible premiums receivables based on management's assessment of the collectibility of the outstanding balances. Such reserves were \$0.4 million at December 31, 2008 and 2007.

**D. Deferred Acquisition Costs.**

Acquisition costs, consisting principally of commissions and brokerage expenses and other fees incurred at the time a contract or policy is issued and that vary with and are directly related to the Company's reinsurance and insurance business, are deferred and amortized over the period in which the related premiums are earned, generally one year. Deferred acquisition costs are limited to their estimated realizable value by line of business based on the related unearned premiums, anticipated claims and claim expenses and anticipated investment income. Deferred acquisition costs amortized to income were \$457.9 million and \$416.2 million in 2008 and 2007, respectively.

The present value of in force annuity business is included in deferred acquisition costs. This value is amortized over the expected life of the business from the time of acquisition. The amortization each year is a function of the gross profits each year in relation to the total gross profits expected over the life of the business, discounted at an assumed net credit rate.

**E. Reserve for Losses and Loss Adjustment Expenses.**

The reserve for losses and loss adjustment expenses ("LAE") is based on individual case estimates and reports received from ceding companies. A provision is included for losses and LAE incurred but not reported ("IBNR") based on past experience. A provision is also included for certain potential liabilities relating to asbestos and environmental ("A&E") exposures, which liabilities cannot be estimated using traditional reserving techniques. See also Note 3. The reserves are reviewed periodically and any changes in estimates are reflected in earnings in the period the adjustment is made. The Company's loss and LAE reserves represent management's best estimate of the ultimate liability. Loss and LAE reserves are presented gross of reinsurance receivables and incurred losses and LAE are presented net of reinsurance.

Accruals for commissions are established for reinsurance contracts that provide for the stated commission percentage to increase or decrease based on the loss experience of the contract. Changes in estimates for such arrangements are recorded as commission expense. Commission accruals for contracts with adjustable features are estimated based on expected loss and LAE.

**F. Future Policy Benefit Reserve.**

Liabilities for future policy benefits on annuity policies are carried at their accumulated values. Reserves for policy benefits include both mortality and morbidity claims in the process of settlement and IBNR claims. Interest rate assumptions used to estimate liabilities for policy benefits range from 2.34% to 5.88%. Actual experience in a particular period may fluctuate from expected results.

**G. Premium Revenues.**

Written premiums are earned ratably over the periods of the related insurance and reinsurance contracts. Unearned premium reserves are established relative to the unexpired contract period. Such reserves are established based upon reports received from ceding companies or estimated using pro rata methods based on statistical data. Reinstatement premiums represent additional premium received on reinsurance coverages, most prevalently catastrophe related, when limits have been depleted under the original reinsurance contract and additional coverage is granted. Written and earned premiums and the related costs, which have not yet been reported to the Company, are estimated and accrued. Premiums are net of ceded reinsurance.

Annuity premiums are recognized as revenue over the premium-paying period of the policies.

**H. Income Taxes.**

The UK branch of Bermuda Re files a UK income tax return. Deferred income taxes have been recorded to recognize the tax effect of temporary differences between the financial reporting and income tax bases of assets and liabilities, which arise because of differences between GAAP and income tax accounting rules.

**I. Foreign Currency.**

Assets and liabilities relating to foreign operations are translated into U.S. dollars at the exchange rates in effect at the balance sheet date; revenues and expenses are translated into U.S. dollars using average exchange rates in effect during the reporting period. Gains and losses resulting from translating foreign currency financial statements, net of deferred income taxes, are excluded from net income and accumulated in shareholder's equity. Gains and losses resulting from foreign currency transactions, other than debt securities available for sale, are recorded through the statements of operations and comprehensive income (loss) in other income (expense). Gains and losses resulting from changes in the foreign currency exchange rates on debt securities, available for sale at market value, are recorded in the balance sheets in accumulated other comprehensive income (loss) as unrealized appreciation (depreciation).

**J. Derivatives.**

The Company sold seven equity index put option contracts, which are outstanding. These contracts meet the definition of a derivative under Statement of Financial Accounting Standards ("FAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("FAS 133"). The Company's position in these contracts is unhedged and these contracts are accounted for as a derivative in accordance with FAS 133. Accordingly, these contracts are carried at fair value with changes in fair value during the period recorded in the statements of operations and comprehensive income (loss).

**K. Deposit Assets and Liabilities.**

In the normal course of its operations, the Company may enter into contracts that do not meet the risk transfer provisions of FAS No. 113, "Accounting and Reporting for Reinsurance of Short Duration and Long Duration Contracts". Such contracts are accounted for using the deposit accounting method and are included in other liabilities. For such contracts, the Company originally records deposit liabilities for an amount equivalent to the assets received. Actuarial studies are used to estimate the final liabilities under such contracts with any change reflected in the statements of operations and comprehensive income (loss).

**L. Retroactive Reinsurance.**

The gains on assumed retroactive contracts are deferred and amortized into income based on cash payouts. Losses on assumed retroactive contracts are recognized immediately into income.

**M. Application of New Accounting Standards.**

In September 2006, the Financial Accounting Standards Board ("FASB") issued FAS No. 157 "Fair Value Measurements" ("FAS 157"). FAS 157 defines fair value, establishes a framework for measuring fair value consistently in GAAP and expands disclosures about fair value measurements. The Company adopted FAS 157 as of January 1, 2007.

In February 2007, the FASB issued FAS No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities - including an amendment to FASB Statement No. 115" ("FAS 159"). FAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The Company adopted FAS 159 as of January 1, 2007.

In March 2008, the FASB issued FAS No. 161 "Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133" ("FAS 161"). FAS 161 requires entities to provide additional disclosures on derivative and hedging activities regarding their effect on financial position, financial performance and cash flows. This statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company will adopt FAS 161 on January 1, 2009.

In October 2008, the FASB issued FASB Staff Position FAS 157-3 "Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active" ("FAS 157-3"). FAS 157-3 clarifies the application of FAS No. 157 "Fair Value Measurements" ("FAS 157"), in a market that is not active. This FASB Staff Position is effective upon issuance.

