CIRCULAR

Shipowners Claims Bureau, Inc., Manager
60 Broad Street – 37th Floor
New York, New York 10004 U.S.A.

THE AMERICAN CLUB

Tel: 212-847-4500
Fax: 212-847-4599
E-mail: info@american-club.net
Website: www.american-club.com

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TO MEMBERS OF THE ASSOCIATION

Dear Member:

SUPPLEMENTARY CALL AND CLOSURE OF THE 2003 POLICY YEAR, AND DEVELOPMENT OF OPEN POLICY YEARS

At its recent meeting on March 16, 2006, the Board reviewed the status of the 2003 policy year. They also gave consideration to the development of policy years 2004 and 2005, as well as the position of the Contingency Fund balance.

This Circular describes the Board's decisions in regard to the status of the open policy years, the Contingency Fund balance, and the need to make a single final supplementary call to close the 2003 policy year.

Closure of the 2003 Policy Year with Supplementary Call

The 2003 policy year proved to be a difficult year to predict, as it was forecast to close in surplus by about $1 million when first reported in the December 31, 2003 Annual Report. However, due to the Club's successful increase in diversified membership and tonnage on risk, premiums written had increased from $37 million for the 2001 policy year to about $85 million for the 2003 policy year. Losses incurred in any policy year are directly associated with the level of premium (risk) written. Therefore, forecasting ultimate losses for any policy year is based on a database of previous years' ultimate loss development patterns relative to the level and type of risk written. Because of the significant change in the Club's risk profile over a short period of time, traditional loss development assumptions which had proven valid in the past were proven incorrect in initial projections. The new loss development pattern for the year became more apparent after June 30, 2004 when a greater than expected number of claims in the $0 to $500,000 layer were notified to the Club. As a result of this adverse development, a Circular was issued on December 7, 2005 advising the membership of the likelihood of an additional supplementary call being levied for the 2003 policy year.

The 2003 policy year also experienced one notable claim – the Tasman Spirit grounding at the Port of Karachi in July 2003. While the Tasman Spirit grounding received a great deal of media attention, it had a nominal affect on the development to the policy year. The Club's exposure, after pool and reinsurance recoveries, is limited to approximately $3.5 million based on current estimates. The Club's handling of this complex matter led to much favorable commentary and resulted in the American Club being chosen as the Lloyd's List P&I Club of the Year, an honor of which we are particularly proud.

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A recently completed review of all open claims and independent actuarial advice together indicate the 2003 policy year deficit will not materially improve from its present position. The Board had considered the use of the Contingency Fund to eliminate a part of the year's deficit, but unanimously decided that would not be in the best interest of the Club's plan to build capital to a more desirable level.

Accordingly, in order to cure the deficit and close the 2003 policy year, the Board has ordered a Final Supplementary Call in an amount equal to 30% of Estimated Total Cost (ETC) of all mutual premiums. This will be levied as of April 30, 2006 and will be payable in two equal installments on July 20, 2006 and October 20, 2006. It is the Board's intention that the year be closed as of June 30, 2006 with no further calls.

While the Board of Directors and the Managers are disappointed in the adverse development of the 2003 policy year and the need to assess additional premium, we remain confident that the improving quality of tonnage entered and the imposition of strict underwriting guidelines will result in significant improvement of the Club's capital adequacy.

Development of 2004 and 2005 Policy Years

The 2004 policy year remains in surplus, reflecting tighter underwriting guidelines, increased ship surveys, and a more proactive safety program. Original surplus projections have diminished somewhat due in part to the American Club's share of higher than expected IG Pool losses incurred by other Clubs'. We remain confident that the 2004 policy year will close in surplus without the need for additional supplementary calls.

During the 2005 policy year the Club continued to consolidate less profitable tonnage and anticipated a technical underwriting surplus. However, due in part to Katrina wreck removal claims in excess of $6 million, an increase in the value of cargo claims as a result of the increased values of commodities being carried, and a more conservative loss reserving practice resulting in higher year-end reserves for unreported claims, the Club will be reporting a deficit of approximately 15% at December 31, 2005. While it is much too soon to determine the final position of this policy year, the Club's increased investment portfolio to more than $200 million could generate sufficient returns to balance the policy year before it is closed while adding to surplus.

The Loss Prevention & Technical Services Department performed 424 condition surveys during the 2005 policy year, an increase of 20% over the previous year. Consequently, the Managers have taken on additional qualified technical staff and have significantly improved the survey review process and response time to Members.

In addition, the Club's Pre-Employment Medical Examination (PEME) program continued into its second year. The first year results were very encouraging as it has been estimated that the Club saved more than $2 million on illness-related claims by conducting intensive medical screenings and examinations and thereby preventing unfit seamen from joining Member's vessels.

S & P and New York Regulators

The membership may be aware that the American Club has recently been subject to a rating adjustment by S&P due to statutory surplus falling below the Risk Based Capital (RBC) Control levels. The RBC is a capital adequacy model regulators use to monitor insurance companies, and is similar to S&P's capital adequacy model used in their rating process. S&P tends to look at P&I clubs as insurance companies, rather than as not for profit assessable mutuals and when capital falls below certain levels internal guidelines require that ratings be reviewed and adjusted.

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It is important to note, however, that the American Club's statutory surplus at December 31, 2005 exceeded the New York State Insurance Department's regulated minimum surplus of $7,500,000. This was communicated to S&P in a follow-up meeting on April 4, 2006. Additional meetings with S&P are scheduled later this spring to review the effect of the Club's implementation of enhanced underwriting parameters, loss prevention programs, and capital forecasting models.

Invested Assets and Capital

The American Club does not have a liquidity problem, and due to the growth in premiums written and collected over the past years it now enjoys a record invested asset portfolio in excess of $200 million. The Board has recently retained the services of an investment consulting team from Merrill Lynch to select investment managers and structure the Club's portfolio to maximize performance while preserving capital. Expected increased investment returns on the higher portfolio value will contribute more to the bottom line than in previous years and will provide the Club with capital.

The Board and its Managers are committed to strengthening the Club's capital while building a quality book of business and maintaining the highest level of service to its membership. The American Club is in an excellent position to accomplish these goals and improve its rating to investment grade in the near future.

Sincerely yours,

Vincent J. Solarino
President & C.O.O.
Shipowners Claims Bureau, Inc.
Managers for American Steamship Owners Mutual
Protection and Indemnity Association, Inc.