

QUANTA CAPITAL HOLDINGS LTD
Form 10-K
March 14, 2008

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File number: 000-50885

QUANTA CAPITAL HOLDINGS LTD.
(Exact name of registrant as specified in its charter)

Bermuda

n/a (State or other jurisdiction of

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incorporation or organization) (I.R.S. Employer Identification No.) 22 Church Street, Penthouse
Hamilton, Bermuda HM

(Address of principal executive offices) HM 11

(Zip code) Securities registered pursuant to Section 12(b) of the Act: Title of each class Name of each exchange on
which registered Common Shares, Par Value \$0.01 The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the
Act. Yes No

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of
the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant
was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained
herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements
incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or
a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company"
in Rule 12b-2 of the Exchange Act. (Check one).

Accelerated Filer Accelerated Filer Non-Accelerated Filer (do not check if a smaller reporting company) }
Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes
No

The aggregate market value of the Registrant's common shares, \$0.01 par value, held by non-affiliates of the
Registrant as of June 30, 2007, was \$167,819,906. For purposes of the foregoing calculation only, all directors,
executive officers and 10% beneficial owners have been deemed affiliates.

Number of the Registrant's common shares outstanding as of February 15, 2008 was 70,135,502.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's proxy statement for the 2008 annual general meeting of shareholders are incorporated by
reference into Part III.

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PART I

Item 1. Business

General

In this annual report, references to the “company,” “we,” “us” or “our” refer to Quanta Capital Holdings Ltd. and its subsidiaries (which include, Quanta Reinsurance Ltd., Quanta U.S. Holdings Inc., Quanta Reinsurance U.S. Ltd., Quanta 4000 Holding Company Ltd., Quanta Indemnity Company, Quanta Specialty Lines Insurance Company, Quanta Europe Ltd., Quanta Technical Services LLC and, on or before February 13, 2008, Quanta 4000 Ltd.) unless the context suggests otherwise. We refer to Quanta Reinsurance Ltd., Quanta Reinsurance U.S. Ltd., Quanta Indemnity Company, Quanta Specialty Lines Insurance Company, Quanta Europe Ltd., Quanta 4000 Ltd. and Pembroke JV Ltd. as Quanta Re, Quanta U.S. Re, Quanta Indemnity, Quanta Specialty Lines, Quanta Europe, Syndicate 4000 and Pembroke JV, as the case may be. References to Quanta Holdings refer solely to Quanta Capital Holdings Ltd.

In this annual report, amounts are expressed in U.S. dollars, except as otherwise indicated, and the financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America, except as otherwise indicated. We have registered the mark “Quanta” in the U.S. Patent and Trademark Office. All other brand names or trade names appearing in this annual report are the property of their respective holders.

Overview and Recent Events

Quanta Holdings was incorporated on May 23, 2003 as a Bermuda holding company formed to provide specialty lines insurance, reinsurance, risk assessment and risk technical services on a global basis through its affiliated companies. Following events in the first half of 2006, we have been conducting a self-managed run-off of our insurance and reinsurance businesses as more fully described below. Until February 13, 2008, we also participated in the “A” rated Lloyd’s market through Syndicate 4000.

We conduct our operations principally through our subsidiaries domiciled in Bermuda, Ireland and the United States. We may change our corporate organization from time to time as we run-off our business.

On February 13, 2008, we completed the disposition of all of our interests at Lloyd’s which was our only line of business not in active run-off and on March 13, 2008, we announced that we declared a dividend of \$1.75 per common share payable on March 28, 2008 to our shareholders of record on March 25, 2008. We continue to consider and evaluate strategic alternatives that may include the sale of the company or some or all of our remaining businesses or assets, or a combination of one or more alternatives. There can be no assurance as to the timing, structure or terms of such a transaction.

Our Business

Run-off of Our Specialty Insurance and Reinsurance Portfolios

On March 2, 2006, A.M. Best announced that it had downgraded the financial strength rating assigned to Quanta Re and its subsidiaries and Quanta Europe to “B++” (very good), under review with negative implications. The A.M. Best “A” (excellent) rated Lloyd’s market, including Syndicate 4000, was not subject to the rating downgrade. Following this rating action, our board of directors decided to explore strategic alternatives, including the potential sale of some or all

of our businesses, the run-off of certain product lines or business or a combination of alternatives. On June 7, 2006, A.M. Best, downgraded our financial strength rating, from “B++” (Very Good) to “B” (Fair). Following this rating action, A.M. Best, at our request, withdrew the financial strength ratings of Quanta Holdings and its operating subsidiaries, excluding Syndicate 4000 in the A-rated Lloyd’s market. During the third quarter of 2006, following A.M. Best’s rating actions our board of directors,

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after a review of strategic alternatives, decided to substantially cease writing new insurance and reinsurance business and commenced a self-managed run-off of our remaining insurance and reinsurance portfolios. Also during the third quarter of 2006, we sold ESC, a subsidiary through which we provided environmental consulting services, including investigation, remediation and engineering services, assessment services, information management services and other technical services.

The self-managed run-off of insurance and reinsurance portfolios, is expected to continue to take place over a number of years (because our policy obligations remain in force during that period) and may result in the dissolution or sale of our Company. During this time, the main activities we are undertaking are:

negotiating cancellations, commutations, novations and portfolio transfers with counterparties;

receivables and reinsurance recoverables;

investment assets;

handling by our third party claims administrators; and

negotiating with regulatory agencies in multiple jurisdictions, including regarding license renewals, withdrawal plans and return of capital following satisfaction of policy obligations and other requirements.

- collecting premium
- managing our
- supervising claims
- reporting to and

Until we substantially ceased writing new business, our two traditional product lines were specialty insurance and specialty reinsurance. Our specialty insurance product line focused on professional liability, environmental liability, fidelity and crime, technical risk property, trade credit, political risk and surety. Our specialty reinsurance product line included marine and aviation reinsurance and casualty reinsurance. Some of the products offered to our clients were written as programs or as a structured product or a combination of a traditional policy with a program or a structured product. Programs rely on third parties, called program managers, who are engaged in the business of managing one or a combination of the underwriting, administration and claim related activities of a group of distinct specialty insurance policies under the supervision of an insurance company. Traditionally, program managers contract with an insurance company, which provides the insurance policies and capacity and supervises the program manager. Each group of policies and the related relationship with the program manager is called a program. Our largest program was our residential builders' and contractors' program that provides general liability, builders' risk and excess liability insurance coverages and reinsurance warranty coverages for new home contractors throughout the U.S. We refer to this program as the HBW program.

Syndicate 4000 at Lloyd's

On February 13, 2008, we sold Quanta 4000 and our interest in Pembroke JV to Chaucer Holdings PLC and received the return of \$117.2 million which had previously been pledged to Lloyd's as security for the business being written by Syndicate 4000. Therefore, we no longer participate in Syndicate 4000. The sale of our insurance operations at Lloyd's follows the restructuring of those operations on March 1, 2007 through which we diversified the capital that was provided to Syndicate 4000 by obtaining 10% of this capital commitment from a subsidiary of Chaucer Holdings PLC and maintaining the capital we had previously pledged which then accounted for the remaining 90% of Syndicate 4000's capital. This restructuring also resulted in the appointment of Pembroke Managing Agency as the managing agent of Syndicate 4000, a role that was previously held by a subsidiary of Chaucer Holdings PLC.

During 2007, Syndicate 4000 wrote financial institution, professional indemnity and directors' and officers', specie and fine art coverage in the A.M. Best "A" rated Lloyd's market in London. The location of the risks that were written in Syndicate 4000 may be anywhere in the world. Syndicate 4000 was the market lead on a significant number of policies in the syndicate, which allowed it to deal with the broker or insured in establishing policy terms and managing particular claims.

Our Website

We maintain a website at www.quantaholdings.com where we make available, free of charge, our annual, quarterly and other reports, proxy statements and other information generally on the same

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day as we electronically file such material with, or furnish it to, the U.S. Securities and Exchange Commission (the “SEC”). Information about the code of business conduct on our website and any amendment or waivers is included in Part III, Item 10 below. Information contained on our website is not part of this annual report.

Claims Management

In the fourth quarter of 2007, we outsourced our claims to third party claim administrators, over whom we have direct oversight. The third party claims administrators strive to investigate, evaluate and settle claims as efficiently and effectively as possible.

When a claim is reported, the third party claims administrators conduct an initial review of the validity of the claim and communicate the assessment of coverage and, if possible, the proposed method of handling the claim to the insured. Depending on the severity, the third party claims administrators also communicate with our management team. We base the authority for payment and establishing reserves on the level and experience of our management team.

We have established procedures, along with our third-party claim administrators, to record reported insurance claims upon receipt of notice of the claim. To assist with the adjustment and tracking of losses, we have established an information database for all insurance claims. The database is also used for management reporting and accumulation of significant reported events.

The third party claims administrators draw on internal and external resources to analyze the basis for coverage and determine the proper settlement of claims. We have also established networks of external legal and claims experts to augment the third party claims administrators.

With respect to reinsurance contracts, claims are mainly managed by the claims department of the ceding company or primary insurer. As individual claims become larger and more complex, we may confer with underlying carriers and ceding companies. From time to time, our claims professionals conduct audits of specific claims and the overall claims procedures of our clients. Through these audits, we seek to evaluate their claims-handling practices, including the organization of their claims departments, their fact-finding and investigation techniques, their reinsurance loss notification procedures, the adequacy of their reserves, their negotiation and settlement practices, their adherence to claims-handling guidelines and the validity of claims.

Reserves

We are required to establish reserves for losses and loss expenses under applicable insurance laws and regulations and U.S. GAAP. These reserves are balance sheet liabilities representing estimates of future amounts required to pay losses and loss expenses for insured and/or reinsured claims that have occurred at or before the balance sheet date, whether already known to us or not yet reported. Our policy is to establish these losses and loss reserves prudently after considering all information known to us as of the date they are recorded.

Loss reserves fall into two categories: case reserves for reported losses and loss expenses associated with a specific reported insured claim and reserves for incurred but not reported, or IBNR, losses and loss expenses. We have established these two categories of loss reserves as follows:

- Case reserves — Following our analysis of a notice of claim received from an insured, broker or ceding company, we

determine whether the claim is valid and, if so, we establish a case reserve for the estimated amount of its ultimate settlement and its estimated loss expenses. We establish case reserves based upon the availability of coverage and may subsequently supplement or reduce the reserves as our claims department deems necessary. We also review our case reserves on a quarterly basis.

- IBNR reserves — We estimate and establish reserves for loss amounts incurred but not yet reported, including expected development of reported claims. These IBNR reserves include estimated loss expenses. We calculate IBNR reserves by using generally accepted actuarial techniques. We rely on the most recent information available, including pricing information, industry information and our historical reported claims data. We will revise these reserves for losses and loss expenses as additional information becomes available and as claims are reported and paid. We also review our IBNR reserves on a quarterly basis.

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Loss reserves represent our best estimate, at a given point in time, of the ultimate settlement and administration cost associated with incurred claims. Our ultimate liability may exceed or be less than these estimates. The process of estimating loss reserves requires significant judgment due to a number of variables. Internal and external events, such as fluctuations in inflation, judicial trends, legislative changes and changes in claims handling procedures, will affect these variables. We are not able to directly quantify many of these items, particularly on a prospective basis. There may also be significant lags between the occurrence of the insured event and the time it is actually reported to us.

Several aspects of our insurance and reinsurance products we offered until we ceased writing new business and our Lloyd's insurance products further complicate the actuarial reserving techniques for loss reserves as compared to other insurance and reinsurance carriers. Among these aspects are the differences in our policy forms from more traditional forms, the lack of complete historical data for losses and our expectation that losses in excess of our attachment levels will be characterized by low frequency and high severity claims. All of these factors tend to limit the amount of relevant loss experience that we can use to gauge the emergence, severity and payout characteristics of our loss reserves.

We use statistical and actuarial methods to estimate our ultimate expected losses and loss expenses. Several years may pass between the time an insured or reinsured reports a loss to us and the time we settle our liability. During this period, we will learn additional facts and trends related to the loss. As we learn these additional facts and trends, we will adjust case reserves and incurred but not reported reserves as necessary. These adjustments will sometimes require us to increase our overall reserves and at other times will require us to reallocate incurred but not reported reserves to specific case reserves.

We base reserves for losses and loss expenses in part upon our estimates of losses. Initially, it may be difficult for us to estimate losses based upon our own historical claim experiences because of our lack of operating history. Therefore, we utilize commercially available models to evaluate future trends and estimate our ultimate claims costs.

U.S. GAAP does not permit us to establish loss reserves until the occurrence of an actual loss event. Once such an event occurs, we establish reserves based upon estimates of total losses as a result of the event and our estimate of the portion of the loss we have insured or reinsured. As a result, we set aside only loss reserves applicable to losses incurred up to the reporting date, with no allowance for the provision of a contingency reserve to account for expected future losses. We will estimate and recognize losses arising from future events at the time the loss is incurred.

To assist us in establishing appropriate reserves for losses and loss expense, we analyze a significant amount of insurance industry information with respect to the pricing environment and loss settlement patterns. In combination with our individual pricing analyses, we use this industry information to guide our loss and loss expense estimates. We regularly review these estimates, and we reflect adjustments, if any, in earnings in the periods in which they are determined. We have engaged, and we expect that we will continue, from time to time, to engage, independent external actuarial specialists to review specific reserving methods and results.

With respect to the year ended December 31, 2007, in establishing our reserves for losses and loss expenses, we reviewed reserve estimates of an actuary employed with our company and of an external actuary specialist. We recorded these reserves as of the year ended December 31, 2007 based on the highest aggregate reserve amount of the estimates we reviewed. While we believe that we are able to make a reasonable estimate of our ultimate losses, we may not be able to predict our ultimate claims experience as reliably as other companies that have had insurance and reinsurance operations for a period of time, and we cannot assure you that our losses and loss expenses will not exceed our total reserves.

For more discussion of our estimation and establishment of loss reserves, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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Ceded Reinsurance

During 2007, Syndicate 4000 ceded a portion of its written premiums through excess of loss treaty and facultative reinsurance contracts, as well as other agreements, which provide substantially similar financial protections. Prior to ceasing the writing of insurance, we also ceded a portion of our written premiums and purchased retrocessional coverage, which is reinsurance of a reinsurer's business.

We use ceded reinsurance to lower our net exposure to our planned net limit and risk of individual loss, to control our aggregate exposures to a particular risk or class of risks and to reduce our overall risk of loss. Reinsurance companies cede risks under retrocessional agreements to other reinsurers, known as retrocessionaires, for reasons similar to those that cause primary insurers to purchase reinsurance. The amount of ceded reinsurance and retrocessional protection that we purchased varied based on business segment market conditions, pricing terms and credit risk, as well as other factors.

Ceded reinsurance and retrocessional protection do not relieve us of our obligations to our insureds or reinsureds. We must pay these obligations without the benefit of reinsurance to the extent our reinsurers or retrocessionaires do not pay us. We evaluate and monitor the financial condition of our reinsurers and monitor concentrations of credit risk. We have sought to purchase reinsurance from entities rated "A-" or better by S&P or A.M. Best, and we regularly monitor its collectibility, making balance sheet provisions for amounts we consider potentially uncollectible and requesting collateral where possible.

Investments

Our board of directors established our investment policies and mandated a list of authorized investments for company funds. Management implements our investment strategy with the assistance of external managers, who use guidelines which are created by us and compliant with the investment mandates of our board to establish their portfolios. Our investment guidelines specify minimum criteria on the overall credit quality, liquidity and risk-return characteristics of our investment portfolio and include limitations on the size of particular holdings, as well as restrictions on investments in different asset classes. The board of directors monitors our overall investment returns and reviews compliance with our investment guidelines.

Our investment strategy seeks to preserve principal and maintain liquidity while trying to maximize total return through a high quality, diversified portfolio. Investment decision making is guided mainly by the nature and timing of our expected liability payouts, management's forecast of our cash flows and the possibility that we will have unexpected cash demands, for example, to satisfy claims due to catastrophic losses. Our investment portfolio currently consists mainly of highly rated and liquid fixed income securities. However, to the extent our insurance liabilities are correlated with an asset class outside our minimum criteria, our investment guidelines will allow a deviation from those minimum criteria provided such deviations reduce overall risk. In addition, although we record our investments at fair value as required by GAAP and based on information provided by our external investment managers, there can be no assurance that we would collect these amounts in cash if we were to liquidate portions or our entire investment portfolio at this time. For more information about our investments, see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" below.

Our investment guidelines require compliance with applicable local regulations and laws. Without board approval, we will not purchase financial futures, forwards, options, swaps and other derivatives, except for instruments that are purchased as part of our business, for purposes of hedging capital market risks (including those within our structured product transactions), or as replication transactions, which are defined as a set of derivative, insurance and/or

securities transactions that when combined produce the equivalent economic results of an investment meeting our investment guidelines. While we expect that the majority of our investment holdings will continue to be denominated in U.S. dollars, we may make investments in other currency denominations depending upon the currencies in which loss reserves are maintained, or as may be required by regulation or law.

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Risk Management in Syndicate 4000

In Syndicate 4000, during 2007, underwriting authority was granted to Mark H. Wheeler who, in turn, issued detailed letters of underwriting authority to each of the leaders of our product lines at Lloyd's. Mr. Wheeler reviewed these letters annually. These letters contain underwriting eligibility criteria and quantifiable limits depending on the product line.

While we were conducting insurance business through Syndicate 4000, we believe we employed a disciplined approach to underwriting and risk management that relied heavily upon the collective underwriting expertise of our management and staff. We believe this expertise was guided by the following underwriting principles:

- Our own independent pricing or risk review of insurance and facultative risks;
- Acceptance of only those risks that we believed would earn a level of profit commensurate with the risk they present; and
- Limitation of the business we accepted to only that business that was consistent with our corporate risk objectives.

Additionally, underwriters at Syndicate 4000 used contract exclusions and terms and conditions, as appropriate, to further eliminate particular risk exposures that our underwriting team deems to be unacceptable.

Relationships with Brokers in Syndicate 4000

During 2007, Syndicate 4000 produced substantially all of its business through insurance brokers worldwide who receive a brokerage commission usually equal to a percentage of gross premiums. Brokerage commissions are generally negotiated on a policy by policy basis. Aon Ltd and Marsh Ltd. accounted for approximately 19% and 17% of the gross premiums of Syndicate 4000 during 2007. Eight other brokers accounted for approximately 41% of additional gross premiums of Syndicate 4000 during 2007.

Competition for Syndicate 4000

The insurance industry is highly competitive. During 2007, Syndicate 4000 competed both within the Lloyd's market and with insurance carriers outside of the Lloyd's market. Competition varied depending on the type of business being insured or reinsured. Syndicate 4000 competed on an international and regional basis with major U.S., Bermuda, European and other international insurers and certain underwriting syndicates.

Regulation

The business of insurance and reinsurance is regulated in most countries, although the degree and type of regulation varies significantly from one jurisdiction to another. Reinsurers are generally subject to less direct regulation than primary insurers.

Our run-off activities are subject to regulation in Bermuda, Ireland and the United States.

Bermuda Regulation

As a holding company, Quanta Holdings is not subject to Bermuda insurance regulations.

Quanta Re and Quanta U.S. Re are registered as Class 4 and Class 3 insurers under the Insurance Act by the Bermuda Monetary Authority, or the BMA, which is responsible for the day-to-day supervision of insurers. Under the Insurance Act, insurance business includes reinsurance business. Since the businesses of Quanta Re and Quanta U.S. Re are in run-off, the BMA has amended the licenses of these entities to require that they seek the approval from the BMA prior to paying any dividend to Quanta Holdings and to prohibit them from engaging in any new transactions.

The Insurance Act imposes on Bermuda insurance companies, including those in run-off, solvency and liquidity standards and auditing and reporting requirements and grants to the BMA powers to

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supervise, investigate and intervene in the affairs of insurance companies. Certain significant aspects of the Bermuda insurance regulatory framework are set forth below.

Cancellation of Insurer's Registration

An insurer's registration may be canceled by the BMA on certain grounds specified in the Insurance Act, including failure of the insurer to comply with its obligations under the Insurance Act or if, in the opinion of the BMA, the insurer has not been carrying on business in accordance with sound insurance principles.

Statutory Financial Statements

An insurer must prepare annual statutory financial statements. The Insurance Act prescribes rules for the preparation and substance of such statutory financial statements (which include, in statutory form, a balance sheet, an income statement, a statement of capital and surplus and notes thereto). The insurer is required to give detailed information and analyses regarding premiums, claims, reinsurance and investments. The statutory financial statements are not prepared in accordance with U.S. GAAP and are distinct from the financial statements prepared for presentation to the insurer's shareholders under the Companies Act, which financial statements will be prepared in accordance with U.S. GAAP. Each of Quanta Re and Quanta U.S. Re, as a general business insurer, is required to submit the annual statutory financial statements as part of the annual statutory financial return. The statutory financial statements and the statutory financial return do not form part of the public records maintained by the BMA.

The BMA has announced that it is proposing that Class 4 insurers file, with their annual statutory return, audited GAAP financial statements, which will be published subject to certain conditions.

Annual Statutory Financial Return

Quanta Re and Quanta U.S. Re are required to file with the BMA statutory financial returns no later than four months after their financial year end (unless specifically extended). The statutory financial return for an insurer includes, among other matters, a report of the approved auditor on the statutory financial statements of such insurer, the solvency certificates, the declaration of statutory ratios, the statutory financial statements, the opinion of the loss reserve specialist and a schedule of reinsurance ceded. The solvency certificates must be signed by the principal representative and at least two directors of the insurer who are required to certify, among other matters, whether the minimum solvency margin has been met and whether the insurer complied with the conditions attached to its certificate of registration. The approved auditor is required to state whether in his opinion it was reasonable for the directors to so certify. Where an insurer's accounts have been audited for any purpose other than compliance with the Insurance Act, a statement to that effect must be filed with the statutory financial return.

The BMA has announced that it proposes to expand the statutory financial return to include additional forward-looking risk management information, such as pro forma financial statements and prescribed stress and scenario testing.

Minimum Solvency Margin and Restrictions on Dividends and Distributions

Under the Insurance Act, the value of the general business assets of a Class 4 insurer, such as Quanta Re must exceed the amount of its general business liabilities by an amount greater than the prescribed minimum solvency margin. Quanta Re is required, with respect to its general business, to maintain a minimum solvency margin equal to the greatest of:

\$100,000,000;

(A)

(B) 50% of net premiums written (being gross premiums written less any premiums ceded by Quanta Re, but Quanta Re may not deduct more than 25% of gross premiums when computing net premiums written); and

(C) 15% of loss and other insurance reserves.

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Quanta Re is prohibited from declaring or paying any dividends during any financial year if it is in breach of its minimum solvency margin or minimum liquidity ratio or if the declaration or payment of such dividends would cause it to fail to meet such margin or ratio. In addition, if it has failed to meet its minimum solvency margin or minimum liquidity ratio on the last day of any financial year, Quanta Re will be prohibited, without the approval of the BMA, from declaring or paying any dividends during the next financial year. Quanta Re is also prohibited from declaring or paying in any financial year dividends of more than 25% of its total statutory capital and surplus (as shown on its previous financial year's statutory balance sheet) unless it files with the BMA at least seven days before payment of such dividends an affidavit stating that it will continue to meet the required margins.

Quanta Re is prohibited, without the approval of the BMA, from reducing by 15% or more its total statutory capital as set out in its previous year's financial statements, and any application for such approval must include an affidavit stating that it will continue to meet the required margins. In addition, at any time it fails to meet its solvency margin, Quanta Re will be required, within 30 days (45 days where total statutory capital and surplus falls to \$75 million or less) after becoming aware of such failure or having reason to believe that such failure has occurred, to file with the BMA a written report containing certain information.

Under the Insurance Act, the value of the general business assets of a Class 3 insurer, such as Quanta U.S. Re must exceed the amount of its general business liabilities by an amount greater than the prescribed minimum solvency margin. Quanta U.S. Re is required, with respect to its general business, to maintain a minimum solvency margin equal to the greatest of:

		(A)
\$1,000,000	(B) Net Premium Income ("NPI")	Up to \$6,000,000
	Greater than \$6,000,000	20% of NPI
	The aggregate of \$1,200,000 and 15% of the amount by which NPI exceeds \$6,000,000 in that year.	

In general, net premium income equals gross premium income after deduction of any premium ceded by the insurer for reinsurance; or

	(C) 15%
of the aggregate of the insurer's loss expense provisions and other general business insurance reserves.	

Quanta U.S. Re is prohibited from declaring or paying any dividends during any financial year if it is in breach of its minimum solvency margin or minimum liquidity ratio or if the declaration or payment of such dividends would cause it to fail to meet such margin or ratio. In addition, if it has failed to meet its minimum solvency margin or minimum liquidity ratio on the last day of any financial year, Quanta U.S. Re will be prohibited, without the approval of the BMA, from declaring or paying any dividends during the next financial year. Quanta U.S. Re is prohibited, without the approval of the BMA, from reducing by 15% or more its total statutory capital as set out in its previous year's financial statements, and any application for such approval shall provide such information as the BMA may require. In addition, at any time it fails to meet its solvency margin, Quanta U.S. Re will be required, within 30 days after becoming aware of such failure or having reason to believe that such failure has occurred, to file with the BMA a written report containing certain information.

Additionally, under the Companies Act, neither Quanta Holdings nor Quanta Re nor Quanta U.S. Re may declare or pay a dividend, or make a distribution from contributed surplus, if there are reasonable grounds for believing that it is, or would after the payment be, unable to pay its liabilities as they become due, or the realizable value of its assets

would be less than the aggregate of its liabilities and its issued share capital and share premium accounts.