## 2. INVESTMENTS

The amortized cost, market value, and gross unrealized appreciation and depreciation of available for sale, market value fixed maturity and equity security investments are as follows for the periods indicated:

	At December 31, 2008			
	Amortized Cost	Unrealized Appreciation	Unrealized Depreciation	Market Value
(Dollars in thousands)				
Fixed maturities - available for sale				
U.S. Treasury securities and obligations of U.S. government agencies and corporations	\$ 213,295	\$ 39,502	\$ (663)	\$ 252,134
Corporate securities	1,896,643	40,326	(113,738)	1,823,231
Mortgage-backed securities	1,492,578	20,973	(66,195)	1,447,356
Foreign government securities	498,164	82,452	(398)	580,218
Foreign corporate securities	445,963	49,839	(5,434)	490,368
Total fixed maturities	<u>\$ 4,546,643</u>	<u>\$ 233,092</u>	<u>\$ (186,428)</u>	<u>\$ 4,593,307</u>
Equity securities	<u>\$ 14,900</u>	<u>\$ 1,984</u>	<u>\$ -</u>	<u>\$ 16,884</u>

	At December 31, 2007			
	Amortized Cost	Unrealized Appreciation	Unrealized Depreciation	Market Value
(Dollars in thousands)				
Fixed maturities - available for sale				
U.S. Treasury securities and obligations of U.S. government agencies and corporations	\$ 130,551	\$ 3,543	\$ (105)	\$ 133,989
Corporate securities	1,566,606	16,938	(37,327)	1,546,217
Mortgage-backed securities	902,414	2,883	(11,539)	893,758
Foreign government securities	626,768	4,383	(4,817)	626,334
Foreign corporate securities	487,534	3,005	(10,837)	479,702
Total fixed maturities	<u>\$ 3,713,873</u>	<u>\$ 30,752</u>	<u>\$ (64,625)</u>	<u>\$ 3,680,000</u>
Equity securities	<u>\$ 14,482</u>	<u>\$ 315</u>	<u>\$ -</u>	<u>\$ 14,797</u>

The amortized cost and market value of fixed maturities are shown in the following table by contractual maturity. Mortgage-backed securities generally are more likely to be prepaid than other fixed maturities. As the stated maturity of such securities may not be indicative of actual maturities, the total for mortgage-backed securities is shown separately.

	At December 31, 2008	
	Amortized Cost	Market Value
(Dollars in thousands)		
Fixed maturities - available for sale		
Due in one year or less	\$ 280,334	\$ 285,329
Due after one year through five years	1,385,228	1,437,481
Due after five years through ten years	1,022,714	1,046,584
Due after ten years	365,789	376,557
Mortgage-backed securities	1,492,578	1,447,356
Total	<u>\$ 4,546,643</u>	<u>\$ 4,593,307</u>

The changes in net unrealized gains (losses) for the Company's investments are derived from the following sources for the periods indicated:

(Dollars in thousands)	<u>Years Ended December 31,</u>	
	<u>2008</u>	<u>2007</u>
Increase during the period between the market value and cost of investments carried at market value, and deferred taxes thereon:		
Fixed maturities	\$ 80,537	\$ 23,511
Equity securities	<u>1,669</u>	<u>315</u>
Change in unrealized appreciation, pre-tax	82,206	23,826
Deferred taxes	<u>(47,915)</u>	<u>(3,399)</u>
Change in unrealized appreciation, net of deferred taxes, included in shareholder's equity	<u>\$ 34,291</u>	<u>\$ 20,427</u>

The Company frequently reviews its investment portfolio for declines in market value and focuses its attention on securities whose fair value has fallen below 80% of their amortized value at the time of review. The Company then assesses whether the decline in value is temporary or other-than-temporary. In making its assessment, the Company evaluates the current market and interest rate environment as well as specific issuer information and the Company's ability and intent to hold to recovery. Generally, a change in a security's value caused by a change in the market or interest rate environment does not constitute an other-than-temporary impairment, but rather a temporary decline in market value. Temporary declines in market value are recorded as unrealized losses in accumulated other comprehensive income. If the Company determines that the decline is other-than-temporary, the carrying value of the investment is written down to fair value and a realized loss is recorded in the Company's statements of operations and comprehensive income (loss). The Company's assessments are based on the issuer's current and expected future financial position, timeliness with respect to interest and/or principal payments, speed of repayments and any applicable credit enhancements or breakeven constant default rates on asset-backed securities, as well as relevant information provided by rating agencies, investment advisors and analysts.

The table below displays the aggregate market value and gross unrealized depreciation of fixed maturity securities, by investment category and maturity category by length of time that individual securities had been in a continuous unrealized loss position for the period indicated:

Duration by security type of unrealized loss at December 31, 2008						
Less than 12 months		Greater than 12 months		Total		
Gross Unrealized		Gross Unrealized		Gross Unrealized		
Market Value	Depreciation	Market Value	Depreciation	Market Value	Depreciation	
(Dollars in thousands)						
Fixed maturity securities						
U.S. government						
agencies and authorities	\$ 5,686	\$ (663)	\$ -	\$ -	\$ 5,686	\$ (663)
Foreign governments	1,130	(194)	7,672	(204)	8,802	(398)
All other corporate	811,047	(55,854)	910,989	(129,513)	1,722,036	(185,367)
Total fixed maturities	\$ 817,863	\$ (56,711)	\$ 918,661	\$ (129,717)	\$ 1,736,524	\$ (186,428)

Duration by maturity of unrealized loss at December 31, 2008						
Less than 12 months		Greater than 12 months		Total		
Gross Unrealized		Gross Unrealized		Gross Unrealized		
Market Value	Depreciation	Market Value	Depreciation	Market Value	Depreciation	
(Dollars in thousands)						
Fixed maturity securities						
Due in one year or less	\$ 12,749	\$ (853)	\$ 44,951	\$ (1,170)	\$ 57,700	\$ (2,023)
Due in one year through five years	336,029	(20,144)	262,970	(21,735)	598,999	(41,879)
Due in five years through ten years	238,461	(15,629)	261,690	(31,861)	500,151	(47,490)
Due after ten years	48,610	(8,360)	102,887	(20,481)	151,497	(28,841)
Mortgage-backed securities	182,014	(11,725)	246,163	(54,470)	428,177	(66,195)
Total fixed maturities	\$ 817,863	\$ (56,711)	\$ 918,661	\$ (129,717)	\$ 1,736,524	\$ (186,428)

The aggregate market value and gross unrealized losses related to investments in an unrealized loss position as of December 31, 2008 were \$1,736.5 million and \$186.4 million, respectively. There were no unrealized losses on a single security that exceeded 0.21% of the market value of the fixed maturities at December 31, 2008. In addition, there was no significant concentration of unrealized losses in any one market sector. The \$56.7 million of unrealized losses related to fixed maturity securities that had been in an unrealized loss position for less than one year were generally comprised of highly rated domestic corporate securities and mortgage-backed securities with the losses primarily the result of widening credit spreads from the financial markets crisis during the latter part of the year. Of these unrealized losses, \$54.8 million were related to securities that were rated investment grade or better by at least one nationally recognized statistical rating organization. The \$129.7 million of unrealized losses related to fixed maturity securities in an unrealized loss position for more than one year also related primarily to highly rated domestic corporate securities and mortgage-backed securities and were also the result of widening credit spreads during the latter part of the year. Of these unrealized losses, \$120.1 million were related to securities that were rated investment grade or better by at least one nationally recognized statistical rating organization.

The Company, given the size of its investment portfolio and capital position, has the ability to hold these securities until recovery of market value. In addition, all securities currently in an unrealized loss position are current with respect to principal and interest payments.

The table below displays the aggregate market value and gross unrealized depreciation of fixed maturity securities, by investment category and maturity category by length of time that individual securities had been in a continuous unrealized loss position for the period indicated:

Duration by security type of unrealized loss at December 31, 2007						
Less than 12 months		Greater than 12 months		Total		
Gross Unrealized		Gross Unrealized		Gross Unrealized		
Market Value	Depreciation	Market Value	Depreciation	Market Value	Depreciation	
(Dollars in thousands)						
Fixed maturity securities						
U.S. government						
agencies and authorities	\$ -	\$ -	\$ 5,538	\$ (105)	\$ 5,538	\$ (105)
Foreign governments	31,846	(1,340)	306,329	(3,477)	338,175	(4,817)
All other corporate	215,074	(6,054)	1,646,964	(53,649)	1,862,038	(59,703)
<b>Total fixed maturities</b>	<b>\$ 246,920</b>	<b>\$ (7,394)</b>	<b>\$ 1,958,831</b>	<b>\$ (57,231)</b>	<b>\$ 2,205,751</b>	<b>\$ (64,625)</b>

Duration by maturity of unrealized loss at December 31, 2007						
Less than 12 months		Greater than 12 months		Total		
Gross Unrealized		Gross Unrealized		Gross Unrealized		
Market Value	Depreciation	Market Value	Depreciation	Market Value	Depreciation	
(Dollars in thousands)						
Fixed maturity securities						
Due in one year or less	\$ -	\$ -	\$ 148,014	\$ (367)	\$ 148,014	\$ (367)
Due in one year through five years	52,647	(1,528)	432,271	(8,279)	484,918	(9,807)
Due in five years through ten years	103,889	(1,887)	539,267	(21,585)	643,156	(23,472)
Due after ten years	56,152	(3,542)	188,168	(15,898)	244,320	(19,440)
Mortgage-backed securities	34,232	(437)	651,111	(11,102)	685,343	(11,539)
<b>Total fixed maturities</b>	<b>\$ 246,920</b>	<b>\$ (7,394)</b>	<b>\$ 1,958,831</b>	<b>\$ (57,231)</b>	<b>\$ 2,205,751</b>	<b>\$ (64,625)</b>

The aggregate market value and gross unrealized losses related to investments in an unrealized loss position as of December 31, 2007 were \$2,205.8 million and \$64.6 million, respectively. There were no material concentrations of unrelated losses by issuer, security type or industry within the fixed maturity portfolio. The \$7.4 million of unrealized losses related to fixed maturity securities that had been in an unrealized loss position for less than one year were generally comprised of highly rated government and corporate bonds and the losses were primarily the result of widening credit spreads during the latter part of the year. Of these unrealized losses, \$6.3 million were related to securities that were rated investment grade or better by at least one nationally recognized statistical rating organization. The \$57.2 million of unrealized losses related to fixed maturity securities in an unrealized loss position for more than one year also related primarily to highly rated government and corporate bonds and were the result of widening credit spreads during the latter part of the year. Of these unrealized losses, \$54.1 million related to securities that were rated investment grade or better by at least one nationally recognized statistical rating organization.

The components of net investment income are presented in the table below for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Fixed maturities	\$ 198,753	\$ 175,002
Equity securities	11,813	7,234
Short-term investments and cash	16,293	33,489
Other invested assets		
Limited partnerships	(54,470)	24,018
Total gross investment income	172,389	239,743
Interest credited and other expense	(1,109)	(1,448)
Total net investment income	\$ 171,280	\$ 238,295

The losses from the limited partnership investments emanated from several partnerships that invest in public equity securities. The Company is a passive investor in these partnerships and has less than a 10% participation.

The Company had contractual commitments to invest up to an additional \$74.1 million in limited partnerships at December 31, 2008. These commitments will be funded when called in accordance with the partnership agreements, which have investment periods that expire, unless extended, through 2013.

The components of net realized capital (losses) gains are presented in the table below for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Fixed maturities, market value:		
Other-than-temporary impairments	\$ (89,788)	\$ (4,369)
Gains (losses) from sales	3,293	(4,683)
Equity securities, fair value:		
(Losses) gains from sales	(100,366)	30,341
Losses from fair value adjustments	(118,180)	(8,560)
Other invested assets gains	-	13
Short-term investments gains	96	1
Total net realized capital (losses) gains	\$ (304,945)	\$ 12,743

Proceeds from sales of fixed maturity investments during 2008 and 2007 were \$121.0 million and \$230.6 million, respectively. Gross gains of \$9.3 million and \$0.2 million and gross losses of \$6.0 million and \$4.9 million were realized on those fixed maturity sales during 2008 and 2007, respectively. Proceeds from sales of equity security investments during 2008 and 2007 were \$572.1 million and \$972.7 million, respectively. Gross gains of \$15.5 million and \$34.6 million and gross losses of \$115.8 million and \$4.2 million were realized on those equity sales during 2008 and 2007, respectively.

Included in net realized capital losses for 2008 and 2007 was \$89.8 million and \$4.4 million, respectively, for write-downs in the value of securities deemed to be impaired on an other-than-temporary basis.