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Bermuda Solvency Capital Requirement

As part of the BMA's ongoing review of Bermuda's insurance supervisory framework, the BMA is introducing a new risk-based capital model (the "Bermuda Solvency Requirement" or "BSCR") as a tool to assist both in measuring risk and determining appropriate capitalization. It is expected that formal legislation will come into force in 2008 to apply these standards. In addition, the BMA intends to allow insurers to make application to the BMA to use their own internal capital models instead of the BSCR in cases where insurers can establish that their respective internal capital models better reflect their company characteristics. The BMA intends to consult further with insurers on these proposals prior to their formal implementation.

Minimum Liquidity Ratio

The Insurance Act provides a minimum liquidity ratio for general business insurers. An insurer engaged in general business is required to maintain the value of its relevant assets at not less than 75% of the amount of its relevant liabilities. Relevant assets include cash and time deposits, quoted investments, unquoted bonds and debentures, first liens on real estate, investment income due and accrued, accounts and premiums receivable and reinsurance balances receivable. There are certain categories of assets which, unless specifically permitted by the BMA, do not automatically qualify as relevant assets, such as unquoted equity securities, investments in and advances to affiliates and real estate and collateral loans. The relevant liabilities are total general business insurance reserves and total other liabilities less deferred income tax and sundry liabilities (by interpretation, those not specifically defined).

Supervision, Investigation and Intervention

The BMA may appoint an inspector with extensive powers to investigate the affairs of an insurer if the BMA believes that an investigation is required in the interest of the insurer's policyholders or persons who may become policyholders. In order to verify or supplement information otherwise provided to the BMA, the BMA may direct an insurer to produce documents or information relating to matters connected with the insurer's business.

If it appears to the BMA that there is a risk of the insurer becoming insolvent, or that it is in breach of the Insurance Act or any conditions imposed upon its registration, the BMA may, among other things, direct the insurer (1) not to take on any new insurance business, (2) not to vary any insurance contract if the effect would be to increase the insurer's liabilities, (3) not to make certain investments, (4) to realize certain investments, (5) to maintain in, or transfer to the custody of, a specified bank, certain assets, (6) not to declare or pay any dividends or other distributions or to restrict the making of such payments and/or (7) to limit its premium income.

Disclosure of Information

In addition to powers under the Insurance Act to investigate the affairs of an insurer, the BMA may require certain information from an insurer (or certain other persons) to be produced to it. Further, the BMA has been given powers to assist other regulatory authorities, including foreign insurance regulatory authorities, with their investigations involving insurance and reinsurance companies in Bermuda but subject to restrictions. For example, the BMA must be satisfied that the assistance being requested is in connection with the discharge of regulatory responsibilities of the foreign regulatory authority. Further, the BMA must consider whether cooperation is in the public interest. The grounds for disclosure are limited and the Insurance Act provides sanctions for breach of the statutory duty of confidentiality.

Notification by shareholder of new or increased control

Any person who, directly or indirectly, becomes a holder of at least 10% , 20%, 33% or 50% of the common shares of Quanta Holdings must notify the BMA in writing within 45 days of becoming such a holder or 30 days from the date they have knowledge of having such a holding, whichever is

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later. The BMA may, by written notice, object to such a person if it appears to the BMA that the person is not fit and proper to be such a holder. The BMA may require the holder to reduce their holding of shares and direct, among other things, that voting rights attaching to those shares shall not be exercisable.

Objection to existing shareholder

For so long as Quanta Holdings has as a subsidiary an insurer registered under the Insurance Act, the BMA may at any time, by written notice, object to a person holding 10% or more of Quanta Holdings' common shares if it appears to the BMA that the person is not or is no longer fit and proper to be such a holder. In such a case, the BMA may require the shareholder to reduce its holding of shares and direct, among other things, that such shareholder's voting rights attaching to those shares shall not be exercisable.

Certain other Considerations

Although Quanta Holdings is incorporated in Bermuda, it is classified as a non-resident of Bermuda for exchange control purposes by the BMA. Pursuant to its non-resident status, Quanta Holdings may engage in transactions in currencies other than Bermuda dollars and there are no restrictions on its ability to transfer funds (other than funds denominated in Bermuda dollars) in and out of Bermuda or to pay dividends to U.S. residents who are holders of its common shares.

Under Bermuda law, exempted companies are companies formed for the purpose of conducting business outside Bermuda from a principal place of business in Bermuda. As "exempted" companies, Quanta Holdings, Quanta Re and Quanta U.S. Re may not, without the express authorization of the Bermuda legislature or under a license or consent granted by the Minister of Finance, participate in certain business transactions, including: (1) the acquisition or holding of land in Bermuda (except that held by way of lease or tenancy agreement which is required for its business and held for a term not exceeding 50 years, or which is used to provide accommodation or recreational facilities for its officers and employees and held with the consent of the Bermuda Minister of Finance, for a term not exceeding 21 years); (2) the taking of mortgages on land in Bermuda to secure an amount in excess of \$50,000; or (3) the carrying on of business of any kind for which it is not licensed in Bermuda, except in certain limited circumstances such as doing business with another exempted undertaking in furtherance of Quanta Holdings' business, Quanta Re's business or Quanta U.S. Re's business (as the case may be) carried on outside Bermuda. Quanta Re and Quanta U.S. Re both are licensed insurers in Bermuda, and it is expected that they will be able to carry on activities from Bermuda that are related to and in support of their insurance business in accordance with their licenses.

Shares may be offered or sold in Bermuda only in compliance with the provisions of the Investment Business Act of 2003 of Bermuda, which regulates the sale of securities in Bermuda. In addition the BMA must approve all issuances and transfers of shares of a Bermuda exempted company.

The Bermuda government actively encourages foreign investment in "exempted" entities like Quanta Holdings that are based in Bermuda, but which do not operate in competition with local businesses. Quanta Holdings, Quanta Re and Quanta U.S. Re are not currently subject to taxes computed on profits or income or computed on any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax or to any foreign exchange controls in Bermuda; however, Quanta U.S. Re will be taxed as a U.S. corporation.

Under Bermuda law, non-Bermudians (other than spouses of Bermudians) may not engage in any gainful occupation in Bermuda without the specific permission of the appropriate governmental authority. Such permission may be granted or extended upon showing that, after proper public advertisement, no Bermudian, or spouse of a Bermudian or

individual holding a permanent resident certificate is available who meets the minimum standards for the advertised position. We employ primarily non-Bermudians. None of the executive officers of Quanta Holdings is a Bermudian, and all of these officers work in Bermuda under work permits. The Bermuda government recently announced a new policy that places a six-year term limit on individuals with work permits, subject to certain exceptions for key employees.

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Irish Regulation

Quanta Europe is incorporated under the laws of Ireland, has a registered office in Ireland and is in the process of running off its business. In March 2007, it submitted a withdrawal plan to the Irish Financial Services Regulatory Authority (which has recently re-branded itself as the Financial Regulator), or FR. During the second quarter of 2007, Quanta Europe returned \$12.2 million which was the majority of its capital to Quanta Holdings, its parent, and it continues to execute on the withdrawal plan so that it may return the remaining portion of its capital to its parent in the future. As a non-life insurance company, Quanta Europe is subject to the regulation and supervision of FR pursuant to the Insurance Acts and Regulations and is authorized to undertake various classes of non-life insurance business.

Quanta Europe is primarily regulated under the Insurance Acts and Regulations. In addition, Quanta Europe is subject to supervisory requirements imposed by FR. These include the guidelines referred to in this section.

In addition to the obligations imposed on Quanta Europe by the Insurance Acts and Regulations, FR has granted the authorization subject to certain conditions as is typical for Irish authorized insurers. The following are the main conditions that have been imposed:

Europe will not be permitted to reduce the level of its initial capital without the consent of FR;
not make any dividend payments without FR's prior approval;
made by Quanta Europe without prior notification to and approval of FR;
must maintain a minimum solvency margin equal to 200% of the solvency margin laid down by the Insurance Acts and Regulations (and a solvency ratio (of free assets to net premium) of 50%); and
required to maintain a minimum guarantee fund (minimum capital) irrespective of capital requirements under solvency calculations of 3.0 million Euro.

- Quanta
- Quanta Europe may
- no loans may be
- Quanta Europe
- Quanta Europe is

Annual Returns

Quanta Europe must file annual statutory insurance returns with FR in the format prescribed by the European Communities (Non-Life Insurance Accounts) Regulations, 1995. Insurers must also pay annual supervision fees.

Qualifying Shareholding

The Insurance Acts and Regulations require that anyone acquiring or disposing of a "qualifying holding" in an Irish authorized insurer or anyone who proposes to increase that holding or to decrease it below specified levels must first notify FR of their intention to do so. Any Irish-authorized insurer that becomes aware of any acquisition or disposal of a qualifying holding in that insurer or which result in a holding reaching or being reduced below one of the "specified levels" is required to notify FR.

FR has three months from the date of submission of a notification within which to oppose any such proposed acquisition if FR is not satisfied as to the suitability of the acquiror "in view of the necessity to ensure sound and prudent management of the insurance undertaking."

A “qualifying holding” means a direct or indirect holding in an insurer that represents 10% or more of the capital or of the voting rights of the insurer or that makes it possible to exercise a significant influence over the management of the insurer. The specified levels are 20%, 33% and 50%, or such other level of ownership that results in the insurer becoming the acquiror’s subsidiary.

Any person having a shareholding of 10% or more of our issued share capital would be considered to have an indirect qualifying holding in Quanta Europe, whether or not those shares confer 10% or more of our voting rights. FR will need to pre-clear any change that results in the

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direct or indirect acquisition of a qualifying holding in Quanta Europe or a change that results in an increase in a holding to one of the specified levels.

Quanta Europe is required, at such times as may be specified by FR, and at least once a year, to notify FR of the names of shareholders possessing qualifying holdings and the size of such holdings.

Transactions with Related Companies

Under the Insurance Acts and Regulations, prior to entering into any transaction of a material nature with a related company or companies (including, in particular, the provision of loans to and acceptance of loans from a related company or companies) Quanta Europe must submit to FR a draft of any contract or agreement which is to be entered into by Quanta Europe in relation to the transaction. In addition to the above, there is a requirement that Quanta Europe notify FR on an annual basis of transactions with related companies in excess of 10,000 Euro.

Financial Requirements

Quanta Europe is required to maintain technical reserves calculated in accordance with the Insurance Acts and Regulations. Assets representing its technical reserves are required to cover Quanta Europe's underwriting liabilities.

Quanta Europe is obligated to prepare annual accounts (comprising balance sheet, profit and loss account and notes) in accordance with the provisions of the European Communities (Insurance Undertakings: Accounts) Regulations, 1996 (the 'Insurance Accounts Regulations'). Such accounts must be filed with FR and with the Registrar of Companies in Ireland.

Additionally, Quanta Europe is required to establish and maintain an adequate solvency margin and a minimum guarantee fund, both of which must be free from all foreseeable liabilities and not available for other purposes such as use as reserves.

The minimum guarantee fund is equal to one third of the solvency margin requirement as set out above, subject to a minimum. It is not an additional fund and is included in the solvency margin. Where an insurer is part of an insurance group, the solvency margin must be recalculated to eliminate any double counting of capital within the group.

Investment Restrictions

The Insurance Acts and Regulations limit the categories of assets that may be used to represent technical reserves and the required solvency margin. They also impose asset diversification, localization and currency matching rules and limit the use of derivatives in relation to assets used to represent technical reserves.

The localization rules require that assets representing technical reserves in respect of EU risks be localized in the EU. The documents of title must be held in the EU and the assets themselves must comply with the tests for localization set out in the Insurance Acts and Regulations. The currency matching rules require that a proportion of the assets representing risks arising in any currency must be held in assets denominated or readily realizable in that currency.

Withdrawal of Authorization

An insurer supervised by FR may have its authorization revoked by FR, if FR is satisfied that the insurer:

used its authorization for the last 12 months, has expressly renounced its authorization or has ceased to carry on business covered by the authorization for more than six months;

of certain offences under the Insurance Acts and Regulations;

conditions for authorization required by the Insurance Acts and Regulations;

- has not
- has been convicted
- no longer fulfils the

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take measures contained in a restoration plan or finance scheme envisaged by the Insurance Acts and Regulations;

- has been unable to
- fails

seriously in its obligations under the Insurance Acts and Regulations;

- fails to comply with

a requirement to produce certain documentation pursuant to an investigation; or

- fails to comply with

a direction from FR as provided for in the Insurance Acts and Regulations.

FR may also suspend an authorization in certain circumstances. If FR revokes the authorization of an insurer, the right of that insurer to continue its activities in another European Economic Area member state, whether by way of freedom of services or through a right of establishment of a branch, will immediately cease.

Approval of Directors and Managers

In addition to the restrictions set forth above, FR must approve the appointment of any new directors or managers of Quanta Europe.

Supervision, Investigation and Intervention

The Insurance Acts and Regulations confer on FR wide-ranging powers in relation to the supervision and investigation of insurers, including the following:

- FR has power to require an insurer to submit returns and documents to it in such form as may be prescribed by regulation and to require that they be attested by directors and officers of the insurer. FR may also require that such returns and documents be attested by independent professionals and be published. Additionally, FR has a right to disclose any such returns or documents to the supervisory authorities of other EU Member States;
- FR may require information in relation to the insurer or any connected body;
- FR has power to direct that an investigation of an insurer's affairs be carried out in order to be satisfied that the insurer is complying or has the ability to comply with its obligations under the Insurance Acts and Regulations. If necessary FR may seek a High Court order prohibiting the free disposal of an insurer's assets;
- In certain circumstances, including where FR believes that an insurer may be unable to meet its liabilities or provide the required solvency margin, FR may direct the insurer to take measures including: closing to new business, limiting its premium income, restricting its investments in certain assets, realizing assets, maintaining assets in Ireland and any further measures specified in the direction;
- If FR considers that policyholders' rights are threatened, it can require the insurer concerned to produce a financial recovery plan, covering the next three years and to maintain a higher solvency margin; FR is prohibited from issuing a certificate that the insurer meets the required solvency margin while it believes that policyholders' rights are threatened;
- If the solvency margin of the insurer falls below the minimum guarantee fund, FR must require the insurer to submit a short-term finance scheme; and
- FR may confer wide ranging powers on "authorized officers" in relation to insurers for the purpose of the Insurance Acts and Regulations.

These powers include permitting an authorized officer to search a premises and remove documents. An authorized officer may also be empowered to compel persons to provide information and documentation and to prepare a report on specified aspects of the business or activities of an insurer and other prescribed persons.

Auditors to an insurer have a statutory duty to report to FR in certain circumstances.

Certain breaches of the Insurance Acts and Regulations may constitute criminal offences and render the persons found guilty of such offences liable to fines and/or imprisonment.

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Certain other Irish Law Considerations

Quanta Europe is subject to the laws and regulations of Ireland. The Irish Companies Acts, 1963 to 2005 (the “Companies Acts”) and the common law include the following restrictions applicable to Quanta Europe:

- Irish law requires the directors of a company to act in good faith for the benefit of the company and for example, prohibits the gratuitous use of corporate assets for the benefit of directors and persons connected with them;
- Irish company law applies capital maintenance rules. In particular, Quanta Europe is restricted to declaring dividends only out of “profits available for distribution.” Profits available for distribution are a company’s accumulated realized profits less its accumulated realized losses. Such profits may not include profits previously utilized either by distribution or capitalization and such losses do not include amounts previously written-off in a reduction or reorganization of capital;
- Irish law restricts a company from entering into certain types of transactions with its directors and officers by either completely prohibiting such transactions or permitting them only subject to conditions;
- Irish law restricts the giving of financial assistance by a company in connection with the purchase of its own shares or those of its holding company;
- All Irish companies are obliged to file prescribed returns (including, in most cases, audited accounts) in the Companies Registration Office annually and on the happening of certain events such as the creation of new shares, a change in directors or the passing of certain shareholder resolutions;
- A private limited company cannot offer shares or debentures to the public. Quanta Europe is a private limited company;
- A statutory body known as the Office of the Director of Corporate Enforcement (the “ODCE”) has power to carry out investigations into the affairs of Irish companies in circumstances prescribed in the Companies Acts. The powers of the ODCE include the prosecution (both civil and criminal) of persons for suspected breaches of the Companies Acts; and
- Certain civil and criminal sanctions exist for breaches of the Companies Acts.

Quanta Europe is also required to comply with laws such as Irish Data Protection law.

U.S. Regulation

Quanta Indemnity and Quanta Specialty Lines are regulated insurance companies in Colorado and Indiana respectively.

Holding Company Acts

State insurance holding company system statutes and related regulations provide a regulatory apparatus that is designed to protect the financial condition of domestic insurers operating within a holding company system. All insurance holding company statutes require disclosure and, in some instances, prior approval of material transactions between the domestic insurer and an affiliate. These transactions typically include sales, purchases, exchanges, loans and extensions of credit, reinsurance agreements, service agreements, guarantees and investments between an insurance company and its affiliates, involving in the aggregate specified percentages of an insurance company’s

admitted assets or policyholders surplus, or dividends that exceed specified percentages of an insurance company's surplus or income.

The state insurance holding company system statutes may discourage potential acquisition proposals and may delay, deter or prevent a change of control of Quanta Holdings, Quanta

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U.S. Holdings, Quanta Indemnity or Quanta Specialty Lines including through transactions, and in particular unsolicited transactions, that we or our shareholders might consider to be desirable.

Before a person can acquire control of a domestic insurer or reinsurer, prior written approval must be obtained from the insurance commissioner of the state where the domestic insurer is domiciled. Prior to granting approval of an application to acquire control of a domestic insurer, the state insurance commissioner where the insurer is domiciled will consider such factors as the financial strength of the applicant, the integrity and management of the applicant's board of directors and executive officers, the acquiror's plans for the future operations of the domestic insurer and any anti-competitive results that may arise from the closing of the acquisition of control. Generally, state statutes provide that "control" over a domestic insurer is presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent or more of the voting securities of the domestic insurer. Because a person acquiring ten percent or more of the common shares of Quanta Holdings would indirectly acquire the same percentage of Quanta Specialty Lines' and Quanta Indemnity's common stock, the U.S. insurance change of control laws will likely apply to such a transaction.

Typically, the holding company statutes will also require each of our U.S. subsidiaries periodically to file information with state insurance regulatory authorities, including information concerning capital structure, ownership, financial condition and general business operations.

Regulation of Dividends and other Payments from Insurance Subsidiaries

The ability of a U.S. insurer to pay dividends or make other distributions is subject to insurance regulatory limitations of the insurance company's state of domicile. Generally, these laws require prior regulatory approval before an insurer may pay a dividend or make a distribution above a specified level. In many U.S. jurisdictions, including the State of Indiana where Quanta Specialty Lines is domiciled and the State of Colorado where Quanta Indemnity is domiciled, dividends may only be paid out of earned surplus and may not exceed the greater of (1) 10% of the insurer's statutory surplus as of the end of the last preceding calendar year or (2) levels of the insurer's net income for the prior calendar year. In addition, the laws of many U.S. jurisdictions require an insurer to report for informational purposes to the insurance commissioner of its state of domicile all declarations and proposed payments of dividends and other distributions to security holders. Any return of capital from a U.S. insurance company would require prior approval of the domestic regulators.

The dividend limitations imposed by the state laws are based on statutory financial results, determined by using statutory accounting practices which differ in certain respects from accounting principles used in financial statements prepared in conformity with U.S. GAAP. The significant differences relate to treatment of deferred acquisition costs, deferred income taxes, required investment reserves, reserve calculation assumptions and surplus notes. In connection with the acquisition of a U.S. insurer, insurance regulators in the United States often impose, as a condition to the approval of the acquisition, additional restrictions on the ability of the U.S. insurer to pay dividends or make other distributions. These restrictions generally prohibit the U.S. insurer from paying dividends or making other distributions for a number of years without prior enhanced regulatory approval.

Insurance Regulatory Information System Ratios

The NAIC Insurance Regulatory Information System ("IRIS") was developed by a committee of state insurance regulators and is intended primarily to assist state insurance departments in executing their statutory mandates to oversee the financial condition of insurance companies operating in their respective states. IRIS identifies 11 industry ratios and specifies "usual values" for each ratio. Departure from the usual values of the ratios can lead to inquiries from

individual state insurance commissioners regarding different aspects of an insurer's business. Insurers that report four or more unusual values are generally targeted for regulatory review.

Accreditation

The NAIC has instituted its Financial Regulatory Accreditation Standards Program ('FRASP') in response to federal initiatives to regulate the business of insurance. FRASP provides a set of

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standards designed to establish effective state regulation of the financial condition of insurance companies. Under FRASP, a state must adopt certain laws and regulations, institute required regulatory practices and procedures, and have adequate personnel to enforce these laws and regulations in order to become an “accredited” state. Accredited states are not able to accept certain financial examination reports of insurers prepared solely by the regulatory agency in an unaccredited state.

Risk-Based Capital Requirements

In order to enhance the regulation of insurer solvency, the NAIC adopted in December 1993 a formula and model law to implement risk-based capital requirements for property and casualty insurance companies. These risk-based capital requirements change from time to time and are designed to assess capital adequacy and to raise the level of protection that statutory surplus provides for policyholder obligations. The risk-based capital model for property and casualty insurance companies measures three major areas of risk facing property and casualty insurers:

- underwriting, which encompasses the risk of adverse loss developments and inadequate pricing;
- declines in asset values arising from credit risk; and
- declines in asset values arising from investment risks.

Insurers having less statutory surplus than required by the risk-based capital calculation will be subject to varying degrees of regulatory action, depending on the level of capital inadequacy. Equity investments in common stock typically are valued at 85% of their market value under the risk-based capital guidelines.

Under the approved formula, an insurer’s statutory surplus is compared to its risk-based capital requirement. If this ratio is above a minimum threshold, no company or regulatory action is necessary. Below this threshold are four distinct action levels at which a regulator can intervene with increasing degrees of authority over an insurer as the ratio of surplus to risk-based capital requirement decreases. The four action levels include:

- insurer is required to submit a plan for corrective action,
- insurer is subject to examination, analysis and specific corrective action,
- regulators may place insurer under regulatory control, and
- regulators are required to place insurer under regulatory control.

Guaranty Funds and Assigned Risk Plans

Most states require all admitted insurance companies to participate in their respective guaranty funds that cover various claims against insolvent insurers. Solvent insurers licensed in these states are required to cover the losses paid on behalf of insolvent insurers by the guaranty funds and are generally subject to annual assessments in the state by its guaranty fund to cover these losses. Some states also require licensed insurance companies to participate in assigned risk plans which provide coverage for automobile insurance and other lines for insureds which, for various reasons, cannot otherwise obtain insurance in the open market. This participation may take the form of reinsuring a portion of a

pool of policies or the direct issuance of policies to insureds. The calculation of an insurer's participation in these plans is usually based on the amount of premium for that type of coverage that was written by the insurer on a voluntary basis in a prior year. Participation in assigned risk pools tends to produce losses which result in assessments to insurers writing the same lines on a voluntary basis.

Credit for Reinsurance

Licensed reinsurers in the United States are subject to insurance regulation and supervision that is similar to the regulation of licensed primary insurers. However, the terms and conditions of

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reinsurance agreements generally are not subject to regulation by any governmental authority with respect to rates or policy terms. This contrasts with primary insurance policies and agreements, the rates and terms of which generally are regulated by state insurance regulators. As a practical matter, however, the rates charged by primary insurers do have an effect on the rates that can be charged by reinsurers.

A primary insurer ordinarily will enter into a reinsurance agreement only if it can obtain credit for the reinsurance ceded on its statutory financial statements. In general, credit for reinsurance is allowed in the following circumstances:

- if the reinsurer is licensed in the state in which the primary insurer is domiciled or, in some instances, in certain states in which the primary insurer is licensed;
- if the reinsurer is an “accredited” or otherwise approved reinsurer in the state in which the primary insurer is domiciled or, in some instances, in certain states in which the primary insurer is licensed;
- in some instances, if the reinsurer (a) is domiciled in a state that is deemed to have substantially similar credit for reinsurance standards as the state in which the primary insurer is domiciled and (b) meets financial requirements; or
- if none of the above apply, to the extent that the reinsurance obligations of the reinsurer are secured appropriately, typically through the posting of a letter of credit for the benefit of the primary insurer or the deposit of assets into a trust fund established for the benefit of the primary insurer.

As a result of the requirements relating to the provision of credit for reinsurance, Quanta Re, Quanta U.S. Re and Quanta Europe are indirectly subject to some regulatory requirements imposed by jurisdictions in which ceding companies are licensed. Because Quanta Re, Quanta U.S. Re and Quanta Europe were not licensed, accredited or otherwise approved by or domiciled in any state in the United States, primary insurers were only willing to cede business to Quanta Re, Quanta U.S. Re and Quanta Europe if we provided adequate security to allow the primary insurer to take credit on its balance sheet for the reinsurance it purchased. We typically provided this security through the posting of a letter of credit or deposit of assets into a trust fund for the benefit of the primary insurer.

Statutory Accounting Principles

Statutory accounting principles, or SAP, is a basis of accounting developed to assist insurance regulators in monitoring and regulating the solvency of insurance companies. It is primarily concerned with measuring an insurer’s surplus to policyholders. Accordingly, statutory accounting focuses on valuing assets and liabilities of insurers at financial reporting dates in accordance with appropriate insurance law and regulatory provisions applicable in each insurer’s domiciliary state.

U.S. GAAP is concerned with a company’s solvency, but it is also concerned with other financial measurements, such as income and cash flows. Accordingly, U.S. GAAP gives more consideration to appropriate matching of revenue and expenses and accounting for management’s stewardship of assets than does SAP. As a direct result, different assets and liabilities and different amounts of assets and liabilities will be reflected in financial statements prepared in accordance with U.S. GAAP as opposed to SAP.

Statutory accounting practices established by the NAIC and adopted, in part, by State Insurance Departments, will determine, among other things, the amount of statutory surplus and statutory net income of our U.S. insurance subsidiaries, which will affect, in part, the amount of funds they have available to pay dividends to us.

Federal Regulation

We are subject to numerous federal regulations, including the Securities Act of 1933, the Securities Exchange Act of 1934 (the ‘Exchange Act’) and other federal securities laws. As we

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continue with the run-off of our business, we must monitor our compliance with these laws, including our maintenance of any available exemptions from registration as an investment company under the Investment Company Act of 1940. Any failure to comply with these laws or maintain our exemption could have a material adverse effect on our operations and on the market price of our common shares. Although state regulation is the dominant form of U.S. regulation for insurance and reinsurance business, from time to time Congress has shown concern over the adequacy and efficiency of the state regulation.

Material Tax Considerations

The following is a summary of our taxation under certain tax laws, does not purport to be a comprehensive discussion of all the tax considerations that may be relevant and is for general information only. The discussion is based upon current law. Legislative, judicial or administrative changes or interpretations may be forthcoming that could be retroactive and could affect the tax consequences discussed herein. Statements contained in this report as to the beliefs, expectations and conditions of Quanta Holdings and its subsidiaries as to the application of such tax laws or facts represent the view of management as to the application of such laws and do not represent the opinions of counsel.

You should consult your own tax advisor concerning the U.S. federal, state, local and non-U.S. tax consequences of owning our securities.

Taxation of Quanta Holdings and Subsidiaries

Certain Bermuda Tax Considerations

Bermuda does not currently impose any income, corporation or profits tax, withholding tax, capital gains tax, capital transfer tax, estate duty or inheritance tax on us or our shareholders, other than shareholders ordinarily resident in Bermuda, if any. There is currently no Bermuda withholding or other tax on principal, interest or dividends paid to holders of the shares, other than holders ordinarily resident in Bermuda, if any. We cannot assure you that we or our shareholders will not be subject to any such tax in the future.

Quanta Holdings has received written assurance dated May 27, 2003 from the Bermuda Minister of Finance under the Exempted Undertakings Tax Protection Act 1966 of Bermuda, as amended, that if any legislation is enacted in Bermuda imposing tax computed on profits or income, or computed on any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax, then the imposition of that tax would not be applicable to Quanta Holdings or to any of its operations, shares, debentures or obligations until March 28, 2016; provided, that the assurance is subject to the condition that it will not be construed to prevent the application of such tax to people ordinarily resident in Bermuda, or to prevent the application of any taxes payable by Quanta Holdings in respect of real property or leasehold interests in Bermuda held by it. Quanta Re and Quanta U.S. Re also received such written assurance dated June 23, 2003.

Certain Irish Tax Considerations

We intend that Quanta Europe, a company incorporated in Ireland, will be managed and controlled in Ireland and, therefore, will be resident in Ireland for Irish tax purposes and subject to Irish corporation tax on its worldwide profits (including revenue profits and capital gains). Income derived by Quanta Europe, once authorized, from an Irish trade (that is, a trade that is not carried on wholly outside of Ireland) will be subject to Irish corporation tax at the current rate of 12.5%. Other income (that is income from passive investments, income from non-Irish trades and income from

certain dealings in land) will generally be subject to Irish corporation tax at the current rate of 25%.

The Irish Revenue Commissioners have published a statement indicating that deposit interest earned by an insurance company on funds held for regulatory purposes will be regarded as part of its

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trading income, and accordingly will be part of the profits taxed at 12.5%. This statement also indicates acceptance of case law which states that investment income of an insurance company will likewise be considered as trading income where it is integral to the insurance trade and available for satisfying the liabilities of the insurance business.

Other investment income earned by Quanta Europe will generally be taxed in Ireland at a rate of 25%. Capital gains realized by Quanta Europe will generally be subject to Irish corporation tax at an effective rate of 20%.

We expect that none of Quanta Holdings and its subsidiaries, other than Quanta Europe, will be resident in Ireland for Irish tax purposes unless the central management and control of such companies is, as a matter of fact, located in Ireland. A company not resident in Ireland for Irish tax purposes can be subject to Irish corporation tax if it carries on a trade through a branch or agency in Ireland or disposes of certain specified assets (e.g., Irish land, minerals, or mineral rights, or shares deriving the greater part of their value from such assets). In such cases, the charge to Irish corporation tax is limited to trading income connected with the branch or agency, and capital gains on the disposal of assets used in the branch or agency which are situated in Ireland at or before the time of disposal, and capital gains arising on the disposal of specified assets, with tax imposed at the rates discussed above. A company not resident in Ireland is otherwise subject to Irish income tax at the standard rate, currently 20%, on other taxable income arising from sources within Ireland, and to capital gains tax at the current rate of 20% of the taxable gain, on disposals of certain specified assets, Irish land, minerals, exploration and exploitation rights, and unquoted shares directly or indirectly deriving the greater part of their value from such assets.

Certain United Kingdom Tax Considerations

The following is a summary of certain U.K. tax considerations under current U.K. law relating to Quanta Holdings and its subsidiaries.

U.K. Taxation of Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines, Quanta Indemnity and Quanta 4000

U.K. Residence. None of Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines nor Quanta Indemnity are incorporated in the U.K. Accordingly, they should not be treated as being resident in the U.K. unless their central management and control is exercised in the U.K. The concept of central management and control is indicative of the highest level of control of a company, which is wholly a question of fact. We intend to manage Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines and Quanta Indemnity so they are not resident in the U.K. for U.K. corporation tax purposes. Quanta 4000 and Pembroke JV, as companies incorporated in the U.K., are treated as being resident in the U.K. and are subject to U.K. corporation tax on their respective worldwide income and gains. The maximum rate of U.K. corporation tax is currently 30%.

U.K. Permanent Establishment. As a matter of U.K. domestic tax law, a company not resident in the U.K. for U.K. corporation tax purposes can be subject to U.K. corporation tax if it carries on a trade in the U.K. through a permanent establishment in the U.K. but the charge to U.K. corporation tax is limited to all profits (including revenue profits and capital gains), wherever arising, that are attributable to such permanent establishment. The term “permanent establishment” is defined for these purposes in a manner that is consistent with various internationally recognized characteristics commonly used in the U.K.’s double tax treaties. The maximum rate of U.K. corporation tax is currently 30%.

We intend to operate in such a manner that none of Quanta Holdings nor any of its subsidiaries will carry on a trade in the U.K. through a permanent establishment in the U.K. Whether a trade is being carried on in the U.K. through a

permanent establishment in the U.K. is an inherently factual determination. Since U.K. case law and U.K. statutes fail to identify definitively activities that constitute a trade being carried on in the U.K. through a permanent establishment in the U.K., we

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cannot assure you that HM Revenue & Customs will not contend successfully that Quanta Holdings or any of its subsidiaries has been or will be carrying on a trade in the U.K. through a permanent establishment in the U.K. We believe that the U.S. subsidiaries of Quanta Holdings qualify for benefits under the tax treaty between the U.K. and the United States. If any of our U.S. subsidiaries qualifying for such benefits were to be carrying on a trade in the U.K. through a U.K. permanent establishment, they would only be subject to U.K. corporation tax if the U.K. permanent establishment constituted a permanent establishment for the purposes of that treaty and then only to the extent that any profits were attributable to that permanent establishment in the U.K. determined in accordance with the provisions of the U.K.—United States tax treaty.

The U.K. has no tax treaty with Bermuda and if any of Quanta Holdings or our subsidiaries in Bermuda were to be carrying on a trade in the U.K. through a permanent establishment in the U.K., they would be subject to U.K. corporation tax on all profits, wherever arising, attributable to that permanent establishment in accordance with the provisions of U.K. tax law.

There are circumstances in which companies that are neither resident in the U.K. nor entitled to the protection afforded by a tax treaty between the U.K. and the jurisdiction in which they are resident may be exposed to income tax in the U.K. on income arising in the U.K. (other than by deduction or withholding) but we intend to operate in such a manner that none of us will fall within the charge to income tax in the U.K. (other than by deduction or withholding) in this respect.

If we or any of our subsidiaries, other than any subsidiary incorporated in the U.K. as a contact office for Quanta Re, were treated as being resident in the U.K. for U.K. corporation tax purposes, or, were to be carrying on a trade in the U.K. through a permanent establishment in the U.K., the results of our operations and your investment could be materially adversely affected.

The U.K. imposes Insurance Premium Tax, or IPT, on the receipt of premiums by insurers under insurance contracts in respect of risks situated in the U.K. Certain types of insurance risks situated in the U.K. are exempt from IPT, including reinsurance. IPT is generally collected from the insurer, although the economic cost of the IPT is usually passed to the insured by way of an IPT-inclusive premium. The rate of IPT is 5% (or 17.5% for insurance contracts relating to certain goods in certain circumstances) and is calculated as a percentage of the premium received.

Certain U.S. Federal Income Tax Considerations

The following discussion is a summary of certain U.S. federal income tax considerations relating to Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines, Quanta Indemnity and Quanta U.S. Re and the ownership of our shares by investors. As discussed further in this annual report and based on our expected business, properties, ownership, organization, source of income and manner of operation, we believe that (1) no U.S. Person that owns shares in Quanta Holdings directly or indirectly through foreign entities should be subject to treatment as a 10% U.S. Shareholder of a controlled foreign corporation, or CFC, and (2) Quanta Holdings should not be considered a passive foreign investment company, for the year ended December 31, 2007. We have not sought and do not intend to seek an opinion of legal counsel as to whether or not we were a passive foreign investment company for the year ended December 31, 2007.

This summary is based upon the Internal Revenue Code, the Treasury Regulations promulgated under the Internal Revenue Code, rulings and other administrative pronouncements issued by the IRS, judicial decisions, the tax treaty between the United States and Bermuda, or the “Bermuda Treaty” and the tax treaty between the United States and Ireland, or the “Irish Treaty”, all as currently in effect, and all of which are subject to differing interpretations or to

change, possibly with retroactive effect. No assurance can be given that the IRS would not assert, or that a court would not sustain, a position contrary to any of the tax consequences described below. No advance ruling has been or will be sought from the IRS regarding any matter discussed in this annual report. This summary is for general information only, and does not purport to discuss all aspects of U.S. federal income taxation that may be important to a particular investor in light of such investor's investment or tax circumstances, or to investors subject to special tax rules, such as shareholders who own directly, or indirectly through certain foreign entities or through the constructive ownership rules of the

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Internal Revenue Code, 10% or more of the voting power or value of Quanta Holdings (or how those ownership rules may apply in certain circumstances), tax-exempt organizations, dealers in securities, banks, insurance companies, persons that hold shares that are a hedge or that are hedged against interest rate or insurance risks or that are part of a straddle or conversion transaction, or persons whose functional currency is not the U.S. dollar. This summary generally does not discuss the federal alternative minimum tax and federal taxes other than income tax or other U.S. taxes such as state or local income taxes. This summary assumes that an investor will acquire and hold our shares as capital assets, which generally means as property held for investment. Special rules, not discussed herein, apply to U.S. persons who are partners in a partnership investing in shares. Prospective investors should consult their tax advisors concerning the consequences, in their particular circumstances, of the ownership of shares under U.S. federal, state, local and other tax laws.

For U.S. federal income tax purposes and purposes of the following discussion, a ‘‘U.S. Person’’ means (1) a citizen or resident of the United States, (2) a corporation or other entity created or organized in the United States or under the laws of the United States or of any of its political subdivisions, (3) an estate the income of which is subject to U.S. federal income tax without regard to its source or (4) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. Persons have the authority to control all substantial decisions of the trust, as well as certain electing trusts.

U.S. Taxation of Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines, Quanta U.S. Re and Quanta Indemnity

U.S. Income and Branch Profits Tax. A foreign corporation deemed to be engaged in the conduct of a trade or business in the U.S. will generally be subject to U.S. federal income tax (at a current maximum rate of 35%), as well as a 30% branch profits tax in certain circumstances, on its income which is treated as effectively connected with the conduct of that trade or business unless the corporation is entitled to relief under an applicable income tax treaty, as discussed below. Quanta Holdings, Quanta Europe and Quanta Re intend to operate in such a manner that they will not be considered to be conducting a trade or business within the United States for purposes of U.S. federal income taxation. Whether a trade or business is being conducted in the United States is an inherently factual determination. Because the Internal Revenue Code, Treasury Regulations and court decisions fail to identify definitively activities that constitute being engaged in a trade or business in the United States, we cannot assure you that the IRS will not contend successfully that Quanta Holdings, Quanta Re and/or Quanta Europe are or will be engaged in a trade or business in the United States. Such income tax, if imposed, would be based on effectively connected income computed in a manner generally analogous to that applied to the income of a U.S. corporation, except that a foreign corporation is entitled to deductions and credits only if it timely files a U.S. federal income tax return (which requirement may be waived if the foreign corporation establishes that it acted reasonably and in good faith in its failure to timely file such return). Quanta Holdings, Quanta Europe and Quanta Re intend to file protective U.S. federal income tax returns on a timely basis in order to preserve the right to claim income tax deductions and credits if it is ever determined that they are subject to U.S. federal income tax.

An insurance enterprise resident in Bermuda generally will be entitled to the benefits of the Bermuda Treaty if (1) more than 50% of its shares are owned beneficially, directly or indirectly, by individual residents of the United States or Bermuda or U.S. citizens and (2) its income is not used in substantial part, directly or indirectly, to make disproportionate distributions to, or to meet certain liabilities of, persons who are neither residents of either the United States or Bermuda nor U.S. citizens. Quanta Re believes it is entitled to the benefits of the Bermuda Treaty. Assuming Quanta Re is entitled to the benefits under the Bermuda Treaty, it will not be subject to U.S. federal income tax on any insurance income found to be effectively connected with a U.S. trade or business unless that trade or business is conducted through a permanent establishment in the United States. Whether business is being conducted in the United

States through a permanent establishment is an inherently factual determination. Quanta Re intends to conduct its activities so as not to have a permanent establishment in the United States, although we cannot assure you that it will achieve this result.

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A company resident in Ireland will generally be entitled to the benefit of the Irish Treaty if (1) more than 50% of its shares are owned beneficially, directly or indirectly, by individual residents of the United States or Ireland or U.S. citizens and (2) deductible amounts paid for certain purposes to persons who are neither residents of either the U.S. or Ireland, nor U.S. citizens do not exceed 50% of the Irish company's income. An Irish company which does not meet those standards may nevertheless be entitled to the benefits of the Irish Treaty with respect to an item of income if the Irish company is engaged in the active conduct of a trade or business in Ireland, and the item of income is connected with or incidental to that trade or business. Quanta Europe believes it is entitled to the benefits of the Irish Treaty. Assuming Quanta Europe is entitled to the benefits of the Irish Treaty, it will not be subject to U.S. federal income tax on any income found to be effectively connected with a U.S. trade or business unless that trade or business is conducted through a permanent establishment in the United States. Quanta Europe intends to conduct its activities in a manner so that it does not have a permanent establishment in the United States, although we cannot assure you that it will achieve this result.

If a non-U.S. company is characterized as engaged in an insurance business in the United States, a portion of its net investment income will be characterized as effectively connected with such U.S. trade or business. The amount so characterized depends on a formula. It is unclear whether applicable income tax treaties apply to the characterization of net investment income and, if so, such benefit would only apply if the non-U.S. insurance company is eligible for such treaty benefit.

Foreign corporations also are subject to U.S. withholding tax at a rate of 30% of the gross amount of certain "fixed or determinable annual or periodical gains, profits and income" derived from sources within the United States (such as dividends and certain interest on investments), to the extent such amounts are not effectively connected with the foreign corporation's conduct of a trade or business in the United States. The tax rate is subject to reduction by applicable treaties. The Bermuda Treaty does not provide such a reduction. Dividends, if any, paid by Quanta U.S. Holdings to Quanta Holdings, therefore, will be subject to 30% U.S. withholding tax. The United States also imposes an excise tax on insurance and reinsurance premiums paid to foreign insurers or reinsurers with respect to risks located in the United States. The rate of tax applicable to premiums paid to Quanta Re is 4% for insurance premiums and 1% for reinsurance premiums. The excise tax does not apply to premiums paid to Quanta Europe assuming that Quanta Europe is entitled to the benefits of the Irish Treaty, to the extent that Quanta Europe does not reinsure the risk with a reinsurer which is not entitled to the benefits of a bilateral tax treaty with the United States in which the United States has waived the excise tax.

Quanta U.S. Holdings is a Delaware corporation, Quanta Indemnity is a Colorado corporation and Quanta Specialty Lines is an Indiana corporation. Quanta U.S. Re is a Bermuda corporation that will be taxed as a U.S. corporation pursuant to an election under section 953(d) of the Internal Revenue Code. Each will be subject to taxation in the United States on its worldwide income at regular corporate rates.

Personal Holding Companies. Quanta Holdings' U.S. subsidiaries could be subject to additional U.S. tax on a portion of their income earned from U.S. sources if any of them is considered to be a personal holding company, or "PHC" for U.S. federal income tax purposes. A corporation generally will be classified as a PHC for U.S. federal income tax purposes in a given taxable year if (1) at any time during the last half of such taxable year, five or fewer individuals (without regard to their citizenship or residency) own or are deemed to own (pursuant to certain constructive ownership rules) more than 50% of the stock of the corporation by value and (2) at least 60% of the corporation's adjusted ordinary gross income, as determined for U.S. federal income tax purposes, for such taxable year consists of "PHC income." PHC income includes, among other things, dividends, certain interest, certain royalties, annuities and, under certain circumstances, rents. For purposes of the 50% test, each partner of an investment partnership who is an individual will be treated as owning his/her proportionate share of any stock owned by the partnership. Additionally,

certain entities (such as tax-exempt organizations and pension funds) will be treated as individuals. The PHC rules contain an exception for foreign corporations.

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If any of Quanta Holdings' U.S. subsidiaries were a PHC in a given taxable year, such corporation would be subject to PHC tax on its "undistributed PHC income" at a rate of 15%. For taxable years beginning after December 31, 2008, the PHC tax rate would be the highest marginal rate on ordinary income applicable to individuals.

Although Quanta Holdings believes that none of its U.S. subsidiaries is a PHC, we cannot provide assurance that this will be the case because of factors including legal and factual uncertainties regarding the application of the constructive ownership rules, the makeup of Quanta Holdings' shareholder base, the gross income of Quanta Holdings' U.S. subsidiaries and other circumstances that could change the application of the PHC rules to Quanta Holdings and its subsidiaries. In addition, if any of Quanta Holdings' U.S. subsidiaries were to become PHCs we cannot be certain that the amount of PHC income would be immaterial.

Employees

As of March 10, 2008, we employed approximately 46 full-time employees, all of whom are engaged in our run-off activities. Of these employees, the majority deal with financial, legal, regulatory and general administrative matters, four are engaged in assumed and ceded reinsurance, four serve in the policy servicing administration and one handles claims. We also engage consultants and temporary personnel when needed.

In order to retain the services of Jonathan J.R. Dodd, our chief financial officer, and a number of other key employees, we have entered into retention agreements with these employees that provide for specified severance payments in the event of their termination without cause or following a change of control. These agreements also contain non-competition and non-solicitation provisions. However, generally, our other employees, including our chief executive officer, do not have non-competition agreements with us or agreements requiring us to employ them over a fixed term. Therefore, these other employees, including our chief executive officer, may voluntarily terminate their employment with us at any time and are not restricted from seeking employment with others who may seek their expertise.

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Item 1A. Risk Factors

Because of the following factors, as well as other variables affecting our operating results, past financial performance may not be a reliable indicator of future performance, and historical trends should not be used to anticipate results or trends in future periods. Though we have attempted to list comprehensively important cautionary risk factors, we wish to caution investors and others that other factors may in the future prove to be important in affecting our business or results of operations.

Risks Related to the Run-off

Our self-managed run-off is subject to a number of risks.

We recently sold our remaining insurance business and our only remaining business is the run-off of our insurance and reinsurance operations. Running off these businesses includes a number of risks, including the risk that we may not be able to mitigate our existing exposures to our historical underwriting risks, obtain the release of collateral when contracts are cancelled, recover amounts owed to us by our reinsurers and retrocessionaires, enter into commutations, cancellations or other arrangements to mitigate our liabilities, obtain premium that has been due but not paid to us for an extended period of time, release capital from our subsidiaries to our holding company where it is available to our shareholders, reduce our expenses such that they do not exceed income from investments, prevent investment losses or maintain sufficient liquidity in each of our subsidiaries to meet the obligations of those subsidiaries. Furthermore, we remain subject to extensive regulation and the risk that regulators may seek to supervise or gain and retain control over our subsidiaries, which would impede our efforts to extract capital from those subsidiaries over time. In addition, running-off these businesses creates substantial uncertainties and risks that may result in restructuring charges and unforeseen expenses and costs. In addition, as a result of commutations, loss portfolio transfers or other transactions, we may realize gains or losses of assets and liabilities that are different than the amount at which these are currently recorded. If any of these risks materializes, it may have a material adverse impact on the value of our assets, increase our operating costs or result in liquidity strains.

We may experience unfavorable claims development or receive additional claims which could result in additional losses.

Unfavorable claims experience related to the run-off of any or all of our lines of business may occur and would result in losses in the future as we still have policies in force that have terms in excess of ten years. In addition, as required by U.S. Generally Accepted Accounting Principles, we have not established reserves for claims that may arise from losses occurring in the future on the policies that remain in force. If our reserves associated with the underlying reinsurance exposures are insufficient, it could result in losses and an increase in cost and management time related to arbitration and other dispute resolution.

Risks related to any dissolution of our business

In the future, it is possible that we could be placed into liquidation either as a solvent entity or as an insolvent entity. A liquidation as a solvent entity is a voluntary liquidation approved by shareholders. If we were to become insolvent, we would have to be liquidated under the supervision of the Bermuda Supreme Court during which a court appointed liquidator of our company may or may not pursue a scheme of arrangement to shorten the time otherwise required to wind up our business.

In a winding up or liquidation as described above, a liquidator would be appointed and would sell or otherwise dispose of our remaining assets, pay our existing liabilities, including contingent obligations (which would have to be

estimated in advance of payment) and distribute net proceeds, if any, to our shareholders in one or more liquidation distributions. In a liquidation, we may not receive any material amounts for the sale or other disposition of our assets. Further, in a liquidation, we will have significant obligations, including the costs incurred by the independent liquidator appointed and the work required to estimate liabilities and realize assets.

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The amount and timing of distributions, if any, to shareholders in a liquidation cannot be predicted at this time because any distribution would depend on a variety of factors, including the amount of proceeds received from any asset sales or dispositions, the time and amount required to resolve outstanding obligations and the amount of any reserves for future contingencies. If we were to become insolvent, it is unlikely that there will be distributions payable to our common shareholders. Common shareholders will rank last in order of priority of distribution in a liquidation.

We are dependent on our executives and other key employees to run-off our business and to identify, evaluate and complete any strategic transaction. We may not be able to retain our personnel or attract any needed new personnel, which may have a material adverse effect on our company and the execution of our run-off plan.

Our failure to retain members of our management team, key employees and other personnel and our inability to attract any needed new personnel or to use our existing personnel in new, altered or expanded roles could significantly and negatively affect our ability to conduct our self-managed run-off and to evaluate and complete any strategic transaction. In order to retain the services of Jonathan J.R. Dodd, our chief financial officer, and a number of other key employees, we have entered into retention agreements with these employees that provide for specified severance payments in the event of their termination without cause or following a change of control. These agreements also contain non-competition and non-solicitation provisions. However, we do not have a retention agreement with Peter D. Johnson, our chief executive officer. He and our other employees who we did not enter into retention agreements with are not restricted from seeking employment with our competitors or others who may seek their expertise.

We face significant litigation relating to alleged securities law violations.

Two class action lawsuits have been filed against Quanta Holdings and certain of its officers and directors on behalf of putative classes consisting of investors who purchased our publicly traded series A preferred securities and common shares. The complaints allege, among other things, that we made false, misleading and incomplete statements regarding loss estimates in violation of the federal securities laws. It is possible that additional lawsuits relating to these matters may be filed against us and/or certain of our current and former officers and directors in the future. It is also possible that administrative proceedings or regulatory proceedings could be commenced against us in the future.

These lawsuits and any future proceedings could be expensive and could divert management's attention and other resources away from other matters. Any such diversion of management's attention or other resources could negatively and materially impact our self-managed run-off. We cannot predict the timing of any trials with respect to these lawsuits and any future proceedings. We are not currently able to estimate legal defense costs or the amount of any damages that we may be required to pay in connection with these lawsuits and any future proceedings. The class action lawsuits which could continue for a significant period, are currently at an early stage and we have very little information as to the course either will take. In view of the inherent difficulty of predicting the outcome of litigation, particularly where the claimants seek indeterminate damages, we are unable to predict the outcome of these matters and at this time cannot reasonably estimate the possible loss or range of loss with respect to this lawsuit and any future proceedings.

We have not established any reserves for any potential liability relating to the class action lawsuits. We have insurance coverage (above a certain self-insured retention) with respect to claims such as these lawsuits but it is not currently possible to determine whether such insurance coverage will be adequate to cover our defensive costs and any losses.

The existence of the class action lawsuits or the perceived probability of future proceedings could have a material adverse effect on the market price of our common stock.

Our business, results of operations and financial condition have been and could continue to be adversely affected by catastrophic events.

Although we are no longer writing property reinsurance business that is exposed to catastrophes, certain lines of business that we have underwritten, including marine and aviation reinsurance and

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environmental, have large aggregate exposures, including to natural and man-made disasters such as hurricane, typhoon, windstorm, flood, earthquake, acts of war, acts of terrorism and political instability for periods of up to ten years. Additionally, we retain property exposure from our program business. Our loss experience generally has and, despite our exit from the property reinsurance and the technical risk property insurance markets, we expect that it will continue to be subject to infrequent events of great severity. In the future we may recognize additional net losses related to Hurricanes Katrina, Rita and Wilma and other catastrophes. If our actual losses from Hurricanes Katrina, Rita and Wilma are materially greater than our estimated losses, our results of operations and financial condition could be materially adversely affected.