### 3. RESERVE FOR LOSSES, LAE AND FUTURE POLICY BENEFIT RESERVE

#### Reserves for losses and LAE.

Activity in the reserve for losses and LAE is summarized for the periods indicated:

(Dollars in thousands)	At December 31,	
	2008	2007
Gross reserves at January 1	\$ 3,079,102	\$ 2,799,175
Less reinsurance recoverables	(292,889)	(229,440)
Net reserves at January 1	<u>2,786,213</u>	<u>2,569,735</u>
Incurred related to:		
Current year	965,025	964,660
Prior years	(158,814)	(43,455)
Total incurred losses and LAE	<u>806,211</u>	<u>921,205</u>
Paid related to:		
Current year	162,894	135,470
Prior years	571,762	615,273
Total paid losses and LAE	<u>734,656</u>	<u>750,743</u>
Loss portfolio transfer	747,022	-
Foreign exchange/translation adjustment	(158,487)	46,016
Net reserves at December 31	3,446,303	2,786,213
Plus reinsurance recoverables	280,397	292,889
Gross reserves at December 31	<u>\$ 3,726,700</u>	<u>\$ 3,079,102</u>

Prior years' reserves decreased by \$158.8 million and \$43.5 million for the years ended December 31, 2008 and 2007, respectively. The 2008 decrease was primarily attributable to favorable development on attritional (non-catastrophe, non-A&E) loss reserves and no further A&E development, partially offset by the change in foreign exchange rates.

The 2007 decrease was the result of favorable development on attritional loss reserves and the change in foreign exchange rates, partially offset by adverse development on A&E reserves as a result of the extensive in-house study by the parent company's actuarial and claims unit.

In addition, gross reserves increased \$647.6 million in 2008, primarily as a result of a loss portfolio transfer agreement between the Company and an affiliate, whereby the Company assumed \$747.0 million of casualty loss reserves.

Reinsurance receivables for both paid and unpaid losses were \$283.5 million and \$299.7 million at December 31, 2008 and 2007, respectively. At December 31, 2008, \$222.5 million, or 78.5%, was receivable from Everest International Reinsurance, Ltd. ("Everest International"); \$41.7 million, or 14.7%, was receivable from Everest Reinsurance Company ("Everest Re") and \$16.0 million, or 5.6%, was receivable from Zurich Financial Services ("Zurich"). No other retrocessionaire accounted for more than 5% of reinsurance receivables.

The Company continues to receive claims under expired insurance and reinsurance contracts, asserting injuries and/or damages relating to or resulting from environmental pollution and hazardous substances, including asbestos. Environmental claims typically assert liability for (a) the mitigation or remediation of environmental contamination or (b) bodily injury or property damage caused by the release of hazardous substances into the land, air or water. Asbestos claims typically assert liability for bodily injury from exposure to asbestos or for property damage resulting from asbestos or products containing asbestos.

The Company's reserves include an estimate of the Company's ultimate liability for A&E claims. The Company's A&E liabilities emanate from Mt. McKinley's direct insurance business and Everest Re's assumed reinsurance business. All of the contracts of insurance and reinsurance under which the Company has received claims during the past three years expired more than 20 years ago. There are significant uncertainties surrounding the Company's reserves for its A&E losses.

The following table summarizes incurred losses with respect to A&E reserves, gross and net of reinsurance, for the periods indicated:

(Dollars in thousands)	At December 31,	
	2008	2007
Gross basis:		
Beginning of period reserves	\$ 289,835	\$ 198,104
Incurred losses	-	121,172
Paid losses	(26,061)	(29,441)
End of period reserves	<u>\$ 263,774</u>	<u>\$ 289,835</u>
Net basis:		
Beginning of period reserves	\$ 289,835	\$ 198,104
Incurred losses	-	121,172
Paid losses	(26,061)	(29,441)
End of period reserves	<u>\$ 263,774</u>	<u>\$ 289,835</u>

At December 31, 2008, the gross reserves for A&E losses were comprised of \$170.7 million representing case reserves reported by ceding companies and \$93.1 million representing IBNR reserves.

With respect to asbestos only, at December 31, 2008, the Company had gross asbestos loss reserves of \$242.8 million, or 92.0%, of total A&E reserves.

In 2007, the Company's parent completed a detailed study of its experience and its cedants' exposures and also considered industry trends. As a result of the study, and other A&E development, the Company's parent ceded additional A&E losses in the amount of \$121.2 million in 2007. The Company has not experienced significant claims activity related to environmental exposures other than asbestos. The Company's A&E reserves represent management's best estimate of the ultimate liability, however, there can be no assurance that ultimate loss payments will not exceed such reserves, perhaps by a significant amount. No additional reserve strengthening was made in 2008.

### Future Policy Benefit Reserve.

Activity in the reserve for future policy benefit is summarized for the periods indicated:

(Dollars in thousands)	At December 31,	
	2008	2007
Balance at beginning of year	\$ 78,417	\$ 100,962
Liabilities assumed	190	168
Adjustments to reserves	6,546	2,414
Benefits paid in the current year	(18,981)	(25,127)
Balance at end of year	\$ 66,172	\$ 78,417

#### 4. FAIR VALUE

Effective January 1, 2007, the Company adopted and implemented FAS 159 for its actively managed equity securities. The Company implemented a more active management strategy for these securities and FAS 159 provided guidance on accounting and presentation of these investments in the Company's financial statements. Upon adoption of FAS 159, the Company recognized a \$27.5 million positive cumulative-effect adjustment to retained earnings.

The Company records fair value re-measurements as net realized capital gains or losses in the statements of operations and comprehensive income (loss). The Company recorded \$118.2 million and \$8.6 million in net realized capital losses due to fair value re-measurement on equity securities at fair value for the year ended December 31, 2008 and 2007, respectively.

The Company's fixed maturities and equity securities are managed by third party investment asset managers and market and fair values for these securities are obtained from third party pricing services retained by the investment asset managers. In limited instances where prices are not provided by the pricing services, price quotes on a non-binding basis are obtained from investment brokers. The investment asset managers have procedures in place to review the reasonableness of the prices from the service providers and may obtain additional price quotes for verification. In addition, the Company tests the prices on a random basis to an independent pricing source. In limited situations, where financial markets are inactive or illiquid, the Company may use its own assumptions about future cash flows and risk-adjusted discount rates to determine fair value.

Fixed maturities are categorized as Level 2, Significant Other Observable Inputs, since a particular security may not have traded but the pricing services are able to use valuation models with observable market inputs such as interest rate yield curves and prices for similar fixed maturities in terms of issuer, maturity and seniority. Valuations that are derived from techniques in which one or more of the significant inputs are unobservable (including assumptions about risk) are categorized as Level 3, Significant Unobservable Inputs. These securities include broker priced securities and valuation of less liquid securities such as commercial mortgage-backed securities and the Company's equity index put options.

Equity securities in U.S. denominated currency are categorized as Level 1, Quoted Prices in Active Markets for Identical Assets, since the securities are actively traded on an exchange and prices are based on quoted prices from the exchange. Equity securities traded on foreign exchanges are categorized as Level 2 due to potential foreign exchange adjustments to fair or market value.

The Company sold six equity index put options based on the Standard & Poor's 500 ("S&P 500") index for total consideration, net of commissions, of \$22.5 million. At December 31, 2008, fair value for these equity put options was \$54.6 million. These contracts each have a single exercise date, with maturities ranging from 12 to 30 years and strike prices ranging from \$1,141.21 to \$1,540.63. No amounts will be payable under these contracts if the S&P 500 index is at or above the strike prices on the exercise dates, which fall between June 2017 and March 2031. If the S&P 500 index is lower than the strike price on the applicable exercise date, the amount due would vary proportionately with the percentage by which the index is below

the strike price. Based on historical index volatilities and trends and the December 31, 2008 index value, the Company estimates the probability for each contract of the S&P 500 index falling below the strike price on the exercise date to be less than 55%. The theoretical maximum payouts under the contracts would occur if on each of the exercise dates the S&P 500 index value were zero. At December 31, 2008, the present value of these theoretical maximum payouts using a 6% discount factor was \$239.6 million.

The Company sold one equity index put option based on the FTSE 100 index for total consideration, net of commissions, of \$6.7 million. At December 31, 2008, fair value for this equity put option was \$6.0 million. This contract has an exercise date of July 2020 and a strike price of £5,989.75. No amount will be payable under this contract if the FTSE 100 index is at or above the strike price on the exercise date. If the FTSE 100 index is lower than the strike price on the exercise date, the amount due will vary proportionately with the percentage by which the index is below the strike price. Based on historical index volatilities and trends and the December 31, 2008 index value, the Company estimates the probability that the FTSE 100 index contract will fall below the strike price on the exercise date to be less than 57%. The theoretical maximum payout under the contract would occur if on the exercise date the FTSE 100 index value was zero. At December 31, 2008, the present value of the theoretical maximum payout using a 6% discount factor and current exchange rate was \$24.2 million.

These equity index put options meet the definition of a derivative under FAS 133. The Company's position in these contracts is unhedged. The Company recorded the change in fair value of \$20.9 million and \$2.1 million for the years ended December 31, 2008 and 2007, respectively, as net derivative expense in the statements of operations and comprehensive (loss) income.

Collateral held in respect to these equity index put options at December 31, 2008, was \$32.2 million.

The fair value was calculated using an industry accepted option pricing model, Black-Scholes, which used the following assumptions:

	At December 31, 2008	
	Contracts based on S & P 500 Index	Contract based on FTSE 100 Index
Equity index	903.3	4,434.2
Interest rate	5.03% to 5.78%	5.43%
Time to maturity	8.4 to 22.3 yrs	11.6 yrs
Volatility	21.5% to 24.4%	25.8%

The following tables present the fair value measurement levels for all assets and liabilities, which the Company has recorded at fair value as of the periods indicated:

		Fair Value Measurement Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(Dollars in thousands)	December 31, 2008			
<b>Assets:</b>				
Fixed maturities, market value	\$ 4,593,307	\$ -	\$ 4,341,104	\$ 252,203
Equity securities, market value	16,884	16,884	-	-
Equity securities, fair value	13	12	1	-
<b>Liabilities:</b>				
Equity index put options	\$ 60,552	\$ -	\$ -	\$ 60,552

		Fair Value Measurement Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(Dollars in thousands)	December 31, 2007			
<b>Assets:</b>				
Fixed maturities, market value	\$ 3,680,000	\$ -	\$ 3,530,007	\$ 149,993
Equity securities, market value	14,797	14,797	-	-
Equity securities, fair value	612,670	476,760	135,910	-
<b>Liabilities:</b>				
Equity index put options	\$ 39,653	\$ -	\$ -	\$ 39,653

The following table presents the fixed maturity investments for which fair value was measured under Level 3, fair value measurements using significant unobservable inputs, for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
<b>Assets:</b>		
Beginning balance at January 1	\$ 149,993	\$ 114,135
Total gains or (losses) (realized/unrealized)		
Included in earnings (or changes in net assets)	9	(508)
Included in other comprehensive income	(901)	210
Purchases, issuances and settlements	74,383	36,156
Transfers in and/or (out) of Level 3	28,719	-
Ending balance at December 31	<u>\$ 252,203</u>	<u>\$ 149,993</u>
The amount of total gains or losses for the period included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses relating to assets still held at the reporting date		
	<u>\$ -</u>	<u>\$ -</u>

The following table presents the equity index put options for which fair value was measured under Level 3, fair value measurements using significant unobservable inputs, for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Liabilities:		
Beginning balance at January 1	\$ 39,653	\$ 37,529
Total (gains) or losses (realized/unrealized)		
Included in earnings (or changes in net assets)	20,900	2,124
Included in other comprehensive income	-	-
Purchases, issuances and settlements	-	-
Transfers in and/or (out) of Level 3	-	-
Ending balance at December 31	<u>\$ 60,552</u>	<u>\$ 39,653</u>
The amount of total gains or losses for the period included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses relating to liabilities still held at the reporting date	<u>\$ 20,900</u>	<u>\$ 2,124</u>

(Some amounts may not reconcile due to rounding.)

## 5. CREDIT LINES

Effective July 27, 2007, Group, Bermuda Re and Everest International entered into a new five year, \$850.0 million senior credit facility with a syndicate of lenders, replacing the December 8, 2004, senior credit facilities, which would have expired on December 8, 2007. Both the July 27, 2007 and December 8, 2004 senior credit facilities are referred to as the "Group Credit Facility". Wachovia Bank, a subsidiary of Wells Fargo Corporation ("Wachovia Bank") is the administrative agent for the Group Credit Facility, which consists of two tranches. Tranche one provides up to \$350.0 million of unsecured revolving credit for liquidity and general corporate purposes, and for the issuance of unsecured standby letters of credit. The interest on the revolving loans shall, at the Company's option, be either (1) the Base Rate (as defined below) or (2) an adjusted London Interbank Offered Rate ("LIBOR") plus a margin. The Base Rate is the higher of (a) the prime commercial lending rate established by Wachovia Bank or (b) the Federal Funds Rate plus 0.5% per annum. The amount of margin and the fees payable for the Group Credit Facility depends on Group's senior unsecured debt rating. Tranche two exclusively provides up to \$500.0 million for the issuance of standby letters of credit on a collateralized basis.