We purchase reinsurance for our insurance and reinsurance operations in order to mitigate the volatility of losses upon our financial results. Based on our current estimate of losses related to Hurricanes Katrina and Rita, we have exhausted our reinsurance and retrocessional protection with respect to Hurricane Katrina and our marine reinsurance with respect to Hurricane Rita. If our Hurricane Katrina losses prove to be greater than currently anticipated, we have no further reinsurance and retrocessional coverage available for that windstorm. If our marine reinsurance losses for Hurricane Rita prove greater than currently anticipated, we will have no further retrocessional coverage available for marine reinsurance losses for that windstorm. Additionally, the occurrence of additional large loss events could reduce the reinsurance coverage that is available to us and could weaken the financial condition of our reinsurers, which could have a material adverse effect on our results of operations.

Losses from these types of catastrophic events could eliminate our shareholders' equity and statutory surplus (which is the amount remaining after all liabilities, including loss reserves, are subtracted from all admitted assets, as determined under statutory accounting principles). Increases in the values and geographic concentrations of insured property and the effects of inflation have resulted in increased severity of industry losses in recent years and we expect that those factors will increase the severity of catastrophe losses in the future.

We may be required to post additional security under insurance and reinsurance agreements.

If our actual losses exceed our estimates or as a result of future losses and other events, we may be required to post additional security under some of our insurance and reinsurance contracts either through the issuance of letters of credit or the placement of securities in trust under the terms of those insurance or reinsurance contracts. If we fail to maintain or enter into adequate letter of credit facilities on a timely basis, we would be required to place securities in trust or similar arrangements, which would be more difficult and costly to establish and administer and could lead to liquidity strains.

Our reliance on brokers subjects us to their credit risk.

In accordance with industry practice, we frequently pay amounts owed on claims under our insurance or reinsurance contracts to brokers, and these brokers, in turn, are expected to pay these amounts over to the clients that have purchased insurance or reinsurance from us in the past. If a broker fails to make such a payment in a significant portion of business that we write, it is highly likely that we will be liable to the client for the deficiency under local laws or contractual obligations. Likewise, when we are required to return premiums in connection with a cancellation or commutation, the brokers collect these payments from us but these premiums are not considered returned. Accordingly, the policy is not cancelled or commuted and our risk is not terminated until the broker returns these premiums to the client. Lastly, our reinsurers and retrocessionaires in many cases make payments owed to us to brokers and these brokers, in turn, are expected to pay these amounts to us. If a broker fails to make such a payment to us, we may be unsuccessful in obtaining payment from the reinsurer or retrocessionaire or we may incur costs in enforcing the payment of amounts owed to us. Consequently, we assume a degree of credit risk associated with

brokers around the world with respect to most of our business.

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If actual claims exceed our loss reserves, our financial position could be significantly adversely affected.

Our success depends upon our ability to accurately assess the risks associated with the businesses that we insured and reinsured. To the extent actual claims exceed our expectations we will be required to immediately recognize the less favorable experience as we become aware of it. This could cause a material increase in our liabilities and reduction of capital. It is early in our history and the number and size of reported claims may increase, and their size could exceed our expectations.

A portion of our business has high attachment points of coverage. Reserving for losses is inherently complicated in that losses in excess of the attachment level of our policies are characterized by high severity and low frequency, and other factors which could vary significantly as claims are settled. This limits the volume of relevant industry claims experience available from which to reliably predict ultimate losses following a loss event. In addition, there always exists a reporting lag between a loss event taking place and the reporting of the loss to us. These incurred but not reported losses are inherently difficult to predict. Because of the variability and uncertainty associated with loss estimation, it is possible that our individual case reserves for each catastrophic event and other case reserves are incorrect, possibly materially.

These factors require us to make significant assumptions when establishing loss reserves. Since we have insufficient past loss experience, we supplement this information with industry data. This industry data may not match our risk profile, which introduces a further degree of uncertainty into the process. Accordingly, actual claims and claim expenses paid may deviate, perhaps substantially, from the reserve estimates reflected in our financial statements.

In our reinsurance business line, like other reinsurers, we do not separately evaluate each of the individual risks assumed under reinsurance treaties. Therefore, we are largely dependent on the original underwriting decisions made by ceding companies. We are subject to the risk that the ceding companies may not have adequately evaluated the risks to be reinsured and that the premiums ceded may not adequately compensate us for the risks we assume.

If our loss reserves are determined to be inadequate, we will be required to increase loss reserves at the time of such determination with a corresponding reduction in our net income in the period in which the deficiency is rectified. It is possible that claims in respect of events that have occurred could exceed our loss reserves and have a material adverse effect on our results of operations or our financial condition in general.

The failure of any of the loss limitation methods we employ could have a material adverse effect on our financial condition or our results of operations.

We have sought to limit our loss exposure by writing a number of our reinsurance contracts on an excess of loss basis, adhering to maximum limitations on reinsurance written in defined geographical zones, limiting program size for each client and by prudent underwriting of each program written. In the case of proportional treaties, we sought per occurrence limitations or loss ratio caps to limit the impact of losses from any one event. We cannot be sure that any of these loss limitation methods has been or will be effective. We cannot assure you that various provisions of our policies, such as limitations or exclusions from coverage or choice of forum, will be enforceable in the manner we intended. Disputes relating to coverage and choice of legal forum may also arise. Underwriting is inherently a matter of judgment, involving important assumptions about matters that are inherently unpredictable and beyond our control, and for which historical experience and probability analysis may not provide sufficient guidance. As a result, our actual claims could substantially exceed our expectations, which could have a material adverse effect on our financial condition or our results of operations, possibly to the extent of eliminating our shareholders' equity.

A significant amount of our invested assets is subject to market volatility.

We invest the premiums we received from customers. Our investment portfolio currently contains highly rated and liquid fixed income securities. Our investment portfolio is invested by professional investment advisory management firms under the direction of our management team in accordance

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with our investment guidelines and are subject to market-wide risks and fluctuations, as well as to risks inherent in particular securities. The volatility of our claims may force us to liquidate securities. The obligations under the credit facility are currently fully secured by investments and cash. If a default occurs under the credit agreement, our lenders may require us to cash collateralize a portion or all of the outstanding letters of credit issued under the facility, which may be accomplished through the substitution or liquidation of collateral. These events may cause us to incur capital losses. Our investment results and, therefore, our financial condition may also be impacted by changes in the business, financial condition or results of operations of the entities in which we invest, as well as changes in interest rates, government monetary policies, general economic conditions and overall market conditions. Further, if we do not structure our investment portfolio so that it is appropriately matched with our insurance and reinsurance liabilities, we may be forced to liquidate investments prior to maturity at a significant loss to cover such liabilities. Investment losses could significantly decrease our asset base, which will affect our ability to conduct business.

Our utilization of program managers and other third parties to support our business exposes us to operational and financial risks.

In our program product line, we relied on program managers, and other agents and brokers participating in our programs, to produce and service a substantial portion of our business in this segment. In these arrangements, we typically granted the program manager the right to bind us to newly issued insurance policies, subject to underwriting guidelines we provided and other contractual restrictions and obligations. Should our managers have issued policies that contravene these guidelines, restrictions or obligations, we could nonetheless be deemed liable for these policies. We aim to resist claims related to policies that exceeded or expanded on our underwriting intention, however, it is possible that we would not prevail in such an action, or that our program managers would be unable to substantially indemnify us for their contractual breach.

We also relied on our managers, or other third parties we retained, to collect premiums and to pay valid claims. While we strive to mitigate these risks through our contractual arrangement with the program managers and other third parties, we remain exposed to these credit and operational risks, without necessarily relieving us of our obligations to potential insureds. We could also be exposed to potential liabilities relating to the claims practices of the third-party administrators we have retained to manage claims activity that we expect to arise in our program operations. Although we have implemented auditing and other oversight protocols for our program, we cannot assure you that these measures will be sufficient to alleviate all of these exposures.

Assessments and other surcharges for guaranty funds and similar arrangements may have a negative impact on our financial condition.

Virtually all states in the U.S. require insurers licensed to do business therein to bear a portion of the unfunded obligations of impaired or insolvent insurance companies. These obligations are funded by assessments, which are levied by guaranty associations or similar entities within the state, up to prescribed limits, on all member insurers in the state on the basis of the proportionate share of the premiums written by member insurers in the lines of business in which the impaired, insolvent or failed insurer was engaged during the period in which the member insurer was engaged in those lines of business. Accordingly, we may be assessed in the future on a portion of premiums we wrote before we commenced our self-managed run-off. The effect of these assessments and arrangements, or changes in them, could have a negative impact on our financial condition in any given period.

The availability of reinsurance and retrocessional coverage that we use to limit our exposure to risks may be limited, and counterparty credit and other risks associated with our reinsurance arrangements may result in losses which could adversely affect our financial condition and results of operations.

To limit our risk of loss and to mitigate the volatility of losses upon our financial results, we used reinsurance and retrocessional coverage, which is reinsurance of a reinsurer's business. The availability and cost of reinsurance and retrocessional protection is subject to market conditions, which are

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beyond our control. Currently, there is a high level of demand for these arrangements. The occurrence of additional large loss events could reduce the reinsurance coverage that is available to us and could weaken the financial condition of our reinsurers which could have a material adverse effect on our results of operations. We cannot assure you that we will be able to renew adequate protection at cost-effective levels in the future. Our failure to maintain adequate reinsurance or retrocessional arrangements could adversely affect our business, financial condition and results of operations.

As a result of market conditions and other factors, we may not be able to successfully alleviate risk through reinsurance and retrocessional arrangements. Further, we are subject to credit risk with respect to our reinsurance and retrocessional arrangements because the ceding of risk to reinsurers and retrocessionaires will not relieve us of our liability to the clients or companies we insure or reinsure. In addition, we have experienced some instances of slower payments from, and disputes about amounts owed to us with, our reinsurers and retrocessionaires. As a result, we may incur losses attributable to our inability to recover amounts from retrocessionaires or ceding companies either due to disputes with the retrocessionaires or ceding companies, their financial condition or both. If our reserves for amounts recoverable from retrocessionaires or ceding companies, as well as reserves associated with the underlying reinsurance exposures are insufficient, it could result in losses and an increase in cost and management time related to arbitration and other dispute resolution.

We could face unanticipated losses from war, terrorism and political unrest, and these or other unanticipated losses could have a material adverse effect on our financial condition and results of operations.

We may have exposure to unexpected losses resulting from future man-made catastrophic events, such as acts of war, acts of terrorism and political instability. Although we may attempt to exclude losses from terrorism and certain other similar risks from some coverages we wrote, we may not be successful in doing so. In addition, we have written policies explicitly limiting the exposure of our clients to the credit worthiness of their commercial trade partners in some emerging markets or to political uncertainty in those countries which could interfere with the execution of commercial contracts they have entered into. These risks are inherently unpredictable and may increase the frequency or severity of losses. It is difficult to predict the timing of such events or to estimate the amount of loss that any given occurrence will generate. To the extent that losses from such risks occur, our financial condition and results of operation could be materially adversely affected.

We rely on our information technology and telecommunication systems, and the failure of these systems could materially and adversely affect our business.

We are highly dependent upon the successful and uninterrupted functioning of our information technology and telecommunications systems. We rely on these systems to process claims, commutations and cancellations, to facilitate collections and to monitor our investment portfolio. These systems also enable us to perform actuarial and other modeling functions. We believe our technology and telecommunications systems are critical to our business and our ability to compete successfully. The failure of these systems, or the termination of a third-party software license upon which any of these systems is based, could interrupt our operations. Because our information technology and telecommunications systems interface with and depend on third-party systems, we cannot be certain that we will have continued access to these third-party systems and we could experience service denials if demand for such services exceeds capacity or such third-party systems fail or experience interruptions. In addition, we cannot make any assurances that our systems will continue to operate as intended. If sustained or repeated, a system failure or service denial could result in a deterioration of our ability to write and process new and renewal business and provide customer service or compromise our ability to pay claims in a timely manner. This could result in a material adverse effect on our business.

Our holding company structure and certain regulatory and other constraints, including our credit facility, affect our ability to pay dividends on our shares and return capital.

Quanta Holdings is a holding company. As a result, we do not, and will not, have any significant operations or assets other than our ownership of our subsidiaries. Dividends and other permitted

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distributions from our operating subsidiaries will be our sole source of funds to pay dividends, if any, to our common shareholders and to meet ongoing cash requirements. Additionally, as we continue to run-off and wind-up our businesses we will be seeking, over time and subject to the approval of our regulators, to extract additional capital from our subsidiaries and dividend it to our holding company where it can be available to our shareholders. Because we are a holding company, our ability to pay additional dividends on our common shares is limited by restrictions on our ability to obtain funds through dividends from our subsidiaries.

The ability of our operating subsidiaries to make payments to Quanta Holdings is limited by the applicable laws and regulations of the domiciles in which the subsidiaries operate. These laws and regulations subject our subsidiaries to significant restrictions and require, among other things, the submission and approval of a withdrawal plan or similar arrangements by regulators, the maintenance by some of our subsidiaries of minimum solvency requirements and the limitation of the amount of dividends that these subsidiaries can pay to us. In addition, following the withdrawal of our A.M. Best rating, the BMA, the regulator of one of our principal insurance subsidiaries, Quanta Re, amended Quanta Re's license to, among other things, restrict it from making any dividend payments to Quanta Holdings without the prior approval of the BMA and to prohibit it from entering into certain transactions. The inability of our operating subsidiaries to pay dividends or to return capital in an amount sufficient to enable us to meet our cash requirements at the holding company level could have a material adverse effect on our operations and on our ability to pay additional dividends. The paying of dividends or the return of capital to the holding company requires regulatory approval. We have worked, and will continue to work, over time, with applicable regulatory authorities to facilitate further dividends from our insurance subsidiaries to Quanta Holdings. Working with these regulators takes time and will require us to meet many conditions, especially given that most of our business is in run-off.

We are subject to Bermuda regulatory constraints that affect our ability to pay dividends on our shares and make other payments. Under the Companies Act 1981 of Bermuda, as amended, or the Companies Act, even though we are solvent and able to pay our liabilities as they become due, we may not declare or pay a dividend or make a distribution if we have reasonable grounds for believing that we are, or will after the payment be, unable to pay our liabilities as they become due or if the realizable value of our assets will thereby be less than the aggregate of our liabilities and our issued share capital and share premium accounts.

Our business could be adversely affected by Bermuda employment restrictions.

We have hired a number of non-Bermudians to work for us in Bermuda. Under Bermuda law, non-Bermudians (other than spouses of Bermudians) may not engage in any gainful occupation in Bermuda without an appropriate governmental work permit. Work permits may be granted or extended by the Bermuda government upon showing that, after proper public advertisement in most cases, no Bermudian (or spouse of a Bermudian) or a holder of a permanent resident's certificate or holder of a working resident's certificate is available who meets the minimum standard requirements for the advertised position. The Bermuda government recently announced a new policy limiting the duration of work permits to six years, with certain exemptions for key employees. While we have been able to obtain work permits that we have needed for our employees to date, we can not assure you that we will not encounter difficulties in the future. We may not be able to use the services of one or more of our key employees if we are not able to obtain work permits for them, which could have a material adverse effect on our business.

We may be adversely affected by interest rate changes.

Our investment portfolio contains interest rate-sensitive instruments, such as bonds, which may be adversely affected by changes in interest rates. Because of the unpredictable nature of losses that may arise under insurance and reinsurance policies, we expect our liquidity needs will be substantial and may arise at any time. Increases in interest

rates during periods when we sell investments to satisfy liquidity needs may result in losses. Changes in interest rates could also have an adverse effect on our investment income and results of operations. For example, if interest rates decline, reinvested funds will earn less than expected.

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In addition, our investment portfolio includes highly-rated mortgage-backed securities. As with other fixed income investments, the fair market value of these securities fluctuates depending on market and other general economic conditions and the interest rate environment. Changes in interest rates can expose us to prepayment risks on these investments. In periods of declining interest rates, mortgage prepayments generally increase and mortgage-backed securities are prepaid more quickly, requiring us to reinvest the proceeds at the then current market rates. In periods of increasing interest rates, these investments are exposed to extension risk, which occurs when the holders of underlying mortgages reduce the frequency on which they prepay the outstanding principal before the maturity date and delay any refinancing of the outstanding principal.

Interest rates are highly sensitive to many factors, including governmental monetary policies, domestic and international economic and political conditions and other factors beyond our control. Although we attempt to take measures to manage the risks of investing in a changing interest rate environment, we may not be able to mitigate interest rate sensitivity effectively. Our mitigation efforts include maintaining a high quality portfolio with a relatively short duration to reduce the effect of interest rate changes on book value. Despite our mitigation efforts, a significant increase in interest rates could have a material adverse effect on our book value.

Fluctuations in currency exchange rates may cause us to experience losses.

Our functional currency is the U.S. dollar. Our operating currency generally is also the U.S. dollar. However, the premiums receivable and losses payable in respect of a portion of our business is denominated in currencies of other countries. For example, Quanta Europe operated in a variety of currencies. We attempt to manage our foreign currency risk by seeking to match our liabilities under insurance and reinsurance policies that are payable in foreign currencies either with forward purchase contracts or with investments that are denominated in these currencies.

To the extent we believe that it may be practical, we hedge our foreign currency exposure with respect to potential losses by maintaining assets denominated in the same currency or entering into forward purchase contracts for specific currencies. We may use forward purchase contracts if we are advised of known or probable significant losses that will be paid in non-U.S. currencies in order to manage currency fluctuation exposure. We may also use forward purchase contracts to hedge our non-U.S. dollar currency exposure with respect to premiums receivable, which will be generally collected over the relevant contract term to the extent practical and to the extent we do not expect we will need these receipts to fund potential losses in such currencies. We may also make foreign currency-denominated investments, generally for the purpose of improving overall portfolio yield. However, we may not be successful in reducing foreign currency exchange risks. As a result, we may from time to time experience losses resulting from fluctuations in values of foreign currencies, which could have a material adverse effect on our results of operations.

Our returns may be adversely impacted by inflation.

The effects of inflation could cause the severity of claims to rise in the future. Our reserve for losses and loss expenses will include assumptions about future payments for settlement of claims and claims handling expenses, such as medical treatments and litigation costs. To the extent inflation causes these costs to increase above reserves established for these costs, we would be required to increase our loss reserves with a corresponding reduction in our net income in the period in which the deficiency is identified.

Our liability transfer program may expose us to liability.

We have created two liability assumption programs under which a special-purpose entity assumes specified liabilities associated with environmental exposures. Our liability assumption program requires extensive technical skills and

judgments in order to evaluate the significant risks associated with the properties subject to the program. We are exposed to substantial liabilities related to the environmental conditions associated with assuming liabilities with respect to these properties that could materially adversely affect our financial position.

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We are subject to extensive regulation in Bermuda, the United States and Ireland, which may adversely affect our ability to achieve our run-off objectives. If we do not comply with these regulations, we may be subject to penalties, including fines, suspensions and withdrawals of licenses, which may adversely affect our financial condition and results of operations.

We are subject to extensive governmental regulation and supervision. Most insurance regulations are designed to protect the interests of policyholders rather than shareholders and other investors. These regulations, generally administered by a department of insurance in each jurisdiction in which we will do business, relate to, among other things:

- of solvency, including risk-based capital measurements;
 - and their agents;
 - and nature of risks assumed;
 - nature, quality and concentration of investments;
 - ability of our insurance company subsidiaries to pay dividends to us;
 - ability to transfer shares in our insurance company subsidiaries;
 - transactions between insurance company subsidiaries and their affiliates;
 - size of risks insurable under a single policy;
 - for the benefit of policyholders;
 - forms and premium rates;
 - methods of accounting;
 - examinations of our operations and finances;
 - and content of records of financial condition required to be filed; and
 - for unearned premium, losses and other purposes.
- standards
 - licensing of insurers
 - limits on the size
 - restrictions on the
 - restrictions on the
 - restrictions on our
 - restrictions on
 - restrictions on the
 - requiring deposits
 - approval of policy
 - requiring certain
 - periodic
 - prescribing the form
 - requiring reserves

Insurance departments also conduct periodic examinations of the affairs of insurance companies and require the filing of annual and other reports relating to financial condition, holding company issues and other matters. These regulatory requirements and the periodic examinations which, because of our run-off activities, we may be more frequently subject to than more established companies, may adversely affect or inhibit our ability to achieve some or all of our business objectives.

Regulation in the United States. In recent years, the state insurance regulatory framework in the United States has come under increased federal scrutiny, and some state legislators have considered or enacted laws that may alter or

increase state authority to regulate insurance companies and insurance holding companies. Moreover, the National Association of Insurance Commissioners, which is an association of the insurance regulatory officials of all 50 states and the District of Columbia, and state insurance regulators regularly reexamine existing laws and regulations, interpretations of existing laws and the development of new laws. In addition, surplus lines associations in various states are asserting themselves more aggressively. Federal legislation is also being discussed that would require all states to adopt uniform standards relating to the regulation of products, licensing, rates and market conduct. We are unable to predict whether any of these or other proposed laws and regulations will be adopted, the form in which any such laws and regulations would be adopted, or the effect, if any, these developments would have on our run-off operations and financial condition.

We are subject to numerous federal regulations, including the Securities Act of 1933, the Exchange Act and other federal securities laws. As we continue with the run-off of our business, we must monitor our compliance with these laws, including our maintenance of any available exemptions from registration as an investment company under the Investment Company Act of 1940. Any failure to comply with these laws or maintain our exemption could have a material adverse effect on our operations and on the market price of our common shares.

Regulation in Bermuda. Quanta Re and Quanta U.S. Re are registered Bermuda insurance companies and subject to regulation and supervision in Bermuda. The applicable Bermuda statutes

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and regulations generally are designed to protect insureds and ceding insurance companies, not our shareholders. Quanta Re and Quanta U.S. Re are not registered or licensed as insurance companies in any jurisdiction outside Bermuda, conduct business through offices in Bermuda and do not maintain an office, and their personnel do not conduct any insurance activities, in the United States or elsewhere. Inquiries or challenges to the activities of Quanta Re or Quanta U.S. Re. may be raised in the future.

Regulation in Ireland. Quanta Europe is a non-life insurance company incorporated under the laws of Ireland subject to the regulation and supervision of the Irish Financial Regulator, or FR, under the Irish Insurance Acts, 1909 to 2000 and the regulations relating to insurance business and directions made under those regulations, or together, the Insurance Acts and Regulations. In addition, Quanta Europe is subject to certain additional supervisory requirements of the FR for authorized non-life insurers that fall outside the strict legislative framework, such as guidelines issued by the FR in 2001 requiring actuarial certification of certain reserves. Among other things, without consent of the FR, Quanta Europe is not permitted to reduce the level of its initial capital, or make any dividend payments or loans.

We may be subject to U.S. tax that may have a material adverse effect on our results of operations and your investment.

Quanta Holdings and Quanta Re are Bermuda companies and Quanta Europe is an Irish company. We believe we are managing our business so that each of these companies is not treated as engaged in a trade or business within the United States and, as a result, will not be subject to U.S. tax (other than U.S. excise tax on insurance and reinsurance premium income attributable to insuring or reinsuring U.S. risks and U.S. withholding tax on certain U.S. source investment income). However, because there is considerable uncertainty as to what activities constitute being engaged in a trade or business within the United States, we cannot be certain that the U.S. Internal Revenue Service will not be able to successfully contend that any of Quanta Holdings or its foreign subsidiaries are engaged in a trade or business in the United States. If Quanta Holdings or any of its foreign subsidiaries were considered to be engaged in a business in the United States, we could be subject to U.S. corporate income and branch profits taxes on the portion of our earnings effectively connected to such U.S. business, in which case our results of operations and your investment could be materially adversely affected. See “Item 1. Business—Material Tax Considerations—Certain U.S. Federal Income Tax Considerations—U.S. Taxation of Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines, Quanta U.S. Re and Quanta Indemnity.”

Quanta Holdings’ U.S. subsidiaries might be subject to additional U.S. tax on a portion of their income if a subsidiary is considered a personal holding company, or PHC, for U.S. federal income tax purposes. This status will depend on whether more than 50% of our shares by value could be deemed to be owned (under some constructive ownership rules) by five or fewer individuals and whether 60% or more of the income of any of its U.S. subsidiaries, as determined for U.S. federal income tax purposes, consists of “personal holding company income,” which is, in general, certain forms of passive and investment income. We believe based upon information made available to us regarding our shareholder base that none of Quanta Holdings’ subsidiaries should be considered a PHC. Additionally, we believe we are managing our business to minimize the possibility that we will meet the 60% income threshold. However, because of the lack of complete information regarding our ultimate share ownership (i.e., as determined by the constructive ownership rules for PHCs), we cannot assure you that none of Quanta Holdings’ subsidiaries will be considered a PHC or that the amount of U.S. tax that would be imposed if it were not the case would be immaterial. See “Item 1. Business—Material Tax Considerations—Certain U.S. Federal Income Tax Considerations—U.S. Taxation of Quanta Holdings, Quanta Re, Quanta Europe, Quanta U.S. Holdings, Quanta Specialty Lines, Quanta U.S. Re and Quanta Indemnity—Personal Holding Companies.”

We may be subject to additional Irish tax or U.K. tax.

If any of our non-Irish companies were considered to be resident in Ireland, or to be doing business in Ireland, or, in the case of our U.S. subsidiaries which qualify for the benefits of an existing

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tax treaty with Ireland, to be doing business through a permanent establishment in Ireland, those companies would be subject to Irish tax. If we or any of our subsidiaries were considered to be resident in the United Kingdom, or to be carrying on a trade in the United Kingdom through a permanent establishment in the United Kingdom, those companies would be subject to United Kingdom tax. If any of our U.S. subsidiaries were subject to Irish tax or U.K. tax, that tax would generally be creditable against their U.S. tax liability, subject to limitations. If we or any of our Bermuda subsidiaries were subject to Irish tax or U.K. tax, that could have a material adverse impact on our results of operation and on the value of our shares.

The impact of Bermuda's letter of commitment to the Organization for Economic Cooperation and Development to eliminate harmful tax practices is uncertain and could adversely affect our tax status in Bermuda.

A number of multinational organizations, including the European Union, the Financial Action Task Force, the Financial Stability Forum, and the Organization for Economic Cooperation and Development, which is commonly referred to as the OECD, have published reports and launched a global dialogue among member and non-member countries on measures to limit harmful tax competition. These measures are largely directed at counteracting the effects of tax havens and preferential tax regimes in countries around the world. Tax haven jurisdictions that do not cooperate with the OECD could face sanctions imposed by OECD member countries. In the OECD's report dated June 26, 2000, Bermuda was not listed as a tax haven jurisdiction because it had previously signed a letter committing itself to eliminate harmful tax practices by the end of 2005 and to embrace international tax standards for transparency, exchange of information and the elimination of any aspects of the regimes for financial and other services that attract business with no substantial domestic activity. We are not able to predict what changes will arise from the commitment or whether these changes will subject us to additional taxes. In addition, we cannot assure you that the OECD will not adopt measures that will have a negative impact on Bermuda companies.

We may become subject to taxes in Bermuda after March 28, 2016, which may have a material adverse effect on our results of operations and your investment.

The Bermuda Minister of Finance, under the Exempted Undertakings Tax Protection Act 1966, as amended, of Bermuda, has given each of Quanta Holdings, Quanta Re and Quanta U.S. Re, an assurance that if any legislation is enacted in Bermuda that would impose tax computed on profits or income, or computed on any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax, then the imposition of any such tax will not be applicable to Quanta Holdings, Quanta Re and Quanta U.S. Re or any of their operations, shares, debentures or other obligations until March 28, 2016. See "Item 1. Business—Material Tax Considerations—Certain Bermuda Tax Considerations." Given the limited duration of the Minister of Finance's assurance, we cannot be certain that we will not be subject to any Bermuda tax after March 28, 2016.

Risks Related to the Industry

The effects of emerging claim and coverage issues on our business are uncertain.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected issues related to claims and coverage may emerge. These issues may adversely affect the run-off of our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until some time after we have issued insurance or reinsurance contracts that are affected by the changes. As a result, the full extent of liability under our insurance or reinsurance contracts may not be known for many years after a contract is issued.

Recent examples of emerging claims and coverage issues include:

• larger settlements and jury awards against professionals and corporate directors and officers covered by professional liability and directors' and officers' liability insurance; and

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plaintiffs targeting property and casualty insurers in purported class action litigation relating to claims-handling, insurance sales practices and other practices related to the conduct of business in our industry.

- a growing trend of

The effects of these and other unforeseen emerging claim and coverage issues are extremely hard to predict and could harm our business, financial condition and results of operations.

Risks Related to our Securities

Provisions in our charter documents may reduce or increase the voting power associated with our shares.

Our bye-laws generally provide that common shareholders have one vote for each common share held by them and are entitled to vote, on a non-cumulative basis, at all meetings of shareholders.

Pursuant to a mechanism specified in our bye-laws, the voting rights exercisable by a shareholder may be limited so that certain persons or groups are not deemed to hold more than 9.5% of the voting power conferred by our shares. In addition, our board of directors retains certain discretion to make adjustments to the aggregate number of votes attaching to the shares of any shareholder that they consider fair and reasonable in all the circumstances to ensure that no person will hold more than 9.5% of the voting power represented by our then outstanding shares.

Under these provisions, some shareholders may have the right to exercise their voting rights limited to less than one vote per share. Moreover, these provisions could have the effect of reducing the voting power of certain shareholders who would not otherwise be subject to the limitation by virtue of their direct share ownership. As a result of any reduction in the votes of other shareholders, your voting power might increase above 5% of the aggregate voting power of the outstanding shares, which may result in your becoming a reporting person subject to Schedule 13D or 13G filing requirements under the Securities Exchange Act of 1934, as amended, or the Exchange Act.

We also have the authority under our bye-laws to request information from any shareholder for the purpose of determining whether a shareholder's voting rights are to be reduced pursuant to the bye-laws. If a shareholder fails to respond to our request for information or submits incomplete or inaccurate information in response to our request, we may, in our sole discretion, determine that the votes of that shareholder shall be disregarded until the shareholder provides the requested information.

It may be difficult for a third party to acquire us.

Provisions of our organizational documents may discourage, delay or prevent a merger, tender offer or other change of control that holders of our shares may consider favorable. These provisions impose various procedural and other requirements that could make it more difficult for shareholders to effect various corporate actions. These provisions could:

effect of delaying, deferring or preventing a change in control of us;

- have the
- discourage bids for
- adversely affect the
- impede the ability

our securities at a premium over the price;

price of, and the voting and other rights of the holders of, our securities; or

of the holders of our securities to change our management.

U.S. persons who own our shares may have more difficulty in protecting their interests than U.S. persons who are shareholders of a U.S. corporation.

The Companies Act, which applies to us, differs in certain material respects from laws generally applicable to U.S. corporations and their shareholders including:

director transactions. Under Bermuda law and our bye-laws, any transaction entered into by us in which a director has an interest is not voidable by us nor can such

- Interested

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director be accountable to us for any benefit realized under that transaction provided the nature of the interest is disclosed at the first opportunity at a meeting of directors, or in writing to the directors. In addition, our bye-laws allow a director to be taken into account in determining whether a quorum is present and to vote on a transaction in which he has an interest following a declaration of the interest pursuant to the Companies Act unless the chairman of the meeting determines otherwise. U.S. companies are generally required to obtain the approval of a majority of disinterested directors or the approval of shareholders before entering into any transaction or arrangement in which any of their directors have an interest, unless the transaction or arrangement is fair to the company at the time it is authorized by the company's board or shareholders.

- Certain transactions with significant shareholders. As a Bermuda company, we may enter into certain business transactions with our significant shareholders, including asset sales, in which a significant shareholder receives, or could receive, a financial benefit that is greater than that received, or to be received, by other shareholders. Such transactions may be entered into with prior approval from our board of directors but without obtaining prior approval from our shareholders. U.S. companies in general may not enter into business combinations with interested shareholders, namely certain large shareholders and affiliates, unless the business combination had been approved by the board in advance or by a supermajority of shareholders or the business combination meets specified conditions.

- Shareholders' suits. The rights of shareholders under Bermuda law are not as extensive as the rights of shareholders under legislation or judicial precedent in many U.S. jurisdictions. Class actions and derivative actions are generally not available to shareholders under the laws of Bermuda. In general, under Bermuda law, derivative actions are permitted only when the act complained of is alleged to be beyond the corporate power of the company, is illegal or would result in the violation of the company's memorandum of association or bye-laws. In addition, Bermuda courts would consider permitting a derivative action for acts that are alleged to constitute a fraud against the minority shareholders or, for instance, acts that require the approval of a greater percentage of the company's shareholders than those who actually approved them.

- Indemnification of directors and officers. Under Bermuda law and our bye-laws, we may indemnify our directors, officers or any other person appointed to a committee of the board of directors (and their respective heirs, executors or administrators) to the full extent permitted by law against all actions, costs, charges, liabilities, loss, damage or expense incurred or suffered by such person by reason of any act done, concurred in or omitted in the conduct of our business or in the discharge of his/her duties; provided that such indemnification shall not extend to any matter involving any fraud or dishonesty (as determined in a final judgment or decree not subject to appeal) on the part of such director, officer or other person. Under our bye-laws, each of our shareholders agrees to waive any claim or right of action, other than those involving fraud or dishonesty, against us or any of our officers or directors. In general, U.S. companies may limit the personal liability of their directors as long as they acted in good faith and without knowing violation of law.

As a result of these differences, U.S. persons who own our shares may have more difficulty protecting their interests than U.S. persons who own shares of a U.S. corporation.

We are a Bermuda company and it may be difficult for you to enforce judgments against us or our directors and executive officers.

We are incorporated under the laws of Bermuda and our business is based in Bermuda. In addition, some of our officers reside outside the United States, and all or a substantial portion of our assets and the assets of these persons are, and will continue to be, located in jurisdictions outside the United States. As such, it may be difficult or impossible to effect service of process within the United States upon us or those persons or to recover against us or them on judgments of U.S. courts, including judgments predicated upon civil liability provisions of the U.S. federal

securities laws.

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Further, no claim may be brought in Bermuda against us or our directors and officers in the first instance for violation of U.S. federal securities laws because these laws have no extraterritorial jurisdiction under Bermuda law and do not have force of law in Bermuda. A Bermuda court may, however, impose civil liability, including the possibility of monetary damages, on us or our directors and officers if the facts alleged in a complaint constitute or give rise to a cause of action under Bermuda law.

We have been advised that there is doubt as to whether the courts of Bermuda would enforce judgments of U.S. courts obtained in actions against us or our directors and officers predicated upon the civil liability provisions of the U.S. federal securities laws or original actions brought in Bermuda against us or these persons predicated solely upon U.S. federal securities laws. Further, we have been advised that there is no treaty in effect between the United States and Bermuda providing for the enforcement of judgments of U.S. courts, and there are grounds upon which Bermuda courts may not enforce judgments of U.S. courts. Some remedies available under the laws of U.S. jurisdictions, including some remedies available under the U.S. federal securities laws, may not be allowed in Bermuda courts as contrary to that jurisdiction's public policy. Because judgments of U.S. courts are not automatically enforceable in Bermuda, it may be difficult for you to recover against us based upon such judgments.

Holders of our shares who own 10% or more of our voting power may be subject to taxation under the "controlled foreign corporation," or CFC, Rules.

Each "10% U.S. Shareholder" of a foreign corporation that is a CFC for an uninterrupted period of 30 days or more during a taxable year, and that owns shares in the CFC directly or indirectly through foreign entities on the last day of the CFC's taxable year, must include in its gross income for U.S. federal income tax purposes its pro rata share of the CFC's "subpart F income," even if the subpart income is not distributed. A foreign corporation is considered a CFC if "10% U.S. Shareholders" own more than 50% of the total combined voting power of all classes of voting stock of the foreign corporation, or the total value of all stock of the corporation. A 10% U.S. Shareholder is a U.S. person, as defined in the Internal Revenue Code, that owns at least 10% of the total combined voting power of all classes of stock entitled to vote of the foreign corporation. A CFC also includes a foreign corporation in which more than 25% of the total combined voting power of all classes of stock (or more than 25% of the total value of the stock) is owned by 10% U.S. Shareholders, on any day during the taxable year of such corporation, if the gross amount of premiums or other consideration for the reinsurance or the issuing of insurance or annuity contracts generating subpart F income exceeds specified limits. For purposes of determining whether a corporation is a CFC, and therefore whether the more-than-50% (or more-than-25%, in the case of insurance income) and 10% ownership tests have been satisfied, shares owned includes shares owned directly or indirectly through foreign entities or shares considered owned under constructive ownership rules. The attribution rules are complicated and depend on the particular facts relating to each investor.

Due to certain bye-law provisions that impose limitations on the concentration of voting power of its shares and that authorize the board to purchase our shares under specified circumstances we believe that we could seek, under certain circumstances, to take action to prevent shareholders from becoming 10% U.S. Shareholders. It is possible, however that the IRS could challenge the effectiveness of these provisions and that a court could sustain such a challenge.

If we determine that your ownership of our shares may result in adverse consequences, we may require you to sell your shares to us.

Our bye-laws provide that we have the option, but not the obligation, to require a shareholder to sell its shares at a purchase price equal to their fair market value to us, to other shareholders or to third parties if our board of directors in its absolute discretion determines that the share ownership of that shareholder may result in adverse tax consequences

to us, any of our subsidiaries or any other shareholder. To the extent possible under the circumstances, the board of directors will use its best

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efforts to exercise this option equally among similarly situated shareholders. Our right to require a shareholder to sell its shares to us will be limited to the purchase of a number of shares that we determine is necessary to avoid or cure those adverse tax consequences.

U.S. persons who hold shares could be subject to adverse tax consequences if we are considered a “passive foreign investment company” for U.S. federal income tax purposes.

We do not intend to conduct our activities in a manner that would cause us to become a passive foreign investment company. However, it is possible that we could be deemed a passive foreign investment company by the IRS for any prior or future year. If we were considered a passive foreign investment company it could have material adverse tax consequences for an investor that is subject to U.S. federal income taxation, including subjecting the investor to a greater tax liability than might otherwise apply or subjecting the investor to tax on amounts in advance of when tax would otherwise be imposed. There are currently no regulations regarding the application of the passive foreign investment company provisions to an insurance company. New regulations or pronouncements interpreting or clarifying these rules may be issued in the future. We cannot predict what impact, if any, this guidance would have on a shareholder that is subject to U.S. federal income taxation. We have not sought and do not intend to seek an opinion of legal counsel as to whether or not we were a passive foreign investment company for any period.

U.S. persons who hold shares may be subject to U.S. income taxation on their pro rata share of our “related party insurance income.”

If:

- Quanta Europe’s or Quanta Re’s related party insurance income equals or exceeds 20% of that company’s gross insurance income in any taxable year,
- direct or indirect insureds (and persons related to such insureds) own (or are treated as owning directly or indirectly) 20% or more of the voting power or value of the shares of Quanta Europe or Quanta Re, and
- U.S. persons are considered to own in the aggregate 25% or more of the stock of either corporation by vote or value,

then a U.S. person who owns shares of Quanta Holdings directly or indirectly through foreign entities on the last day of the taxable year would be required to include in its income for U.S. federal income tax purposes the shareholder’s pro rata share of Quanta Europe’s or Quanta Re’s related party insurance income for the U.S. person’s taxable year that includes the end of the corporation’s taxable year determined as if such related party insurance income were distributed proportionately to such U.S. shareholders at that date regardless of whether such income is distributed. In addition any related party insurance income that is includible in the income of a U.S. tax-exempt organization will be treated as unrelated business taxable income. The amount of related party insurance income earned by Quanta Europe or Quanta Re (generally, premium and related investment income from the direct or indirect insurance or reinsurance of any direct or indirect U.S. shareholder of Quanta Europe or Quanta Re or any person related to such shareholder) will depend on a number of factors, including the geographic distribution of Quanta Europe’s or Quanta Re’s business and the identity of persons directly or indirectly insured or reinsured by Quanta Europe or Quanta Re. Although we do not expect our related party insurance income to exceed 20% of our gross insurance income in the foreseeable future, some of the factors which determine the extent of related party insurance income in any period may be beyond Quanta Europe’s or Quanta Re’s control. Consequently, Quanta Europe’s or Quanta Re’s related party insurance income could equal or exceed 20% of its gross insurance income in any taxable year and ownership of its shares by direct or indirect

insureds and related persons could equal or exceed the 20% threshold described above.

The related party insurance income rules provide that if a shareholder that is a U.S. person disposes of shares in a foreign insurance corporation that has related party insurance income (even if the amount of related party insurance income is less than 20% of the corporation's gross insurance

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income or the ownership of its shares by direct or indirect insureds and related persons is less than the 20% threshold) and in which U.S. persons own 25% or more of the shares, any gain from the disposition will generally be treated as ordinary income to the extent of the shareholder's share of the corporation's undistributed earnings and profits that were accumulated during the period that the shareholder owned the shares (whether or not such earnings and profits are attributable to related party insurance income). In addition, such a shareholder will be required to comply with reporting requirements, regardless of the amount of shares owned by the shareholder. These rules should not apply to dispositions of our shares because Quanta Holdings will not itself be directly engaged in the insurance business and because proposed U.S. Treasury regulations appear to apply only in the case of shares of corporations that are directly engaged in the insurance business. However, the IRS might interpret the proposed regulations in a different manner and the applicable proposed regulations may be promulgated in final form in a manner that would cause these rules to apply to dispositions of our shares.

Changes in U.S. federal income tax law could materially adversely affect an investment in our shares.

The U.S. federal income tax laws and interpretations regarding whether a company is engaged in a trade or business within the United States, or is a passive foreign investment company or whether U.S. persons would be required to include in their gross income the subpart F income or the related party insurance income of a CFC are subject to change, possibly on a retroactive basis. There are currently no regulations regarding the application of the passive foreign investment company rules to insurance companies and the regulations regarding related party insurance income are still in proposed form. New regulations or pronouncements interpreting or clarifying such rules may be issued in the future. We cannot be certain if, when or in what form such regulations or pronouncements may be provided and whether such regulations or guidance will have a retroactive effect.

Information Regarding Forward-Looking Statements

Some of the statements included in this annual report, including those using words such as "believes," "expects," "intends," "estimates," "projects," "predicts," "assumes," "anticipates," "plans," and "seeks" and comparable terms, are forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. Forward-looking statements are not statements of historical fact and reflect our views and assumptions as of the date of this annual report regarding future events and operating performance. Because of our limited operating history, many statements relating to us and our self-managed run-off including statements relating to our position, operations and business strategies, are forward-looking statements.

All forward-looking statements address matters that involve risks and uncertainties. There are important factors that could cause our actual results to differ materially from those indicated in these statements. We believe that these factors include but are not limited to the following:

- We have placed all of our lines of businesses in run-off. Running off these businesses includes a number of risks, including the risk that we may not be able to mitigate our existing exposures to our historical underwriting risks, obtain the release of collateral when contracts are cancelled, recover amounts owed to us by our reinsurers and retrocessionaires, enter into commutations or other arrangements to mitigate our liabilities, obtain premium that has been due but not paid to us for an extended period of time, release capital from our subsidiaries to our holding company where it is available to our shareholders, reduce our expenses such that they do not exceed income from investments, prevent investment losses, maintain sufficient liquidity in each of our subsidiaries to meet the obligations of those subsidiaries or retain control over our subsidiaries;

- The execution of

our run-off plan is expected to create substantial uncertainties and risks that may result in restructuring charges and unforeseen expenses and costs, including expenses related to increased arbitration activities as we seek to enforce our rights. In addition, as a result of commutations, loss portfolio transfers or other transactions, we may realize gains or losses of assets and liabilities that are different than the amount at which these are currently recorded. There can be no assurance that any of these initiatives or their results will not negatively impact our results of operations;

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obligations in certain lines of business that we have underwritten, including marine and aviation reinsurance and environmental insurance, continue to have large aggregate exposures to natural and man-made disasters such as hurricane, typhoon, windstorm, flood, earthquake, acts of war, acts of terrorism and political instability, in certain cases for in excess of ten years, and our results may continue to be volatile as a result;

- Our existing policy

additional dividends from our subsidiaries to Quanta Holdings is restricted by regulations in Bermuda, several states in the United States and the European Union. In addition, the BMA has, pursuant to its regulatory discretion, amended the license of Quanta Re, our principal subsidiary in Bermuda, to require that it, among other things, seek the approval from the BMA prior to paying any dividend to Quanta Holdings and prohibiting it from engaging in any new transactions. We will continue to work with the applicable regulatory authorities to facilitate dividends from our insurance operating subsidiaries to Quanta Holdings. Completing this work is expected to take a long period of time and requires us to meet many conditions, particularly the discharge of all our policy obligations;

- Our ability to pay

estimates of our exposure to ultimate claim costs associated with Hurricanes Katrina, Rita and Wilma are based on available information, claims notifications received to date, industry loss estimates, output from industry models, a review of affected contracts and discussions with brokers and clients. The actual amount of losses from Hurricanes Katrina, Rita and Wilma may vary significantly from our estimates based on such data, which could have a material adverse effect on our financial condition or our results of operations;

- Our current

execute our run-off plan and evaluate and complete any strategic transactions is dependent on our ability to retain our, or attract any needed new, executives and key employees. Our inability to retain, attract and integrate members of our management team, key employees and other personnel could significantly and negatively affect the execution of our run-off plan and the preservation of shareholder value;

- Our ability to

exceed our loss reserves, our financial results could be significantly adversely affected;

- If actual claims

of the loss limitation methods we employ could have a material adverse effect on our financial condition or our results of operations;

- The failure of any

current estimate of losses related to Hurricanes Katrina and Rita, we have exhausted our reinsurance and retrocessional protection with respect to Hurricane Katrina and our marine reinsurance with respect to Hurricane Rita. If our Hurricane Katrina and Rita losses prove to be greater than currently anticipated, we have no further reinsurance and retrocessional coverage available for those windstorms. Furthermore, if there are further catastrophic events relating to our underwriting exposures, our retrocessional coverage for these events may be limited or we may have no coverage at all;

- Based on our

additional premium estimate reductions and cancellations in future periods, we may not receive all of our premiums receivable in cash, and our cash flows could be adversely affected;

- If we receive

significant amount due from reinsurers and retrocessionaires who may refuse to pay our claims because we are a run-off company or for other reasons even when we believe those payments are contractually due to us. These actions, if taken, will increase our expenses as we take legal action and if we are unsuccessful in recovering these amounts, may have a negative impact on our financial results and position;

- We have a

future availability, cost or quality of reinsurance;

- Changes in the

potential litigation and arbitration;

- Risks relating to

regulation or tax laws applicable to us or our customers;

- Changes in
- Risks relating to our

reliance on program managers, third-party administrators, consultants and other supporting vendors for claims handling, data, premium collection, IT and administrative functions;

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accounting policies or practices; and

- Changes in
- Changes in general economic conditions, including inflation, foreign currency exchange rates, interest rates and other factors.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from our projections. Additionally, the list of factors above is not exhaustive and should be read with the other cautionary statements that are included in this annual report under “Item 1A. Risk Factors” and that are otherwise described from time to time in our U.S. Securities and Exchange Commission reports filed after this annual report. Any forward-looking statements you read in this annual report reflect our current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to, among other things, our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You should specifically consider the factors identified in this annual report that could cause actual results to differ from those discussed in the forward-looking statements before making an investment decision. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future events or otherwise.

Market data and forecasts used in this annual report have been obtained from independent industry sources as well as from research reports prepared for other purposes. We have not independently verified the data obtained from these sources and we cannot assure you of the accuracy or completeness of the data. Forecasts and other forward-looking information obtained from these sources are subject to the same qualifications and uncertainties applicable to the other forward-looking statements in this annual report.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We have entered into a lease for office space in Bermuda that contains 5,400 square feet. The lease expires on September 30, 2010. The annual lease payment for this office space is approximately \$244,300.

The lease for office space in Dublin expired on July 31, 2007. However, we extended this lease for a further period expiring on June 30, 2008 and moved into a smaller office of approximately 80 square feet. This lease may be cancelled prior to that date following three months notice. The annual lease payments for this office space is approximately \$55,000

The headquarters of Quanta U.S. Holdings and our other U.S. subsidiaries is located in New York, New York and contains approximately 13,650 square feet. The term of the lease expires in February 2012 with an option to extend the lease term by an additional five years. The annual lease payment for this office starts at approximately \$464,100 and increases in annual increments to approximately \$555,220 at the end of the lease term. Our other offices in the U.S. are located in Hartford, Connecticut with a lease cost of approximately \$230,000 per year.

We believe that these facilities are sufficient for our current purposes and that alternative space will be available, if needed, on commercially reasonable terms.

Item 3. Legal Proceedings

On February 5, 2007, plaintiff Harold Zirkin filed a complaint against the Company in the U.S. District Court for the Southern District of New York. (Zirkin v. Quanta Capital Holdings, Ltd. et al., U.S. District Court, Southern District of New York, Case No. 07 CV 851.) On February 26, 2007, plaintiff Jorge Coronel filed a complaint against the Company in the same Court. (Coronel v. Quanta Capital Holdings, Ltd. et al., U.S. District Court, Southern District of New York, Case No. 07 CV 1405.) Both complaints alleged that the Company violated the federal securities laws as a result of false or misleading statements in disclosures to the investing public.

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Both of these cases are now pending before U.S. District Judge Robert P. Patterson, Jr. On May 7, 2007, Judge Patterson appointed Zirkin-Cutler Investments, Inc. as lead plaintiff for a putative class of investors who purchased our preferred shares, and appointed Washington State Plumbing and Pipefitting Pension Trust as lead plaintiff for a putative class of investors who purchased our common shares. Judge Patterson directed Zirkin and Washington to file amended pleadings that would supersede the complaints previously filed by Mr. Zirkin and Mr. Coronel.

On July 16, 2007, Zirkin filed an Amended Complaint (the “Zirkin Complaint”). Zirkin purports to sue on behalf of itself and a class of investors who purchased preferred shares of the Company between December 14, 2005 and March 2, 2006. The Zirkin Complaint alleges that the Company made false statements concerning reserves for hurricane-related losses in a registration statement and prospectus that were circulated to investors in connection with a securities offering the Company completed in December 2005. The complaint alleges that the Company is liable under Sections 11 and 12(a)(2) of the Securities Act of 1933.

Zirkin has named as defendants, in addition to the Company, two firms that served as underwriters for this offering (Friedman, Billings, Ramsey & Co., Inc. and BB&T Capital Markets), and six individuals who served as officers or directors of the company at the time of the offering (James Ritchie, Jonathan Dodd, Robert Lippincott III, Michael Murphy, Nigel Morris, and W. Russell Ramsey).

Washington filed a separate Amended Complaint (the “Washington Complaint”) on July 16, 2007. Washington purports to sue on behalf of itself and a class of investors who purchased our common shares between October 4, 2005 and April 3, 2006. The Washington Complaint alleges that during that period, the Company made false and misleading statements, and omitted to state material information, in various disclosures. The disclosures and alleged omissions at issue in the case relate to reserves for hurricane-related losses, reserves related to an oil pipeline leak, and the quality of the Company’s internal controls over financial reporting. The Washington Complaint alleges claims against the Company under Sections 11 and 12(a)(2) of the Securities Act of 1933, based on statements made in connection with the above-referenced securities offering; and under Section 10(b) of the Securities Act of 1934 and Rule 10b-5 promulgated thereunder, based on statements made at various times in various contexts.