The Group Credit Facility requires Group to maintain a debt to capital ratio of not greater than 0.35 to 1 and to maintain a minimum net worth. Minimum net worth is an amount equal to the sum of \$3,575.4 million plus 25% of consolidated net income for each of Group's fiscal quarters, for which statements are available ending on or after January 1, 2007 and for which consolidated net income is positive, plus 25% of any increase in consolidated net worth during such period attributable to the issuance of ordinary and preferred shares, which at December 31, 2008, was \$3,856.5 million. As of December 31, 2008, Group was in compliance with all Group Credit Facility covenants.

At December 31, 2008, there were no outstanding letters of credit under tranche one and \$411.9 million issued under tranche two of the Group Credit Facility. At December 31, 2007, there were outstanding letters of credit of \$22.0 million and \$288.0 million under tranche one and tranche two of the Group Credit Facility, respectively.

Costs incurred in connection with the Group Credit Facility were \$1.2 million and \$1.3 million for the years ended December 31, 2008 and 2007, respectively.

## 6. LETTERS OF CREDIT

The Company, in conjunction with Group, has arrangements available for the issuance of letters of credit, which letters are generally collateralized by the Company's cash and investments. The Company's agreement with Citibank is a bilateral letter of credit agreement only. On November 6, 2007, the Citibank bilateral letter of credit agreement was decreased by \$50.0 million to \$300.0 million. All other terms of this agreement remain the same. The Company's other facility, the Wachovia Group Credit Facility, involves a syndicate of lenders (see Note 5), with Wachovia acting as administrative agent. At December 31, 2008 and 2007, letters of credit for \$561.1 million and \$473.9 million, respectively, were issued and outstanding. The letters of credit collateralize reinsurance obligations of the Company's operations. The following table summarizes the Company's letters of credit at December 31, 2008.

(Dollars in thousands)

Bank		Commitment	In Use	Date of Expiry
Citibank Bilateral Letter of Credit Agreement		\$ 300,000	\$ 48,771	12/31/2009
			34,006	01/31/2010
			30,000	12/31/2011
			36,414	12/31/2012
Total Citibank Bilateral Agreement		<u>\$ 300,000</u>	<u>\$ 149,191</u>	
Wachovia Group Credit Facility	Tranche One	\$ 350,000	\$ -	
	Tranche Two	500,000	411,877	12/31/2009
Total Wachovia Group Credit Facility		<u>\$ 850,000</u>	<u>\$ 411,877</u>	
Total letters of credit		<u>\$ 1,150,000</u>	<u>\$ 561,068</u>	

## 7. TRUST AGREEMENTS

Bermuda Re has established trust agreements, which effectively use the Company's investments as collateral, as security for assumed losses payable to certain non-affiliated ceding companies. At December 31, 2008 the total amount on deposit in trust accounts was \$75.5 million.

## 8. OPERATING LEASE AGREEMENTS

The future minimum rental commitments, exclusive of cost escalation clauses, at December 31, 2008 for all of the Company's operating leases with remaining non-cancelable terms in excess of one year are as follows:

(Dollars in thousands)

2009	\$ 262
2010	269
2011	269
2012	45
Thereafter	-
Net commitments	<u>\$ 845</u>

This lease, which will expire in 2012, is for the rental of office space. Rental expense was \$0.2 million for the years ended December 31, 2008 and 2007.

## 9. INCOME TAXES

Under Bermuda law, no income or capital gains taxes are imposed on Bermuda Re. The Minister of Finance of Bermuda has also assured Bermuda Re that, pursuant to The Exempted Undertakings Tax Protection Act of 1966, it will be exempt until 2016 from imposition of any such taxes. Bermuda Re's UK branch is subject to separate taxes in the United Kingdom.

The provision for income taxes in the statements of operations and comprehensive income has been determined by reference to the applicable tax laws of jurisdictions in which the income of Bermuda Re is subject to tax. It reflects the permanent differences between financial and taxable income. The significant components of the provision are as follows for the periods indicated:

	Years Ended December 31,	
	2008	2007
(Dollars in thousands)		
Current foreign tax	\$ 31,133	\$ 43,607
Deferred tax expense	-	-
Total income tax expense	\$ 31,133	\$ 43,607

The weighted average expected tax provision has been calculated using the pre-tax income (loss) in each jurisdiction's applicable statutory tax rate. Reconciliation of the difference between the provision for income taxes and the expected tax provision at the weighted average tax rate for the periods indicated is provided below:

	Years Ended December 31,	
	2008	2007
(Dollars in thousands)		
Expected tax provision at weighted average rate	\$ 29,181	\$ 46,159
Other	1,952	(2,552)
Total income tax provision	\$ 31,133	\$ 43,607

Deferred income taxes reflect the tax effect of the temporary differences between the value of assets and liabilities for financial statement purposes and such values as measured by tax laws and regulations. The principal items making up the net deferred income tax asset are as follows for the periods indicated:

	At December 31,	
	2008	2007
(Dollars in thousands)		
Deferred tax assets:		
Net unrealized depreciation of investments	\$ -	\$ 696
Other	-	-
Total deferred tax assets	-	696
Deferred tax liabilities:		
Net unrealized appreciation of investments	-	-
Total deferred tax liabilities	-	-
Net deferred tax assets	\$ -	\$ 696

The Company has not recorded any liability for unrecognized tax benefits and the Company is not aware of any positions which may give rise to significant unrecognized tax benefits within twelve months of the reporting date.

Returns filed in the United Kingdom for ten years, 2005 and prior, are considered final and not subject to adjustment.

## 10. REINSURANCE

The Company utilizes reinsurance agreements to reduce its exposure to large claims and catastrophic loss occurrences. These agreements provide for recovery from reinsurers of a portion of losses and LAE under certain circumstances without relieving the ceding company of its obligations to the policyholders. Losses and LAE incurred and premiums earned are reported after deduction for reinsurance. In the event that one or more of the reinsurers were unable to meet their obligations under these reinsurance agreements, the Company would not realize the full value of the reinsurance recoverable balances. The Company may hold

partial collateral, including letters of credit and funds held, under these agreements. See also Note 6.