The Company, FBR, BBT, and the six individuals named as individual defendants in the Zirkin Complaint (Messrs. Ritchie, Dodd, Lippincott, Murphy, Morris, and Ramsey) are all named as defendants in the Washington Complaint as well. In addition, the Washington Complaint also names as a defendant Tobey Russ (former Chairman of the Company’s Board of Directors and former Chief Executive Officer).

In September 2007, the Company filed motions challenging the legal sufficiency of the claims asserted in both cases, and asked the Court to dismiss both cases. The briefing on these motions was completed in January 2008, but the Court has not yet addressed the motions. In accordance with the Private Securities Litigation Reform Act, discovery in these cases has been stayed pending a ruling by the Court on the motions.

The Court has not yet made any rulings addressing the merits of these cases, nor has the Court decided whether it will certify any case against the Company to proceed as a class action. The Company intends to continue to defend these actions vigorously.

In the normal course of business, we are involved in various claims and legal proceedings, including litigation and arbitration. Management does not believe that the eventual outcome of any such pending ordinary course of business litigation or arbitration is likely to have a material effect on our financial condition. Many of our insurance and reinsurance arrangements require disputes thereunder to be finally settled by binding arbitration. Assets and liabilities which are or may be the subject of arbitration are reflected in the financial statements based on management’s

estimates of the ultimate amount to be realized as paid.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of shareholders during the fourth quarter of the fiscal year ended December 31, 2007.

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PART II

Item 5.

Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our common shares have been traded on the NASDAQ Global Market of The NASDAQ Stock Market LLC ("NASDAQ") under the symbol "QNTA" since May 14, 2004. The following table contains, for the periods indicated, the high and low sales prices per common share.

		Common Shares								
High	Low	2005	First Quarter	\$ 10.25	\$ 7.60	Second Quarter	\$ 8.50	\$ 5.86	Third Quarter	\$
7.45	\$ 5.40	Fourth Quarter	\$ 6.02	\$ 3.55	2006	First Quarter	\$ 5.80	\$ 2.20	Second Quarter	
\$ 3.10	\$ 2.19	Third Quarter	\$ 2.62	\$ 1.22	Fourth Quarter	\$ 2.51	\$ 1.65	2007	First Quarter	
\$ 2.45	\$ 1.97	Second Quarter	\$ 3.23	\$ 1.94	Third Quarter	\$ 2.95	\$ 2.25	Fourth Quarter	\$ 2.94	\$
2.44										

Holders

As of February 29, 2008, we had 70,135,502 common shares issued and outstanding, which were held by two holders of record. The two holders of record include Cede & Co., which holds shares on behalf of The Depository Trust Company, which itself holds shares on behalf of approximately 1,845 beneficial owners of our common shares.

Dividends

As a holding company, we depend on dividends and other permitted payments from our subsidiaries to pay dividends to our common shareholders. Our subsidiaries' ability to pay dividends, as well as our ability to pay dividends, is subject to regulatory, contractual and other constraints. Furthermore, the terms of our letter of credit facility prohibit us from paying dividends on our shares without the consent of our lenders. Future credit agreements or other agreements relating to indebtedness may also contain provisions prohibiting or limiting the payment of dividends on our shares under certain circumstances.

For a discussion about the regulatory environment relating to dividends from our subsidiaries to Quanta Holdings, see "Item 1. Business—Regulation." For additional discussion concerning risks relating to our dividend policy and our holding company structure and its effect on our ability to receive and pay dividends, see "Item 1A.—Risk Factors—Risks Related to the Run-Off—Our holding company structure and certain regulatory and other constraints, including our credit facility, affect our ability to pay dividends on our shares and return capital."

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To date, we have not paid any dividends on our common shares, but we have declared a dividend of \$1.75 per common share payable on March 28, 2008 to shareholders of record on March 25, 2008. It is our intent to dividend additional assets of our subsidiaries to Quanta Holdings once a portion or all of those assets are released by the applicable regulators, a process which will take time. Subject to the above limitations, our board of directors is free to change our dividend practices from time to time and to decrease or increase the dividend paid, or to not pay a dividend, on our common shares based on factors such as the results of operations, financial condition, cash requirements and future prospects and other factors deemed relevant by our board of directors.

Stock Performance Graph

Set forth below is a line graph comparing the dollar change in the cumulative total shareholder return since May 14, 2004, the date on which the common shares of the Company started trading on NASDAQ, through December 31, 2007 as compared to the cumulative total return of the NASDAQ Insurance Group and the NASDAQ Market Index. This graph assumes that the value of investment in the Company's common shares and each index was \$100 on May 14, 2004 and that all dividends were reinvested. The performance shown below is not necessarily indicative of future performance.

COMPARISON OF CUMULATIVE TOTAL RETURN AMONG QUANTA CAPITAL HOLDINGS LTD.,
NASDAQ MARKET INDEX AND NASDAQ INSURANCE GROUP

CUMULATIVE TOTAL RETURN

	5/14/2004	12/31/2004	12/30/2005	12/29/2006	12/31/2007	Quanta Capital Holdings Ltd.	\$		
100.00	\$ 93.23	\$ 51.57	\$ 21.74	\$ 25.78	NASDAQ Insurance Group	\$ 100.00	\$ 114.64	\$ 130.74	
	\$ 147.68	\$ 146.51	NASDAQ Market Index	\$ 100.00	\$ 113.76	\$ 116.26	\$ 128.19	\$ 127.67	

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Recent Sales of Unregistered Securities

During the year ended December 2007, the Company issued to certain employees and members of the Board of Directors of Quanta Holdings, an aggregate of 121,000 options to purchase common shares. These transactions were completed without registration of the relevant security under the Securities Act of 1933, as amended, in reliance upon the exemptions provided by Section 4(2) for transactions not involving a public offering.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

We did not repurchase any of our equity securities during the fourth quarter of the year ended December 31, 2007 and have not adopted a stock repurchase program.

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Item 6. Selected Financial Data

(Expressed in thousands of U.S. dollars except for share and per share amounts)

		Quanta Capital Holdings Ltd. (3)		Predecessor		Year ended				
December 31,										
2007		Year ended								
December 31,										
2006		Year ended								
December 31,										
2005		Year ended								
December 31,										
2004		Period ended								
December 31,										
2003 (4)		Period ended								
September 3,										
2003 (4)		Selected Income Statement Data		Revenues:		Net premiums earned \$ 87,247				
\$ 225,299	\$ 364,075	\$ 237,140	\$ 1,940	\$ —	Total revenues	142,390	258,483	401,165		
254,625	4,465	—	Expenses:		Net losses and loss expenses	31,077	156,121			
324,249	198,916	1,191	—	General and administrative expenses, depreciation and impairment of intangibles						
59,866	100,006	109,607	58,882	42,307	—	Total expenses	122,327	309,124	510,646	
311,864	43,943	—	Net income (loss) from continuing operations	20,051	(50,655)	(109,713)				
(57,239)	(39,478)	—	Net (loss) income from discontinued operations	—	(12,249)	3,761	2,658			
1,001	1,400	Net income (loss)	20,051	(62,904)	(105,952)	(54,581)	(38,477)	1,400		
		Gain on repurchase of Series A preferred shares	2,364	—	—	—	—	Dividends on preferred shares	—	(1,916)
		Net income (loss) to common shareholders	\$ 22,415	\$ (64,820)	\$ (105,952)	\$ (54,581)	\$ (38,477)	\$ (54,581)		
		Weighted average common shares and common share equivalents outstanding basic	70,076,562	69,971,646	57,205,342	56,798,218	31,369,001	1,093,250	Weighted average common	
		shares and common share equivalents outstanding diluted	70,118,100	69,971,646	57,205,342					
		Income (loss) from continuing operations per share basic and diluted (2)	\$ 0.29	\$ (0.72)	\$ (1.92)	\$ (1.01)	\$ (1.26)	\$ —	(Loss) income from discontinued operations per share	
		basic and diluted (2)	\$ —	\$ (0.19)	\$ 0.07	\$ 0.05	\$ 0.03	\$ 1.28	Income from disposal of discontinued	
		operations per share basic and diluted (2)	\$ —	\$ 0.01	\$ —	\$ —	\$ —	\$ —	Gain on repurchase of Series A	
		preferred shares per share basic and diluted (2)	\$ 0.03	\$ —	\$ —	\$ —	\$ —	\$ —	Dividends on Preferred shares	
		per share basic and diluted (2)	\$ —	\$ (0.03)	\$ —	\$ —	\$ —	\$ —	Net income (loss) per share basic and diluted	
		(2)	\$ 0.32	\$ (0.93)	\$ (1.85)	\$ (0.96)	\$ (1.23)	\$ 1.28	Predecessor Pro Forma Data (unaudited):	
		Net income as shown above							\$ 1,400	Pro forma provision for income taxes
(1)		545	Net income adjusted for pro forma income taxes						\$ 855	Pro forma net
		income per share basic and diluted (2)								\$ 0.78

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Quanta Capital Holdings Ltd. (3)		Predecessor	Year ended
December 31,			
2007	Year ended		
December 31,			
2006	Year ended		
December 31,			
2005	Year ended		
December 31,			
2004	Period ended		
December 31,			
2003 (4)	Period ended		
September 3,			
2003 (4)	Summary Balance Sheet Data	Total assets	1,081,355 1,329,226
1,552,091	980,733 573,761 11,249	Reserves for losses and loss expenses	525,088 623,618
533,983	159,794 4,454 —	Unearned premiums	95,586 119,197 336,550 247,936 20,044
—	Deposit liabilities 36,867 37,014 51,509 43,365 — —	Junior subordinated debentures	— 61,857
61,857	41,238 — —	Total liabilities	730,693 925,892 1,096,089 549,824 86,278 5,198
Redeemable preferred shares	— 74,998 71,838 — — —	Total shareholders' equity	\$ 350,662 \$
328,336	\$ 384,164 \$ 430,909 \$ 487,483 \$ 6,051		

(1) As an S corporation, ESC, our predecessor, was not subject to U.S. federal income taxes. At the time of its acquisition, ESC became subject to U.S. income tax. Accordingly, the predecessor historical operating earnings have been adjusted, on a pro forma basis, to reflect taxes at a 38.9% rate including a 35% statutory rate for U.S. federal income taxes and a 3.9% rate, based on a 6% statutory rate for Virginia state income taxes less the related federal tax benefit. (2) Basic earnings per share are computed using the weighted average number of common shares outstanding during the period. All potentially dilutive securities including stock options, restricted stock and warrants are excluded from the basic earnings per share computation. In calculating diluted earnings per share, the weighted average number of shares outstanding for the period is increased to include all potentially dilutive securities using the treasury stock method. Any common stock equivalent shares are excluded from the computation if their effect is anti-dilutive. Basic and diluted earnings per share are calculated by dividing income available to ordinary shareholders by the applicable weighted average number of shares outstanding during the year. (3) Includes the operations of ESC from September 3, 2003, the date of acquisition. We accounted for the acquisition of ESC as a purchase. Following the disposal of ESC during the third quarter of 2006, ESC was presented in the discontinued operations in the Income Statement. See Note 3 to our consolidated financial statements. (4) Included in our predecessor information are amounts relating to the period from January 1, 2003 to September 3, 2003. The information relating to the period ended December 31, 2003 refers to the period September 3, 2003 to December 31, 2003.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our results of operations, financial condition and liquidity and capital resources should be read in conjunction with our audited consolidated financial statements and related notes for the year ended December 31, 2007 contained in this annual report on pages F-1 to F-64 and with the risk factors appearing under "Item 1A. Risk Factors" in this annual report.

Overview

General

Quanta Holdings was incorporated on May 23, 2003 as a Bermuda holding company formed to provide specialty lines insurance, reinsurance, risk assessment and risk technical services on a global basis through its affiliated companies. From the beginning of 2004 until the second half of 2006 we mainly provided specialty lines insurance and reinsurance services on a global basis and to a lesser extent provided risk assessment and risk technical services. Following A.M. Best's rating action in the first quarter of 2006 in the wake of losses from the 2005 hurricanes and subsequent decisions by our Board of Directors after a review of strategic alternatives, we substantially ceased writing new business and began conducting a self-managed run-off of our remaining insurance and reinsurance businesses with the exception of our business at Lloyd's which we had been conducting since the beginning of 2005 and which is more fully described below. On September 15, 2006, we sold Environmental Strategies Consulting LLC ("ESC") for total consideration of \$12.5 million. Prior to its sale, we provided environmental consulting services through ESC.

On February 13, 2008, we sold our business at Lloyd's and from that date forward our operations have been limited to the run off of our insurance and reinsurance businesses. On March 13, 2008, we announced the payment of a special dividend in the aggregate amount of \$122.7 million payable in cash on March 28, 2008. Our Board of Directors is currently considering and evaluating strategic alternatives that may include the sale of our company or some or all of our remaining businesses or assets, or a combination of one or more alternatives. There can be no assurance as to the timing, structure or terms of such a transaction.

During 2007, the following significant events and achievements occurred, all of which are more fully described throughout this annual report:

- We recorded total net favorable loss development (including \$9.0 million from commutations) related to prior year accident periods of \$39.1 million.
- We further reduced our net loss reserves by \$5.1 million through cancellation of insurance contracts with our clients, primarily as a result of policy cancellations in our HBW program.
- We returned approximately \$23.5 million in premiums to our clients during 2007 in connection with cancellations and terminations of insurance policies.
- In the fourth quarter of 2007, we recorded \$9.8 million of net losses and loss expenses in our Lloyd's segment related to Syndicate 4000's professional liability exposure to the subprime mortgage developments in the United States. We expect claims activity within the D&O and E&O insurance markets to rise as a result of an increase in class action lawsuits filed against public companies due to market losses and related stock price depreciation associated with the subprime mortgage and credit crisis in the United States. Furthermore, we recorded a premium deficiency reserve amounting to approximately

\$8.0 million. This premium deficiency reserve relates to the write-off of deferred acquisition costs that are deemed irrecoverable from the future earning of unearned premium reserves because we expect that potential future subprime reported losses on claims made policies may exceed those unearned premium reserves.

- We recognized net gains on commutation of reinsurance contracts of approximately \$9.7 million which consisted of net favorable loss development of approximately \$9.0 million

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and other income of \$1.9 million. This amount was partially offset by returned earned premium of approximately \$1.3 million. The net commutation payments resulted in a reduction in net loss and loss expenses reserves of approximately \$47.1 million and a reduction in premium receivables of approximately \$15.6 million.

- In the fourth quarter of 2007, we recorded approximately \$4.7 million of charges (including \$1.0 million of legal costs) related to our decision to rescind a non-traditional statutory surplus relief life reinsurance contract, which is more fully described below.

During the third quarter of 2007, we repurchased all of the outstanding Series A preferred shares at a price of \$22.50 per share. The aggregate purchase price for the Series A preferred shares was \$70.4 million which resulted in a gain of \$2.4 million, net of repurchase costs and write off of original deferred issuance costs, which is reported as an increase in net income available to common shareholders.

- In the third quarter of 2007, we purchased all of the outstanding junior subordinated debentures for an aggregate purchase price of \$54.5 million. We originally issued and sold an aggregate \$60.0 million of the junior subordinated debentures in private placements. We recognized a gain on repurchase of \$4.4 million, net of repurchase costs and write off of original deferred issuance costs.

- In the first quarter of 2007, we entered into a 100% quota share reinsurance transaction to replace the expired retrocession of substantially all the in-force business in our technical risk property lines of business and to provide protection from future natural peril or catastrophe events in that line.

- We reduced our total general and administrative costs to \$59.9 million (including \$13.8 million in our Lloyd's segment) for the year ended December 31, 2007.

- We generated net investment income of \$41.9 million, excluding net gains on investments, during the year ended December 31, 2007.

- We have further reduced the total amount of letters of credit outstanding under our credit facility to \$91.6 million at December 31, 2007.

- We have reduced the amount of assets placed in trust as collateral for our clients in our run-off segments to \$153.8 million at December 31, 2007.

Summary of Our Financial and Capital Positions

At December 31, 2007, our unrestricted cash and invested assets totaled approximately \$228.8 million. As of March 3, 2008, our total unrestricted assets increased to \$352.9 million primarily as a result of the release of our funds at Lloyd's. This amount will reduce significantly on March 28, 2008 mainly as a result of the dividend payment more fully described below. As at December 31, 2007, our cash and invested assets, which were invested in instruments with an average rating of "AAA", totaled \$801.7 million. At December 31, 2007, a total of \$331.9 million were restricted, or pledged, under letters of credit or trusts established for the benefit of our clients or deposited with U.S. regulatory authorities and approximately \$241.0 million was pledged or deposited with Lloyd's in support of our participation in Syndicate 4000. We continue to seek ways to reduce these restrictions and encumbrances including through commutations, cancellations and transfers and negotiations with our clients, through claim payments and obtaining recoveries from our reinsurers and by reducing the collateral requirements we have under our credit facility.

Our total gross loss reserves were \$525.1 million at December 31, 2007 as compared to \$623.6 million at December 31, 2006. Included in these amounts are \$160.3 million and \$99.6 million relating to our gross loss reserves

in our Lloyd's segment at December 31, 2007 and 2006. The decrease on our total gross loss reserves primarily reflects claims paid during the year of \$89.3 million (which includes the effect of continued contract commutations of \$47.1 million), net favorable loss development on our maturing policy years of \$39.1 million, as more fully described below, and a reduction in our losses and loss expense reserves of \$5.1 million as a result of

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cancellations on policies primarily in our HBW program and the related reduction in reserves associated with those cancellations. This is partially offset by the increase in reserves in our Lloyd's segment as it continued to expand its business during 2007 and incurred subprime related professional liability losses. Our loss reserves represent obligations with short and long term duration. We believe that our shorter term obligations include reinsurance property, reinsurance marine, fidelity, technical risk property, surety and portions of our programs business, including the property component of HBW. The total gross loss and loss expense reserves associated with these lines was approximately \$89.3 million at December 31, 2007. We believe that our longer term obligations include reinsurance casualty, professional, environmental, the warranty portion of our HBW program. The total gross loss and loss expense reserves associated with these lines, excluding Lloyd's, were approximately \$275.5 million at December 31, 2007. The actual period over which we will pay losses for both of our short and long term business could significantly vary from our expectations given the immaturity of our business and our limited claims paying history and run-off status. Excluding Lloyd's, we estimate that approximately 74% of our total gross loss and loss expense reserves are recorded as incurred but not reported, or IBNR, reserves and there can be no certainty as to when these IBNR amounts may become reported, and ultimately, paid losses. Furthermore, our loss and loss expense reserves may change significantly in future periods as we seek to commute, cancel or otherwise transfer our insurance and reinsurance contracts.

During the year ended December 31, 2007, we recorded total net favorable loss development (including those arising from commutations) related to prior year accident periods of \$39.1 million. This amount includes favorable loss development as follows:

- \$14.9 million in several product lines related to mature accident periods in which actual loss experience was better than expected;
- \$9.0 million relating to the commutations of a number of our reinsurance policies;
- \$8.0 million in our Lloyd's segment particularly in relation to the 2005 and 2006 underwriting years;
- \$6.7 million related to the 2005 and 2004 hurricanes; and
- \$0.5 million related to the tornadoes that occurred in the first quarter of 2006.

Partially offsetting these net favorable loss developments are:

- \$65.5 million of estimated loss and loss expense reserves arising from the earning of our unearned premium reserves; and
- \$9.8 million of net loss and loss expenses recorded in our Lloyd's segment related to our estimate of claims associated with Syndicate 4000's professional liability exposure to the subprime mortgage developments in the United States more fully described below under "Our Lloyd's Business".

We also recorded a reduction in our losses and loss expense reserves of \$5.1 million as a result of cancellations on policies, primarily in our HBW program.

With respect to our remaining policies with current and future exposure periods, our gross unearned premium reserves were approximately \$95.6 million at December 31, 2007, which includes \$58.5 million relating to our Lloyd's segment. Some of these policies have exposure periods that extend beyond one year. Excluding Lloyd's, we believe

that approximately 30.6% of our gross unearned premium reserves will be earned within one year. The balance will be earned after one year over the remaining term of the underlying exposure periods to the extent these premiums are not returned following future commutations or cancellations. In the first quarter of 2007 we purchased 100% quota share reinsurance for future losses from natural peril or catastrophe or accidental events that may occur in our technical risk property product line. This reinsurance purchase resulted in approximately \$4.8 million in ceded premium in the first quarter of 2007, and we believe that this significantly reduces our future net loss exposure from these events. We continue to seek to reduce these exposure periods through policy commutation, cancellation and loss portfolio transfers and, where appropriate, through the purchase of reinsurance protection.

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The specialty insurance and reinsurance business that is subject to our self-managed run-off is still exposed to new losses on unexpired policies particularly on our HBW program and in our environmental line of business and adverse development on recorded loss and loss expense reserves. During the run-off we will continue to pay losses as they fall due and collect outstanding loss and loss expenses recoverable from our reinsurers. As we continue to run-off and wind-up our businesses we have sought and will be seeking, over time and subject to the approval of our regulators, to extract capital from our subsidiaries.

We believe that important factors that have a direct impact on the amount of capital that may ultimately be available to our shareholders and the timing of when it will be available include our ability to (1) determine which portion of our business to maintain, commute, cancel, transfer, or otherwise mitigate, as the case may be, (2) mitigate exposures to our capital by purchasing additional reinsurance, (3) make available sufficient assets to facilitate distributions from our subsidiaries, (4) invest our assets in a way that balances risk with return and that is adequately matched with the expected payment periods of our obligations, (5) reduce our expenses, (6) manage our claims and collect premiums receivable and losses recoverable, (7) achieve the release of cash and investment encumbrances relating to reinsurance deposits and other security requirements, (8) manage our capital structure and (9) obtain the approval of our regulators to extract capital from our subsidiaries and distribute it to Quanta Holdings. This process will take a long period of time and require us to meet many conditions. We have engaged our regulators in this process. Following approval from the Bermuda Monetary Authority we declared a dividend of \$1.75 per share or \$122.7 million which is payable on March 28, 2008 to shareholders of record on March 25, 2008. We refer to this as the March dividend payment.

As of December 31, 2007 our total capital was approximately \$350.7 million. Following the March dividend payment of \$122.7 million our capital will decrease and will be subject to regulation mainly in Bermuda and the United States (in Colorado and in Indiana).

Our Lloyd's Business

On February 13, 2008, we sold all of our interests in Syndicate 4000 through the sale of Quanta 4000 Ltd. ("Quanta 4000") and our interest in Pembroke JV. We expect that, in the first quarter of 2008, we will recognize a gain on the sale of our interest in Quanta 4000, with the amount of such gain being determined based on recorded balances as of the date of sale. If the sale had occurred on December 31, 2007, based on balances recorded at that date, the pro forma amount of the gain would have been approximately \$17.9 million. This gain is net of transaction costs, the payment of bonuses to the management and employees of Syndicate 4000 and writing off the cost of our investment in Pembroke JV. There can be no assurances that the gain we record in the first quarter of 2008 will be substantially similar to the amount stated above or that there will be a gain at all. If we record a loss, it could have a material adverse impact on our financial results and statement of operations.

For the year ended December 31, 2007, our Lloyd's business:

contributed \$124.0 million and \$96.4 million in gross and net written premium to our results for the year ended December 31, 2007 as compared to \$91.8 million and \$61.7 million in gross and net written premiums for the year ended December 31, 2006.

- contributed net earned premium of \$80.8 million for the year ended December 31, 2007 as compared to \$65.5 million in net earned premium for the year ended December 31, 2006.

- incurred charges amounting to \$17.8 million related to our estimate of claims associated with exposures to professional liability

exposure to the subprime mortgage developments in the United States. We have initially based these charges and our net reserves for losses to a significant degree on industry loss estimates of the total expected losses. Any adjustment to these charges will have an impact on the gain or loss on the sale of our interest at Lloyd's we expect to record in the first quarter of 2008 and may have a material impact on our results for the period.

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of 66.7% for the year ended December 31, 2007 as compared to 76.9% for the year ended December 31, 2006.

- had a net loss ratio

During the fourth quarter of 2007, charges of \$17.8 million in our Lloyd's segment's professional liability exposure to the subprime mortgage developments in the United States include the following:

- \$3.9 million of net reserves for reported claims. These claims were reported in Syndicate 4000's professional directors and officers ("D&O") and errors and omissions ("E&O") product lines.

- \$5.9 million of incurred but not reported reserves, net of reinsurance recoverable. Our estimate of IBNR is primarily based on publicly available industry loss estimates for D&O and E&O insurance combined with our estimate of the market share of Lloyd's in this market as well as our estimate of Syndicate 4000's market share in the Lloyd's professional products market.

- A premium deficiency reserve amounting to approximately \$8.0 million. This reserve relates to the write-off of deferred acquisition costs that are deemed irrecoverable from the future earning of unearned premium reserves because we expect that potential future subprime reported losses may exceed those unearned premium reserves.

Our Results

Our net income available to common shareholders was \$22.4 million for the year ended December 31, 2007 as compared to a net loss available to common shareholders of \$64.8 million for the year ended December 31, 2006. Our 2007 results were impacted by total net favorable loss development of \$39.1 million across all segments (including gains on commutation of a number of reinsurance policies of \$9.0 million), losses incurred in our Lloyd's segment related to our estimate of claims associated with exposures to subprime in certain professional lines of \$9.8 million (and the associated premium deficiency of \$8.0 million), a charge of \$4.7 million (including \$1.0 million of legal costs) in relation to the decision to rescind one of our non-traditional statutory surplus relief life reinsurance contracts, the gain on repurchase of junior subordinated debentures of \$4.4 million and the gain on repurchase of our Series A preferred shares of \$2.4 million. Our 2006 results were impacted primarily by the A.M. Best downgrade and our decision to engage in a self-managed run-off in all our business lines other than our Lloyd's business. As a result, we received significantly lower revenues from premiums earned and had significantly higher costs related to employee severance, professional, legal and advisory fees. Our 2006 results were also impacted to a lesser extent by adverse reserve developments on hurricanes Katrina, Rita and Wilma, the oil pipeline claim and other than temporary impairment charges on our invested assets.

In 2007, we generated approximately \$77.9 million of net premiums written, including \$96.4 million from Syndicate 4000, after premiums ceded on purchased reinsurance protection as compared to approximately \$80.6 million of net premiums written, after premiums ceded on purchased reinsurance protection in 2006. The reduction reflects the continuation of our self-managed run-off as well as the purchase of more additional reinsurance protection in 2007 than in 2006, and the return of premiums to our clients through policy cancellations and commutations of approximately \$24.9 million in 2007 and \$97.8 million in 2006 as we sought to reduce our loss exposures. These amounts were partially offset by an increase in the net premiums written by Syndicate 4000.

Similarly, our net premiums earned were \$87.2 million in 2007 as compared to \$225.3 million in 2006. Our net premiums earned were impacted by significantly lower premium writings and, to a lesser extent, by premium returns associated with policy cancellations. Subsequent to the sale of our interest in Syndicate 4000, we expect continued decreases in net premiums earned in future periods as we do not expect to underwrite new policies. The reductions in

premium revenues will likely have a material adverse effect on our future operating results, financial position and liquidity. Historically, net premiums earned have been our primary source of revenue. In 2006 net premiums

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earned contributed approximately 87% to our total revenues, and in 2007 this contribution reduced to 61%, and we expect further significant reductions in future periods.

In 2007, net revenues from non-underwriting activities, for example net investment income and technical services revenues, were not sufficient to offset general and administrative expenses, interest expense and depreciation and amortization. We expect that this trend may continue and that we may incur net losses in future periods. We seek to mitigate any losses through continued overhead reduction strategies.

Our general and administrative expenses in 2007 were \$59.9 million, including \$13.8 million of direct expenses related to our Lloyd's business. Our general and administrative expenses excluding those direct costs associated with our Lloyd's business were \$46.1 million in 2007 as compared to \$87.1 million in 2006. In the fourth quarter of 2007 our total general and administrative expenses were \$13.2 million compared to \$16.0 million in the same period in 2006, and our headcount has reduced to 47 as at December 31, 2007, compared to 81 on December 31, 2006. Our workforce is now allocated to the run-off of our existing business lines, finance, actuarial, general corporate and administrative functions and claims handling. During the years ended December 31, 2007 and 2006, we recorded severance costs of approximately \$0.3 million and \$14.3 million as a result of employee reductions following our decision to place our specialty insurance and reinsurance lines, other than Syndicate 4000, into run-off. This severance cost relates to the cost associated with those employees who have been provided notice and those who we expect to be terminating in the future and excludes those who we deem to be part of our run-off operation. We continue to seek to reduce our general and administrative expenses (including through further employee reductions) and expect, barring unforeseen circumstances that our 2008 general and administrative expenses will be lower than those incurred during 2007.

During 2007 we incurred professional, legal and consulting costs of \$16.3 million compared to \$22.5 million in 2006. During 2007 we incurred significant professional, legal and consulting costs in connection with the management of our Lloyd's business, engagement of third party run-off advisors to assist in certain projects related to our run-off, the restructuring of our Lloyd's business and costs associated with ongoing litigation.

Our investment portfolio generated net investment income of \$41.9 million during the year ended December 31, 2007, compared to \$45.9 million for the year ended December 31, 2006. This decrease is primarily attributable to a decrease in a lower level of invested assets. The lower level of invested assets is a result of the repurchases of our Series A preferred shares and of our junior subordinated debentures, our insurance and reinsurance business being in run-off, reduced cash inflows from premiums written and increased cash outflows associated with loss and loss expenses, commutations and overhead payments. Our average annualized effective yield (calculated by dividing net investment income by the average amortized cost of invested assets, net of amounts payable or receivable for investments purchased or sold) was approximately 4.7% for the year ended December 31, 2007 compared to 5.0% for the year ended December 31, 2006.

During the year ended December 31, 2004, we wrote a non-traditional statutory surplus relief life reinsurance contract that was deemed not to meet the risk transfer criteria set out in the accounting literature and was therefore accounted for as a deposit under the accounting rules. For additional information regarding accounting policies relating to non-traditional contracts, see "Critical Accounting Policies-Non-traditional contracts". Under this contract, we provided reinsurance on certain underlying life insurance contracts written by our client, a U.S. life insurance company. The client is subject to insurance regulation in the United States and, therefore, is required to maintain a certain amount of statutory capital. The client was entitled to reduce its statutory capital requirements as a result of entering into a reinsurance contract with us. The reinsurance transaction was done partially on a funds withheld basis under which some funds are held by the life insurance company. We received fees for this transaction. Other than receipt of our

fees, there were no net cash flows at inception of this contract, nor were there expected to be net cash flows other than fees through the life of the contract. We monitor this transaction on a quarterly basis to, among other things, ensure that the performance of the underlying life insurance

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policies is in line with the representations made by our client to us. During our monitoring process in 2007, it became apparent that this transaction was not performing as anticipated. We continue to obtain facts to evaluate and to analyze the performance of the life insurance policies that are underlying this transaction. We continue to evaluate the validity of data received from the client and the validity of risks ceded to us by our client as provided for by the terms of the reinsurance contract. On February 27, 2008, we exercised our right to cancel the contract ab initio, as we believe there have been material breaches of the contract as defined within the contract. As a result of this rescission notice, and in accordance with the cancellation provisions in the contract, at December 31, 2007 we recorded the return of all fee income, net of commissions, in the amount of \$3.7 million reflecting net fee income earned since inception of the contract. Included in contingencies on the consolidated balance sheet is an amount of \$2.5 million of fees due to be returned upon the rescission of this contract. In addition we have recorded an estimated \$1.0 million in legal costs that may be incurred in pursuing cancellation and any other legal remedies. We have provided approximately \$29.6 million of letters of credit and trust collateral in support of the amount of statutory surplus relief that the U.S. life insurance company has obtained. While the final outcome cannot be ascertained at this time, based on current facts and circumstances, knowledge of the data that has been received and our understanding of the original contract, we believe that the outcome could have a further material adverse effect on its financial position and results of operations in the future. We will continue to pursue any legal remedies against the insurance company that we believe are available and warranted under the circumstances.

Loss and Loss Expense Reserve Development

Our analysis of consolidated losses and loss expense development shown below presents the subsequent development of our estimated year end liability for net loss and loss expenses (net of loss and loss adjustment expenses recoverable) at the end of each balance sheet date for the years ended December 31, 2003 through 2007. The top line of the table shows our estimated net liability for unpaid losses and loss expense reserves recorded at the balance sheet date for each of the indicated periods. The net liability for loss and loss expenses represents the estimated aggregate amount of losses and loss expenses for claims arising from all prior years' accident periods that were unpaid at the balance sheet date.

The upper portion of the table shows our re-estimated amount of the previously recorded net liability as of the end of each succeeding calendar year. The estimate for our liability for loss and loss expense changes as more information becomes known about the frequency and severity of claims for individual years and, accordingly, as we update our actuarial techniques and selections of the appropriate method. The "Cumulative increase (decrease)" line represents the aggregate change in our estimates over all prior years. These increases or decreases in net liabilities generally arise either from net unfavorable or favorable loss development where the emergence of actual reported claims has been worse or better than expected or where we have cancelled or commuted policies. As described earlier, as our business has matured we have placed more reliance on the Bornhuetter-Ferguson actuarial methodologies which utilize our historical loss data in developing our estimate of ultimate loss liabilities.

The lower portion of the table presents the amounts paid as of subsequent periods on those claims for which we recorded reserves as of each balance sheet date. Conditions and trends that have affected development of the liabilities in the past are not indicative of events or development that may occur in the future. Accordingly, it is inappropriate to extrapolate future redundancies or deficiencies based on the tables below.

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Analysis of Consolidated Losses and Loss Expense Reserve Development
 Net of Reinsurance Recoverables

(U.S. dollars in thousands)		Years ended December 31		2003	2004	2005	2006	2007	Net loss and loss	
expense reserves	\$ 1,191	\$ 146,275	\$ 349,573	\$ 442,348	\$ 389,876	Liability re-estimated as of:				
	One year later	1,184	150,297	343,283	398,108	— Two years later		1,184		
148,555	310,286	—	—	Three years later	1,368	145,918	— — — Four years later		1,323	—
—	—	Cumulative increase (decrease)		132	(357)	(39,288)	(44,240)	— Cumulative paid losses		
	One year later	26	53,310	53,910	84,634	— Two years later		79	67,205	
111,895	—	—	Three years later	59	79,526	— — — Four years later		59	—	—

Overall, we have experienced net favorable loss developments as our estimates of ultimate loss liabilities have been adjusted to lower amounts than we had estimated when we were first required to record reserves. This is particularly noticeable in our shorter tail policies we underwrote or in lines of business where policies and periods of exposure have expired with either a fewer number of claims than expected or with lower than expected claim amounts. Prior to 2004 we did not have significant development in our estimation of loss and loss expense reserves since we started our operations in 2003 and only wrote a small number of contracts during that year.

During the year ended December 31, 2004 we recorded approximately \$61.3 million in net loss and loss expenses in our property and marine reinsurance product lines associated with hurricanes Charley, Frances, Ivan and Jeanne (the “2004 hurricanes”).

During the year ended December 31, 2005 we recorded:

- approximately \$83.3 million in net loss and loss expenses in our property and marine reinsurance and technical property and fidelity insurance product lines associated with the hurricanes Katrina, Rita and Wilma (the “2005 hurricanes”);

- approximately \$13.0 million in net loss and loss expenses associated with an oil pipeline claim in our environmental product line;

- an increase of \$5.9 million in loss estimates for the 2004 hurricanes as new information was reported to us by our clients; and

- \$1.9 million of net favorable loss development in certain of our other short-tail policies and product lines.

During the year ended December 31, 2006, we recorded a decrease in our loss reserves of \$6.3 million. The decreases from the 2004 and 2005 accident years were \$1.7 million and \$4.6 million and were primarily driven by the following:

- \$10.4 million of net favorable loss development in several of our product lines, including our fidelity, the property component of HBW, environmental and surety lines where actual loss experience in these product lines was better than expected for the 2005 accident year; and

- \$3.5 million of net favorable loss development as a result of transitioning our ultimate loss selection method in our professional insurance product line from the expected loss ratio method to the Bornhuetter-Ferguson method of which \$1.7 million related to

2004 and \$1.8 million related to 2005.

These net favorable developments of \$13.9 million were offset mainly by:

• a \$5.0 million increase in our loss estimates in relation to the 2005 hurricanes as new information was reported to us by our clients and others; and

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increase in our net loss reserves on the oil pipeline claim during 2006 as we were required by the relevant environmental agencies to extend our remediation activities.

- a \$2.6 million

During the year ended December 31, 2007, we recorded a decrease in our loss reserves of \$44.2 million. The decreases from the 2004, 2005 and 2006 accident years were \$2.6 million, \$30.4 million and \$11.2 million and were primarily driven by the following:

- \$14.9 million in several product lines related to mature accident periods in which aggregate loss experience was better than expected for the 2004, 2005 and 2006 accident years. This included approximately \$14.7 million in our professional liability and \$2.2 million in environmental product lines, offset by a small amount of additional reported losses in our other product lines;
- \$9.0 million related to the commutations of a number of our reinsurance policies relating to the 2005 and 2006 accident years;
- \$8.0 million recorded in our Lloyd's segment of which \$6.7 million related to 2005 and \$1.3 million related to 2006 accident year;
- \$5.8 million in relation to the 2005 hurricanes as new information was reported to us by our clients and others;
- \$5.1 million related to cancellations on policies, primarily in our HBW program, and the related reduction in reserves associated with those cancellations of which \$3.6 million related to the 2006 accident year and \$1.5 million related to the 2005 accident year;
- \$0.9 million related to the 2004 hurricanes; and
- \$0.5 million related to tornadoes that occurred in 2006.

Segment Information

Following the decision of our Board of Directors to place most of our business in run-off in 2006, we changed the composition of our reportable segments and renamed our specialty insurance segment and specialty reinsurance segment as specialty insurance run-off segment and specialty reinsurance run-off segment. We continue to earn premiums in our insurance and reinsurance run-off segments related to business written in prior periods and related to extensions and renewals of policies which we are legally required to write in business lines we have exited. The specialty insurance run-off and specialty reinsurance run-off segments, along with our Lloyd's and technical services segments, are more fully described as follows:

- Specialty insurance run-off. Our specialty insurance run-off segment includes the remaining policies written in our traditional, structured and program specialty insurance product line until the second quarter of 2006 and those policies that we were required by regulation to write in the remainder of 2006 and 2007. Our traditional specialty insurance products included technical risk property, professional liability, environmental liability, fidelity and crime, surety, trade credit and political risk and marine and aviation. These products were written both on a direct basis with insured clients or by reinsuring policies that were issued on our behalf by third-party insurers and reinsurers. Our specialty insurance programs include the HBW program.
- Specialty reinsurance run-off. Our specialty reinsurance run-off segment includes the remaining contracts written in our

traditional specialty reinsurance products line. Our specialty reinsurance products included property, casualty and marine and aviation products.

- Lloyd's. Syndicate 4000 at Lloyd's, our Lloyd's segment, was created in December 2004 and wrote traditional specialty insurance products including professional liability (professional indemnity and directors' and officers' coverage), fidelity and crime (financial institutions), specie and fine art and kidnap and ransom. For the 2007 underwriting year, we provided 90% of the capital of Syndicate 4000 as compared to all of the capital commitment from Syndicate 4000's inception through the 2006 underwriting year. The remaining 10% of Syndicate 4000's

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capital for the 2007 underwriting year was provided by Chaucer Holdings PLC. We included all of the results of insurance business written by Syndicate 4000 since its inception in 2004 through the 2006 underwriting year and 90% of the results of Syndicate 4000 for the 2007 underwriting year. Due to the sale of our interest in Syndicate 4000, this segment will be reclassified as discontinued operations in 2008.

- Technical services. Prior to the sale of ESC in the third quarter of 2006, our technical services segment provided diversified environmental investigation, remediation and engineering services, assessment services, other technical and information management services primarily in the environmental area in the U.S. Our technical services segment also provided technical and information management services to our specialty insurance run-off and reinsurance run-off segments. Following the sale of ESC, the technical services segment now consists of our two environmental liability assumption programs, QLT of Buffalo LLC and QLT of Alabama LLC. The results for the prior years have been reclassified to conform with the presentation of ESC in discontinued operations.

During 2006, we created a Lloyd's operating segment for the results of Syndicate 4000 which was previously aggregated with our specialty insurance run-off reportable segment. We believe it is no longer appropriate to aggregate Lloyd's and specialty insurance run-off operating segments given the different economic characteristics of the specialty insurance run-off segment that is no longer writing new or renewal business while our Lloyd's syndicate continued to write new and renewal business.

We refer to the specialty insurance run-off, specialty reinsurance run-off and Lloyd's segments as our underwriting segments. We refer to our environmental assumption programs as our technical services segment. We evaluate each segment based on its underwriting or technical services results, as applicable, including items of revenue and expense that are associated with, and directly related to, each segment.

During the fourth quarter of 2006 we ceased allocating our indirect corporate, general and administrative expenses to our operating segments. Prior to the fourth quarter of 2006, we allocated corporate general and administrative expenses to each segment based upon each product line's allocated capital for the relevant reporting period. We allocated capital to each of our product lines through the estimated value-at-risk method, which used statistical analyses of historical market trends and volatility to estimate the probable amounts of capital at risk for each reporting period. Since our decision to conduct a self-managed run-off of most of our businesses we no longer allocate capital to our segments and corporate expenses are no longer evaluated at the segment level. We also do not evaluate net investment income, and depreciation and amortization at the segment level.

The geographic locations in which we have conducted our business are the United States, Europe and Bermuda. The location of the risks that are the subject of our remaining insurance and reinsurance policies may be anywhere in the world.

Main Drivers of our Results

Revenues

We have derived the majority of our revenues from two principal sources: premiums from policies written by Syndicate 4000 at Lloyd's in our Lloyd's operating segment and investment income from our investment portfolios.

We record premiums written at the time that there is sufficient evidence of agreement to the significant terms of the contract but no earlier than the effective date of the policy. The amount of our insurance premiums written and earned depends on the number and type of policies we write, as well as prevailing market prices. Furthermore, the amount of

net premiums earned depends upon the type of contracts we have written, the contractual periods of the contracts we write, policy cancellations and commutations, the inception date of the contracts, the expired portions of the

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contract periods and the type of purchased reinsurance protection. Because of all these factors, the amount of premiums written and ceded may not result in a correlative level of profitability.

Our investment income depends on the average invested assets in our investment portfolios and the yield that we earn on those invested assets. Our investment yield is a function of market interest rates and the credit quality and maturity period of our invested assets. Our investment portfolio consists principally of fixed income securities, short-term investments, cash, and cash equivalents. In addition, we realize capital gains or losses on sales of investments as a result of changing market conditions, including changes in market interest rates and changes in the credit quality of our invested assets. We also recognize capital gains and losses on investments as a result of fluctuations in the fair market values of the investments. The objective of our current investment strategy is to preserve investment principal, maintain liquidity and manage duration risk between investment assets and insurance liabilities (when they become due, at the time of either loss settlement, cancellations or commutations), while maximizing investment returns through a diversified portfolio.

Expenses

Our expenses primarily consist of general and administrative expenses, net loss and loss expenses and acquisition expenses.

General and administrative expenses consist primarily of personnel related expenses (including severance costs), professional fees and other operating overheads. From time to time we engage administrative service providers and legal, accounting, tax and financial advisors. These general and administrative expenses may be incurred directly by a segment or indirectly at the corporate level.

Net loss and loss expenses, which are net of loss and loss expenses recovered under our ceded reinsurance contracts, depend on the number and type of insurance and reinsurance contracts we write and reflect our best estimate of ultimate losses and loss expenses we expect to incur on each contract written using various actuarial analyses. Actual losses and loss expenses will depend on either actual costs to settle insurance and reinsurance claims, or the estimated loss amount that we may agree with our policyholders under the terms of commutation and cancellation arrangements. Our ability to accurately estimate expected ultimate loss and loss expense at the time of pricing each insurance and reinsurance contract and the occurrence of unexpected high loss severity catastrophe events are critical factors in determining our profitability.

Acquisition expenses, which are net of expenses recovered under our ceded reinsurance contracts, consist principally of commissions, fees, brokerage and tax expenses that are directly related to obtaining and writing insurance and reinsurance contracts. Typically, acquisition expenses are based on a certain percentage of the premiums written on contracts of insurance and reinsurance and may be adjustable based upon loss experience. These expenses are a function of the number and type of insurance and reinsurance contracts written. We may not be able to recover all or a portion of our acquisition costs on commuted or cancelled policies. A premium deficiency reserve is recognized if the sum of expected losses and loss expenses and unamortized acquisition costs exceeds related unearned premiums. A premium deficiency reserve is recognized by charging unamortized acquisition costs to acquisition expenses in the consolidated statement of operations to the extent required in order to eliminate the deficiency. If the premium deficiency reserve exceeds unamortized acquisition costs then a liability is accrued for the excess deficiency.

Financial Ratios

The financial ratios we use in our Lloyd's segment include the net loss and loss expense ratio, the acquisition expense ratio and the general and administrative expense ratio. Our net loss and loss expense ratio is calculated as net losses and loss expenses incurred divided by net premiums earned. Our acquisition expense ratio is calculated by dividing acquisition expenses by net premiums earned. Our general and administrative expense ratio is calculated by dividing general and administrative expenses by net premiums earned. Our financial ratios provide a measure of the current profitability of the earned portions of insurance contracts that were written in our Lloyd's

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segment. In this report we only present financial ratios related to our Lloyd's segment as our specialty insurance and reinsurance segments are in run-off.

Results of Operations

Our specialty insurance and reinsurance run-off segments are both in run-off. A comparison between our results for the year ended December 31, 2007 and 2006 highlights the differences between running-off our business, which includes, among other things, returning premium upon contract commutations and cancellations, on the one hand, during the year ended December 31, 2007 and writing and earning premium on the other hand in the beginning of the year ended December 31, 2006 before our A.M. Best rating downgrading in March 2006. As a result, a comparison of our results of these periods may not be a meaningful means of analyzing our results of operations.

Years ended December 31, 2007 compared to December 31, 2006

Results of operations for the years ended December 31, 2007 and 2006 were as follows:

2007	2006	(\$ in thousands)	Revenues	Gross premiums written	\$ 106,587	\$ 158,729	Premiums ceded	(28,645)	(78,175)	Net premiums written	77,942	80,554	Change in unearned premium	9,305
144,745	Net premiums earned	87,247	225,299	Technical services revenues	1,707	3,331	Net investment income	41,900	45,934	Net gains (losses) on investments	5,818	(15,945)	Net foreign exchange gains (losses)	850
(3,790)	Gain on repurchase of junior subordinated debentures	4,421	—	Other income	447	3,654	Total revenues	142,390	258,483	Expenses	Net losses and loss expenses			
31,077	156,121	Acquisition expenses	26,728	42,540	General and administrative expenses	59,866	100,006	Interest expense	3,632	5,458	Depreciation and amortization of intangible assets	1,024	4,999	
Total expenses	122,327	309,124	Income (loss) from continuing operations before income taxes	20,063	(50,641)	Income tax expense	12	14	Net income (loss) from continuing operations	20,051	(50,655)	Discontinued operations:	Loss from operations of discontinued operations	—
(12,953)	Income on disposal of discontinued operations	—	704	Net loss from discontinued operations	—	(12,249)	Net income (loss)	20,051	(62,904)	Gain on repurchase of Series A preferred shares	2,364	—	Dividends on preferred shares	—
(1,916)	Net income (loss) to common shareholders	\$ 22,415	\$ (64,820)	Revenues										

Substantially all of our revenues were generated by our underwriting subsidiaries in the U.S., Bermuda and Europe.

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Premiums. Gross premiums written were \$106.6 million for the year ended December 31, 2007, a decrease of \$52.1 million, compared to \$158.7 million for the year ended December 31, 2006. The decrease in our gross premiums written reflects the decision to discontinue writing new business in our insurance and reinsurance lines of business, other than in our Lloyd's segment and the effect of premium returns to our clients when policies are cancelled.

Our Lloyd's segment contributed \$124.0 million of total gross written premiums in 2007, compared to \$91.8 million in 2006. We believe this increase is due to the enhanced ability of Syndicate 4000 to attract new and secure renewal business during the year because of the provision of third party capital to the syndicate, the establishment of the Pembroke Managing Agency and the fact that Syndicate 4000, in its third year, benefited from increased market recognition.

Premiums ceded were \$28.6 million for the year ended December 31, 2007, a decrease of \$49.6 million, compared to \$78.2 million for the year ended December 31, 2006. The decrease in premiums ceded primarily reflects the reduction in gross premiums written.

Net premiums earned were \$87.2 million for the year ended December 31, 2007, a decrease of \$138.1 million, compared to \$225.3 million for the year ended December 31, 2006. The decrease in net premiums earned reflects the decision to discontinue writing new business in our insurance and reinsurance lines of business, other than in our Lloyd's segment, and the continued return of premiums to our clients following policy commutations or cancellations. Our net premiums written are typically earned over the risk periods of the underlying insurance policies which are generally twelve months. Net premiums written that are not yet earned and are deferred as unearned premium reserves, net of deferred reinsurance premiums, totaled \$75.6 million at December 31, 2007 and will be earned and recognized in our results of operations in future periods to the extent these premiums are not returned following future commutations or cancellations. The contribution to net premiums earned from our Lloyd's segment is detailed under "Results by Segments" below.

Technical services revenues. Technical services revenues were \$1.7 million for the year ended December 31, 2007, a decrease of \$1.6 million, compared to \$3.3 million for the year ended December 31, 2006. We expect that our technical services revenues will decrease in future periods as the remediation activities near completion. Technical services revenues prior to the quarter ended September 30, 2006 were derived from the operations of ESC which was sold on September 16, 2006 and from the operations of our environmental liability assumption programs. This revenue is included in the results of our discontinued operations.

Net investment income and net gains (losses) on investments. Net investment income and net gains (losses) on investments consisted of the following for the years ended December 31, 2007 and 2006:

	2006	2007
Net investment income	\$ 41,900	\$ 45,934
Net realized gains (losses) on investments	2,794	(15,945)
Net change in the fair market value of trading investments	29,989	3,024
		\$ 47,718

Net investment income was \$41.9 million for the year ended December 31, 2007 a decrease of \$4.0 million, compared to \$45.9 million for the year ended December 31, 2006. This decrease was primarily due to a decrease in interest earned on fixed maturity and short term investments plus amortization of discounts on fixed maturity investments. Net investment income decreased in the year ended December 31, 2007 as compared to 2006 due to a lower level of

invested assets at December 31, 2007 compared to December 31, 2006. The lower level of invested assets is a result of our insurance and reinsurance businesses being in run-off as well as the repurchase of our Series A preferred shares and junior subordinated debentures. Our average annualized effective yield (calculated by dividing net investment income by the average amortized cost of invested assets, net

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of amounts payable or receivable for investments purchased or sold) was approximately 4.7% for the year ended December 31, 2007 compared to 5.0% for the year ended December 31, 2006. This decrease is due to shortening of the duration of some of our invested assets during 2007 as compared to 2006 and the resulting lowering of the yield on those invested assets.