Premiums written and earned and incurred losses and LAE are comprised of the following for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Written premiums:		
Direct	\$ 354	\$ 12,941
Assumed	1,730,691	1,746,678
Ceded	(155,623)	(179,984)
Net written premiums	<u>\$ 1,575,422</u>	<u>\$ 1,579,635</u>
Premiums earned:		
Direct	\$ 5,115	\$ 22,677
Assumed	1,712,433	1,710,842
Ceded	(153,808)	(181,766)
Net premiums earned	<u>\$ 1,563,740</u>	<u>\$ 1,551,753</u>
Incurred losses and LAE:		
Direct	\$ 2,237	\$ 16,436
Assumed	885,703	1,015,814
Ceded	(81,729)	(112,250)
Net incurred losses and LAE	<u>\$ 806,211</u>	<u>\$ 920,000</u>

The amounts deducted from losses and LAE incurred for net reinsurance recoveries were \$81.7 million and \$112.3 million for the years ended December 31, 2008 and 2007, respectively. See also Note 3.

The Company engages in reinsurance transactions with Everest Re, Everest National Insurance Company ("Everest National"), Everest International and Mt. McKinley, affiliates, primarily driven by enterprise risk and capital management considerations under which business is assumed or ceded at market rates and terms. These transactions include:

- Effective September 19, 2000, Mt. McKinley and Bermuda Re entered into a loss portfolio transfer reinsurance agreement, whereby Mt. McKinley transferred all of its net insurance exposures and reserves to Bermuda Re.
- Effective October 1, 2001, Everest Re and Bermuda Re entered into a loss portfolio reinsurance agreement, whereby Everest Re transferred all of its Belgium branch net insurance exposures and reserves to Bermuda Re.
- For premiums earned and losses incurred for the period January 1, 2002 through December 31, 2002, Everest Re, Everest National and Everest Security Insurance Company ("Everest Security") entered into an Excess of Loss Reinsurance Agreement with Bermuda Re, covering workers' compensation losses occurring on and after January 1, 2002, as respects new, renewal and in force policies effective on that date through December 31, 2002. Bermuda Re is liable for any loss exceeding \$100,000 per occurrence, with its liability not to exceed \$150,000 per occurrence.
- Effective January 1, 2002 for the 2002 underwriting year, Everest Re ceded 20.0% of its net retained liability to Bermuda Re through a quota share reinsurance agreement ("whole account quota share").

- Effective January 1, 2003, Everest Re and Bermuda Re amended the whole account quota share, through which Everest Re previously ceded 20.0% of its business to Bermuda Re so that effective January 1, 2003 Everest Re ceded 25.0% to Bermuda Re of the net retained liability on all new and renewal policies underwritten during the term of this agreement. This amendment remained in effect through December 31, 2003.
- Effective January 1, 2003, Everest Re entered into a whole account quota share with Bermuda Re, whereby Everest Re's Canadian branch ceded to Bermuda Re 50.0% of its net retained liability on all new and renewal property business. This remained in effect through December 31, 2006.
- Effective January 1, 2004, Everest Re and Bermuda Re amended the whole account quota share through which Everest Re previously ceded 25.0% of its business to Bermuda Re so that effective January 1, 2004 Everest Re ceded 22.5% to Bermuda Re of the net retained liability on all new and renewal covered business written during the term of this agreement. This amendment remained in effect through December 31, 2005.
- Effective January 1, 2004, Bermuda Re entered into a whole account quota share with Everest International, whereby Bermuda Re's UK branch ceded to Everest International 25.0% of its net retained liability on all new and renewal policies underwritten during the term of this agreement. This remained in effect through December 31, 2005.
- Effective January 1, 2006, Everest Re and Bermuda Re amended the whole account quota share so that for all new and renewal business recorded on or after January 1, 2006, Everest Re ceded 31.5% of its casualty business to Bermuda Re and Everest Re ceded 18.0% of its property business to Bermuda Re. However, in no event shall the loss cessions to Bermuda Re relating to any one occurrence on the property business exceed \$112.5 million (18.0% of \$625.0 million). The property portion of this amendment remained in effect through December 31, 2006. The casualty portion remained in effect through December 31, 2007.
- Effective January 1, 2006, Bermuda Re and Everest International amended the whole account quota share, through which Bermuda Re previously ceded 25.0% of its UK branch business to Everest International so that effective January 1, 2006, Bermuda Re ceded 30.0% to Everest International of the net retained liability on all new and renewed policies underwritten by its UK branch during the term of this agreement. However, in no event shall the loss cessions to Everest International relating to any one occurrence on the property business exceed £68.6 million (USD \$120.0 million) (being 30% of £228.5 million (USD \$400.0 million)). This amendment remained in effect through December 31, 2008.
- Effective January 1, 2007, Everest Re and Bermuda Re amended the whole account quota share so that for all new and renewal business recorded on or after January 1, 2007, Everest Re cedes 60.0% of its Canadian branch property business to Bermuda Re.
- Effective January 1, 2007, Everest Re and Bermuda Re amended the whole account quota share so that for all new and renewal property business recorded on or after January 1, 2007, Everest Re ceded 22.5% to Bermuda Re. However, in no event shall the loss cessions to Bermuda Re relating to any one occurrence on the property business exceed \$117.0 million (90.0% of \$130.0 million). This amendment remained in effect through December 31, 2007.

- Effective January 1, 2008, Everest Re and Bermuda Re amended the whole account quota share so that for all new and renewal casualty and property business recorded on or after January 1, 2008, Everest Re ceded 36.0% to Bermuda Re. However, in no event shall the loss cessions to Bermuda Re relating to any one catastrophe occurrence on the property business exceed \$117.0 million (90.0% of \$130.0 million) or in the aggregate for each underwriting year for all property catastrophes exceed \$247.5 million (90.0% of \$275.0 million). This amendment remained in effect through December 31, 2008.
- Effective October 1, 2008, Everest Re and Bermuda Re entered into a loss portfolio transfer reinsurance agreement, whereby Everest Re transferred a percentage of its net loss reserves (\$747.0 million) corresponding to all existing open and future liabilities at December 31, 2007, arising from policies, insurance or reinsurance written or renewed by or on behalf of Everest Re during the period of January 1, 2002 through December 31, 2007, classified by Everest Re as casualty.
- Effective January 1, 2009, Everest Re and Bermuda Re amended the whole account quota share whereby, for all new and renewal casualty and property business recorded on or after January 1, 2009, Everest Re will cede 36% to Bermuda Re. However, in no event shall the loss cessions to Bermuda Re relating to any one occurrence exceed \$122.7 million (81.8% of \$150.0 million) or in the aggregate for each underwriting year for all occurrences exceed \$265.9 million (81.8% of \$325.0 million).
- Effective January 1, 2009, Bermuda Re and Everest International amended the whole account quota share, through which Bermuda Re previously ceded 30.0% of its UK branch business to Everest International so that effective January 1, 2009, Bermuda Re will cede 50% to Everest International of the net retained liability on all new and renewed policies underwritten by its UK branch during the term of this agreement. However, in no event shall the loss cessions to Everest International relating to any one occurrence on the property business exceed €100.0 million, being 50% of €200.0 million.

The following table summarizes the premiums and losses assumed and ceded by the Company to and from its affiliates for the periods indicated:

**Everest Re and subsidiaries and Mt. McKinley**

(Dollars in thousands)

	Years Ended December 31,	
	2008	2007
Assumed written premiums	\$ 947,694	\$ 837,129
Assumed earned premiums	916,094	820,400
Assumed losses and LAE	467,901	540,814

**Everest International**

(Dollars in thousands)

	Years Ended December 31,	
	2008	2007
Ceded written premiums	\$ 155,147	\$ 179,902
Ceded earned premiums	153,332	181,683
Ceded losses and LAE	80,435	111,847

Everest Re sold the net assets of its UK branch to Bermuda Re and provided Bermuda Re with a reserve indemnity agreement allowing for indemnity payments of up to 90% of £25.0 million of the excess of 2002 and prior reserves, provided that any recognition of profit from the reserves for 2002 and prior underwriting years are taken into account. The limit available under this agreement was fully exhausted at December 31, 2004.

## 11. COMPREHENSIVE (LOSS) INCOME

The following table presents the components of comprehensive (loss) income for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Net (loss) income	\$ (14,954)	\$ 427,172
Other comprehensive (loss) income, before tax:		
Unrealized (losses) gains on securities arising during the period	(4,193)	14,788
Less: reclassification adjustment for realized losses (gains) included in net (loss) income	86,399	9,038
Foreign currency translation adjustments	(168,523)	6,924
Other comprehensive (loss) income, before tax	(86,317)	30,750
Income tax (expense) benefit related to items of other comprehensive (loss) income:		
Tax (expense) benefit from unrealized losses (gains) arising during the period	(47,915)	(3,399)
Tax reclassification due to realized losses (gains) included in net (loss) income	-	-
Total income tax (expense) benefit related to items of other comprehensive (loss) income:	(47,915)	(3,399)
Other comprehensive (loss) income, net of tax	(134,232)	27,351
Comprehensive (loss) income	\$ (149,186)	\$ 454,523

The following table shows the components of the change in accumulated other comprehensive (loss) income for the periods indicated:

(Dollars in thousands)	Years Ended December 31,	
	2008	2007
Beginning balance of unrealized losses on securities	\$ (32,862)	\$ (25,833)
Current period change in unrealized losses on securities	34,291	20,427
Adjustment to initially apply FAS 159, net of tax	-	(27,456)
Ending balance of unrealized gains (losses) on securities	1,429	(32,862)
Beginning balance of foreign currency translation adjustments	38,638	31,714
Current period change in foreign currency translation adjustments	(168,523)	6,924
Ending balance of foreign currency translation adjustments	(129,885)	38,638
Ending balance of accumulated other comprehensive (loss) income	\$ (128,456)	\$ 5,776

## 12. DIVIDEND RESTRICTIONS AND STATUTORY FINANCIAL INFORMATION

### Dividend Restrictions.

Under Bermuda law, Bermuda Re is prohibited from declaring or making payment of a dividend if it fails to meet its minimum solvency margin or minimum liquidity ratio. As a long term insurer, Bermuda Re is also unable to declare or pay a dividend to anyone who is not a policyholder unless, after payment of the dividend, the value of the assets in its long term business fund, as certified by its approved actuary, exceeds its liabilities for long term business by at least the \$250,000 minimum solvency margin. Prior approval of the Bermuda Monetary Authority is required if Bermuda Re's dividend payments would reduce its prior year-end total statutory capital by 15% or more, or dividends paid would exceed 25% of its prior year-end total statutory capital and surplus.

**Statutory Financial Information.**

Bermuda Re prepares its statutory financial statements in conformity with accounting principles set forth in Bermuda in The Insurance Act 1978, amendments thereto and related regulations. The capital and statutory surplus of Bermuda Re was \$2,181.6 million and \$2,342.5 million at December 31, 2008 and 2007, respectively. The statutory net income of Bermuda Re was \$42.3 million and \$421.4 million for the years ended December 31, 2008 and 2007, respectively.

**13. CONTINGENCIES**

In the ordinary course of business, the Company is involved in lawsuits, arbitrations and other formal and informal dispute resolution procedures, the outcomes of which will determine the Company's rights and obligations under insurance, reinsurance and other contractual agreements. In some disputes, the Company seeks to enforce its rights under an agreement or to collect funds owing to it. In other matters, the Company is resisting attempts by others to collect funds or enforce alleged rights. These disputes arise from time to time and are ultimately resolved through both informal and formal means, including negotiated resolution, arbitration and litigation. In all such matters, the Company believes that its positions are legally and commercially reasonable. While the final outcome of these matters cannot be predicted with certainty, the Company does not believe that any of these matters, when finally resolved, will have a material adverse effect on the Company's financial position or liquidity. However, an adverse resolution of one or more of these items in any one quarter or fiscal year could have a material adverse effect on the Company's results of operations in that period.

**14. RELATED-PARTY TRANSACTIONS**

During the normal course of business, the Company, through its affiliates, engages in reinsurance and brokerage and commission business transactions with companies controlled by or affiliated with its outside directors. Such transactions, individually and in the aggregate, are not material to the Company's financial condition, results of operations and cash flows.

The Company engages in reinsurance transactions with Everest Re, Everest National, Everest Security and Mt. McKinley under which business is assumed and Everest International under which business is ceded. See also Note 10.