Net realized losses for the year ended December 31, 2006 of \$15.9 million were generated primarily from an other than temporary impairment charge of \$16.9 million.

On January 1, 2007 we converted our available-for-sale portfolio to trading as permitted under the early adoption rules of SFAS 159. This resulted in all changes in the fair market value of investments during the year ended December 31, 2007 being recorded as net gains or losses within our statement of operations. During the year ended December 31, 2006 any change in the fair market value of investments were reflected within other comprehensive income within the equity section of the balance sheet unless any securities were deemed to be other than temporarily impaired in which case unrealized losses were recognized as a realized loss in the statement of operations. Other comprehensive income for the year ended December 31, 2006 included \$9.7 million of net change in unrealized losses.

Net foreign exchange losses. Net foreign exchange gains were \$0.9 million for the year ended December 31, 2007 compared to a loss of \$3.8 million for the year ended December 31, 2006. The net foreign exchange gains and losses were driven primarily by our Lloyd's segment and the relationship between the U.S. Dollar and the British Pound. Due to the sale of our interest in Syndicate 4000, we expect that our exposure to foreign currency movements will be significantly reduced in 2008.

Gain on repurchase of junior subordinated debentures. During the year ended December 31, 2007, we repurchased all of our junior subordinated debentures for an aggregate purchase price of \$54.5 million. We originally issued and sold \$60.0 million of the junior subordinated debentures in private placements. A gain on repurchase of \$4.4 million was recognized, net of repurchase costs of \$0.5 million and write off of original deferred issuance costs of \$1.7 million.

Other income. Other income was \$0.4 million for the year ended December 31, 2007 compared to \$3.7 million for the year ended December 31, 2006. The decrease in other income is due to the return of fee income as a result of our decision to cancel one of our non-traditional statutory surplus relief life reinsurance contracts as described more fully in "Our results" above. At December 31, 2007 we have recorded the return of all fee income, net of commissions, in the amount of \$3.7 million reflecting net fee income earned since inception of the contract.

Expenses

Net losses and loss expenses. Net losses and loss expenses were \$31.1 million for the year ended December 31, 2007, a decrease of \$125.0 million, compared to \$156.1 million for the year ended December 31, 2006. Net losses and loss expenses are a function of our net premiums earned and changes in our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance and reinsurance underwritten. The decrease in net losses and loss expenses is due to:

- the reduced number of insurance contracts we entered into in 2007 as compared to the number of insurance and reinsurance contracts we entered into in 2006 and the associated net premiums earned as our insurance and reinsurance portfolios continue to run-off;

experience in mature accident periods in certain of our product lines; and

- favorable loss

experience arising on commutation of certain assumed reinsurance contracts.

- favorable loss

This decrease was partially offset by net losses incurred in our Lloyd's segment of \$9.8 million related to Syndicate 4000's professional liability exposure to the subprime mortgage developments in the United States.

Our expected ultimate losses and loss expenses during the year ended December 31, 2007, included total net favorable loss development (including those arising from commutations) related

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to prior year accident periods of \$39.1 million. This was comprised of \$14.9 million in several product lines related to mature accident periods in which actual loss experience was better than expected, \$9.0 million relating to the commutations of a number of our reinsurance policies, \$8.0 million in our Lloyd's segment particularly in relation to the 2005 underwriting year, \$6.7 million related to the 2005 and 2004 hurricanes and \$0.5 million related to the tornadoes that occurred in the first quarter of 2006. We expect future developments in the loss and loss expenses of our product lines as we continue to receive information related to our loss and loss expense reserves and as those reserves develop over time. We continue to be exposed to potentially significant losses in lines of business where claims may not be reported for some period of time after those claims are incurred. We also recorded a reduction in our losses and loss expense reserves of \$5.1 million as a result of cancellations on policies primarily in our HBW program and the related reduction in reserves associated with those cancellations.

In estimating reserves we may utilize a variety of standard actuarial methods in line with industry practice, including the expected loss ratio method, the Bornhuetter-Ferguson method, paid loss development method and reported loss development method. The loss reserves are based on the loss development characteristics of the specific line of business and specific contracts within that line of business, and consider coverage, type of business, maturity of loss data and claims.

Our total net loss ratio (calculated by dividing net losses and loss expenses by net premiums earned) was 35.6% for the year ended December 31, 2007, a decrease of 33.7% compared to a total net loss ratio of 69.3% for the year ended December 31, 2006. The decrease in the total net loss and loss expense ratio is due to the significant favorable development recognized in our insurance and reinsurance run-off segments and the commutation of several assumed reinsurance contracts.

Acquisition expenses. Acquisition expenses were \$26.7 million for the year ended December 31, 2007, a decrease of \$15.8 million, compared to \$42.5 million for the year ended December 31, 2006. The decrease in acquisition expenses is due to the decrease in net premiums earned and the number of insurance contracts we entered into in 2007 as compared to the number of insurance and reinsurance contract we entered into in 2006.

Within acquisition costs for the year ended December 31, 2007 we have recorded a premium deficiency reserve of approximately \$8.0 million. This premium deficiency reserve relates to the write-off of deferred acquisition costs in our Lloyd's segment that are deemed irrecoverable from the future earning of unearned premium reserves because we expect that potential future subprime reported losses may exceed those unearned premium reserves.

General and administrative expenses. General and administrative expenses were \$59.9 million for the year ended December 31, 2007, a decrease of \$40.1 million, compared to \$100.0 million for the year ended December 31, 2006. General and administrative expenses were comprised of \$28.2 million of personnel related expenses (including \$0.3 million of severance costs), \$16.3 million of professional fees (which includes Lloyd's managing agency fees, legal fees, audit fees, consulting and actuarial) and \$15.4 million of other expenses during the year ended December 31, 2007 compared to \$55.2 million of personnel related expenses (including \$14.3 million of severance costs) and, \$22.6 million of professional fees and \$22.2 million of other expenses during the year ended December 31, 2006. The decrease in general and administrative expenses is due to the cost saving measures taken in response to the decision to cease writing new business in 2006, including the reduction of workforce headcount that was 47 as of December 31, 2007 compared to 81 as of December 31, 2006.

Interest expense. Interest expense was \$3.6 million for the year ended December 31, 2007, a decrease of \$1.9 million compared to \$5.5 million for the year ended December 31, 2006. Interest expense for the year ended December 31, 2007 consists of incurred interest on our junior subordinated debentures. Due to the repurchase of the

junior subordinated debentures in the third quarter of 2007, we did not incur a full year of interest in 2007 as compared to 2006 when we recorded incurred interest for the entire year.

Depreciation and amortization of intangible assets. Depreciation and amortization of intangible assets was \$1.0 million for the year ended December 31, 2007, a decrease of \$4.0 million compared

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to \$5.0 million for the year ended December 31, 2006. The majority of the decrease relates to the following three items. Firstly, an impairment charge of \$1.7 million with respect to our intangible assets associated with our U.S. insurance licenses was made in 2006 to record these licenses at their estimated net realizable value and secondly, amortized \$0.4 million in the year ended December 31, 2007 related to software costs compared to \$1.2 million for the year ended December 31, 2006. Finally, we also amortized approximately \$0.8 million of leasehold improvements during the fourth quarter of 2006 associated with our anticipated relocation of our New York operations. The remaining decrease is due to the decreasing value of our fixed assets.

We have recorded a net deferred income tax benefit of \$5.3 million related to tax operating losses generated in our Lloyd's segment for the year ended December 31, 2007. For the year ended December 31, 2007, the net valuation allowance increased by approximately \$1.8 million, to \$50.9 million.

The realization of deferred tax assets is dependent on future taxable income and future reversals of existing taxable temporary differences. Based upon our assessment of historical data and future earnings, it is our belief that it is more likely than not that the \$5.3 million net deferred tax asset established for the U.K. NOL carryforwards will be realized in future periods by Quanta 4000. We will continue to periodically assess the realizability of the net deferred tax asset and adjust the valuation allowance accordingly.

In relation to the U.S. NOL and Irish NOL, due to prior and existing operating losses, we believe that it is more likely than not that the deferred tax asset will not be realized. Accordingly, we have recorded a full valuation allowance against these net deferred tax assets as of December 31, 2007 and 2006.

Discontinued operations.

(Loss) from operations of discontinued operations. We had no income from discontinued operations for the year ended December 31, 2007. For the period from January 1, 2006 to September 15, 2006, the loss from discontinued operations represented the revenues and expenses from ESC, which was sold on September 15, 2006.

During the period from January 1, 2006 to September 15, 2006, our loss from operations of discontinued operations generated by ESC, previously included in the technical services segment, now reported in discontinued operations was as follows:

Period from				
January 1,				
2006 to				
September 15,				
2006	(\$ in thousands)	Technical services revenues	\$ 21,954	Other income
		14	Direct technical services costs	(13,968)
		General and administrative expenses	(7,725)	Loss on impairment of goodwill
				(12,561)
		Depreciation of fixed assets and amortization of intangible assets	(647)	Income tax expense
				(20)
		Loss from operations of discontinued operations	\$ (12,953)	

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Income on disposal of discontinued operations. Income on disposal of discontinued operations was \$0.7 million for the year ended December 31, 2006. This income is presented in the Consolidated Statement of Operations as Income on disposal of discontinued operations, a component of discontinued operations. The components of this income are summarized below.

						(\$ in thousands)	
from WSP(1)	\$ 11,484	Debt forgiveness	1,000	Total consideration	12,484	Less:	Cash proceeds
ESC(2)	(11,140)	Estimated transaction costs(3)	(640)	Income on disposal of ESC	\$ 704		Carrying value of

disposition include post closing adjustments. (1) Total proceeds from

September 15, 2006, prior to the impact of the sale transaction. (2) Net assets of ESC at

include advisory fees directly associated with the sale. (3) Transaction costs

Preferred Shares

Gain on repurchase of preferred shares. During the year ended December 31, 2007, we repurchased all of our Series A preferred shares at a price of \$22.50 per share. The aggregate purchase price for the Series A preferred shares was \$70.4 million which resulted in a gain of \$2.4 million, net of repurchase costs of \$2.2 million and write off of original deferred issuance costs of \$3.3 million, increasing net income to common shareholders.

Dividends on preferred shares. During the year ended December 31, 2007, we paid no dividend on our Series A preferred shares. During the year ended December 31, 2006, we paid a dividend of \$1.9 million to our Series A preferred shareholders.

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Premiums ceded were \$78.2 million for the year ended December 31, 2006 a decrease of \$140.8 million, or 64.3% compared to \$218.9 million for the year ended December 31, 2005. The decrease in premiums ceded primarily reflects the reduction in gross premiums written.

Net premiums earned were \$225.3 million for the year ended December 31, 2006, a decrease of \$138.8 million, or 38.9%, compared to \$364.1 million for the year ended December 31, 2005. The decrease in net premiums earned reflects the decision to discontinue writing new business in our insurance and reinsurance lines of business, other than in our Lloyd's segment. Our net premiums written are typically earned over the risk periods of the underlying insurance policies. Net premiums written that are not yet earned and are deferred as unearned premium reserves, net of deferred reinsurance premiums, totaled \$119.2 million at December 31, 2006 and will be earned and recognized in our results of operations in future periods. The contribution to net premiums earned from our Lloyd's segment is detailed under "Results by Segments" below.

Technical services revenues. Technical services revenues were \$3.3 million for the year ended December 31, 2006 a decrease of \$15.7 million compared to \$19.0 million for the year ended December 31, 2005. The decrease is due to a significant portion of remediation of our QLT Buffalo LLC environmental liability assumption program occurring during the second and third quarters of 2005. The remediation was close to being completed and, as a result, did not generate technical services revenues in 2006 to the same extent as it did in 2005.

Net investment income and net losses on investments. Net investment income and net realized losses totaled \$30.0 million for the year ended December 31, 2006, an increase of \$15.8 million compared to \$14.2 million for the year ended December 31, 2005. The amounts consisted of the following:

	2006	2005	(\$ in thousands)
Net investment income	\$ 45,934	\$ 27,181	
Net realized losses on investments	(15,945)	(13,020)	
Net change in the fair market value of trading investments	\$ 29,989	\$ 14,161	

The increase is primarily due to an increase in net investment income of \$18.7 million because of our larger amount of invested assets and rises in market interest rates, which is partially offset by an increase in net realized losses of \$2.9 million, of which \$16.9 million is attributable to other than temporary impairment losses recognized during the year ended December 31, 2006, compared to other than temporary losses of \$10.2 million in 2005.

Net investment income was \$45.9 million for the year ended December 31, 2006 an increase of \$18.7 million, or 68.8% compared to \$27.2 million for the year ended December 31, 2005. This was derived primarily from interest earned on fixed maturity and short term investments plus amortization of discounts on fixed maturity investments, partially offset by investment management fees. Our average annualized effective yield (calculated by dividing net investment income by the average amortized cost of invested assets, net of amounts payable or receivable for investments purchased or sold) was approximately 5.0% for the year ended December 31, 2006 compared to 3.5% for the year ended December 31, 2005, reflecting rises in market interest rates. Net realized losses of \$15.9 million were generated primarily from our other than temporary impairment charge of \$16.9 million.

As of December 31, 2006, the average duration of our investment portfolio was approximately 2.5 years with an average credit rating of approximately "AA+", compared to 2.6 years with an average credit rating of approximately "AA+" as at December 31, 2005.

Net foreign exchange losses. Net foreign exchange losses were \$3.8 million for the year ended December 31, 2006 compared to net foreign exchange gains of \$0.3 million in 2005. The increase in net foreign exchange losses was due to an increase in foreign currency assets, liabilities, particularly in Syndicate 4000 combined with a weakening US dollar during 2006 against those foreign currencies.

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Expenses

Net losses and loss expenses. Net losses and loss expenses were \$156.1 million for the year ended December 31, 2006, a decrease of \$168.1 million, or 51.9%, compared to \$324.2 million for the year ended December 31, 2005. Net losses and loss expenses are a function of our net premiums earned and changes in our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance and reinsurance underwritten. The decrease in net losses and loss expenses is due to:

- the reduced number of insurance and reinsurance contracts we entered into and the associated net premiums earned as our insurance and reinsurance portfolios begin to run-off;
- the lack of natural catastrophe events reported during 2006 to which our in-force contracts may be exposed;
- favorable loss experience in mature accident periods in certain of our product lines; and
- several commutations of assumed reinsurance contracts.

Our expected ultimate losses during the year ended December 31, 2006 included adverse development of approximately \$5.0 million related to the 2005 hurricanes and additional net losses of \$2.6 million related to damage caused by an oil pipeline in California which ruptured during a mudslide in the first quarter of 2005, for which the damage is covered by an insurance contract issued by our environmental liability product line. This development in 2006 was primarily related to extended remediation activities required by the relevant environmental agencies.

Our total net loss ratio (calculated by dividing net losses and loss expenses by net premiums earned) was 69.3% for the year ended December 31, 2006, a decrease of 19.8% compared to a total net loss ratio of 89.1% for the year ended December 31, 2005. The decrease in the total net loss and loss expense ratio is due primarily to the hurricanes and the oil pipeline loss that occurred in 2005.

Acquisition expenses. Acquisition expenses were \$42.5 million for the year ended December 31, 2006, a decrease of \$27.1 million, or 38.9%, compared to \$69.6 million for the year ended December 31, 2005. The decrease in acquisition expenses is due to the decrease in the number of insurance and reinsurance contracts we entered into and the associated net premiums earned.

Our acquisition expense ratio for the year ended December 31, 2006 was 18.9%, which is comparable to our acquisition expense ratio of 19.1% for the year ended December 31, 2005. Deferred acquisition costs include, as of December 31, 2006, \$12.1 million of acquisition expenses on written contracts of insurance and reinsurance.

General and administrative expenses. General and administrative expenses were \$100.0 million for the year ended December 31, 2006, a decrease of \$9.6 million, or 8.8%, compared to \$109.6 million for the year ended December 31, 2005. General and administrative expenses were comprised of \$55.2 million of personnel related expenses (including \$14.3 million of severance costs) and \$44.8 million of other expenses during the year ended December 31, 2006 compared to \$52.4 million of personnel related expenses (including \$6.4 million of severance costs) and \$57.2 million of other expenses during the year ended December 31, 2005. The decrease in general and administrative expenses is due to the cost saving measures taken in response to the decision to cease writing new business in 2006 but were mitigated by increased severance costs and to a lesser extent, the increased fees associated with ongoing efforts relating to Sarbanes-Oxley Section 404 compliance and costs relating to information technology

development.

Interest expense. Interest expense was \$5.5 million for the year ended December 31, 2006, an increase of \$1.3 million compared to \$4.2 million for the year ended December 31, 2005 and relates to the increase in interest rates during 2006 leading to a higher interest charge on the junior subordinated debentures.

Depreciation and amortization of intangible assets. Depreciation and amortization of intangible assets was \$5.0 million for the year ended December 31, 2006, an increase of \$2.0 million compared to \$3.0 million for the year ended December 31, 2005. The majority of the increase relates to an

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impairment charge of \$1.7 million with respect to our intangible assets associated with our U.S. insurance licenses. At December 31, 2006, the carrying value of these licenses approximates their estimated net realizable value.

We have not recorded any net deferred income tax benefits or assets relating to tax operating losses generated by our subsidiaries since our results of operations include a 100% valuation allowance against net deferred tax assets. For the year ended December 31, 2006, the net valuation allowance increased by approximately \$24.4 million, to \$49.1 million.

Discontinued operations.

(Loss) income from operations of discontinued operations. The loss from discontinued operations was \$13.0 million for the period from January 1, 2006 to September 15, 2006, compared to income of \$3.7 million for the year ended December 31, 2005 and consisted of revenues and expenses from ESC, which was sold on September 15, 2006.

ESC's (Loss) income from operations, previously included in the technical services segment, for the period from January 1, 2006 to September 15, 2006, and the year ended December 31, 2005, now reported in discontinued operations, are as follows:

	Period from	
	January 1, 2006 to September 15, 2006	For the year ended December 31, 2005
Technical services revenues	\$ 21,954	\$ 50,752
Other income	14	165
Direct technical services costs	(13,968)	(37,027)
General and administrative expenses	(7,725)	(9,129)
Loss on impairment of goodwill	(12,561)	—
Depreciation of fixed assets and amortization of intangible assets	(647)	(988)
Income tax expense	(20)	(12)
(Loss) income from operations of discontinued operations.	\$ (12,953)	\$ 3,761

ESC's technical services revenues include the inter-company revenues charged by ESC to the QLT's and to our underwriting segment.

Technical services revenues. Technical services revenues were \$22.0 million for the period ended December 31, 2006 compared to \$50.8 million for year ended December 31, 2005. The decrease was mainly due to ESC generating significant inter-company revenue for the remediation of the sites of QLT Buffalo, LLC during the second and third quarter of 2005 as compared to the period from January 1, 2006 to September 15, 2006 when there was much less remediation activity. The decrease was also due to our exit from the environmental insurance business.

Direct technical services costs. Direct technical services costs were \$14.0 million for the period ended December 31, 2006, compared to \$37.0 million for the year ended December 31, 2005, and were comprised of subcontractor and direct labor expenses. Direct technical services costs, as a percentage of technical services revenues were approximately 63.6% for the year ended December 31, 2006 compared to 73.0% for the year ended December 31, 2005.

General and administrative expenses. General and administrative expenses were \$7.7 million for the period ended December 31, 2006, compared to \$9.1 million for the year ended December 31, 2005 and consisted primarily of personnel related expenses.

Loss on impairment of goodwill. Loss on impairment of goodwill was \$12.6 million for the period ended December 31, 2006 and relates to our determination that the carrying value of its previously carried goodwill asset related to ESC was impaired during the second quarter of 2006.

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Syndicate 4000 plus all of the results of prior underwriting year activities. The results reported for the year ended December 31, 2006 comprise all of the activities of Syndicate 4000 during that period.

Technical services

Following the sale of ESC in the third quarter of 2006, the technical services segment is composed of our two environmental liability assumption programs. The results for the year ended December 31, 2006 have been reclassified to conform to the presentation of ESC in discontinued operations.

The following is a discussion of our net underwriting results and profitability measures by segment for the years ended December 31, 2007, 2006 and 2005.

Years ended December 31, 2007 and 2006

Specialty insurance run-off

The following table shows the results of the specialty insurance run-off segment for the years ended December 31, 2007 and 2006:

2007	2006	Change	(\$ in thousands)	Gross premiums written	\$ (20,904)	\$ 60,107	\$ (81,011)
Premiums ceded	3,487	(34,126)	37,613	Net premiums written	\$ (17,417)	\$ 25,981	\$ (43,398)
Net premiums earned	\$ 6,127	\$ 113,289	\$ (107,162)	Other income	(2,155)	2,873	(5,028)
Net losses and loss Expenses	16,621	(65,706)	82,327	Acquisition expenses	(441)	(18,029)	17,588
General and administrative expenses	(7,369)	(18,440)	11,071	Segment income	\$ 12,783	\$ 13,987	\$ (1,204)

Premiums. Gross and net premiums written were negative \$20.9 million and \$17.4 million for the year ended December 31, 2007 compared to \$60.1 million and \$26.0 million for the year ended December 31, 2006. The significant decrease in our specialty insurance run-off segment's gross and net premiums written was due to the decision to cease writing new business in 2006, our decision to run-off the majority of our businesses and the effect of premium returns to our clients on policy cancellations and the transfer of policies to third parties.

For the year ended December 31, 2007 we returned or transferred approximately \$23.3 million of gross written premiums, compared to \$58.7 million for the year ended December 31, 2006.

Our technical risk property (primarily the HBW program), environmental liability and other product lines returned premium of \$12.5 million, \$8.5 million and \$2.3 million, for the year ended December 31, 2007.

We ceased to write the HBW program in our technical risk property product line under the terms of the managing agency agreement which expired on December 2, 2006. This program accounted for the substantial majority of total specialty insurance run-off segment gross and net premiums written in the year ended December 31, 2006. The policies in our HBW program were underwritten by a third-party agent which was instructed to follow our underwriting guidelines.

Premiums ceded. Premiums ceded were negative \$3.5 million during the year ended December 31, 2007, a decrease of \$37.6 million, compared to \$34.1 million for the year ended December 31, 2006, reflecting the impact of policy cancellations and transfers and the associated premium returns collected from our reinsurers.

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Net premiums earned. Net premiums earned during the year ended December 31, 2007 were \$6.1 million, a decrease of \$107.2 million, compared to \$113.3 million for the year ended December 31, 2006, representing the reductions of premiums written and the return of premiums to our clients. Gross premiums written and ceded premiums are earned over the period of each insured risk. The terms of our insurance contracts range from between one and ten years with the majority of our contracts being for a one year period.

Other income (expense). Other expense was \$2.2 million for the year ended December 31, 2007, compared to other income of \$2.9 million for the year ended December 31, 2006 and relates to income, including fees, recognized on non-traditional insurance contracts. The decrease in other income is due to the recording of the return of all fee income earned to date as a result of our decision to cancel one of our non-traditional statutory surplus relief life reinsurance contracts as discussed in more detail in "Our results" above. At December 31, 2007 we have recorded the return of all fee income, net of commissions, in the amount of \$3.7 million reflecting net fee income earned since inception of the contract, which will become payable upon the effectiveness of the rescission, if at all.

Net losses and loss expenses. Net losses and loss expenses had a favorable impact of \$16.6 million for the year ended December 31, 2007 compared to an expense of \$65.7 million for the year ended December 31, 2006. Net losses and loss expenses are a function of our net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance and reinsurance underwritten. The decrease in net losses and loss expenses is due largely to the net favorable loss development in maturing accident periods in several of our product lines, the reduction of losses as a result of the cancellation of policies, particularly in our HBW program, and the substantial decline in the number of insurance contracts we entered into and the associated net premiums earned. We continue to participate in lines of business where claims may not be reported for some period of time after those claims are incurred.

Acquisition expenses. Acquisition expenses were \$0.4 million for the year ended December 31, 2007 compared to \$18.0 million for the year ended December 31, 2006. The decrease in acquisition expenses was due to the substantial decline in the number of insurance contracts we entered into and the associated net premiums earned. These acquisition expenses primarily represented brokerage fees, commission fees and premium tax expenses and were net of ceding commissions earned on purchased reinsurance treaties.

Specialty reinsurance run-off

The following table shows the results of the specialty reinsurance run-off segment for the years ended December 31, 2007 and 2006:

2007	2006	Change	(\$ in thousands)	Gross assumed premiums written	\$ 3,442	\$ 6,864	\$(3,422)
Premiums ceded	(4,478)	(14,035)	9,557	Net premiums written	\$ (1,036)	\$ (7,171)	\$ 6,135
Net premiums earned	\$ 336	\$ 46,487	\$(46,151)	Other income	2,602	781	1,821
expenses	6,147	(40,033)	46,180	Acquisition expenses	1,100	(12,468)	13,568
administrative Expenses	(1,357)	(6,420)	5,063	Segment income (loss)	\$ 8,828	\$ (11,653)	\$ 20,481

Premiums. Gross and net premiums written were \$3.4 million and \$(1.0) million for the year ended December 31, 2007 compared to \$6.8 million and \$(7.2) million of gross and net premiums written for the year ended December 31, 2006. The decrease in our specialty reinsurance run-off

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segment's gross premiums written reflects the decrease in our reinsurance business lines as a result of our decision to discontinue the writing of new and renewal business in our reinsurance business line, combined with changes in estimates in written premiums, return premiums and contract commutations. Ceded written premiums in 2006 were greater than gross premiums written because of the purchase of additional reinsurance protection for exposures in our marine, technical risk and aviation product line.

Gross written premiums in our specialty reinsurance run-off segment of \$3.4 million for the year ended December 31, 2007 consisted primarily of \$4.8 million in premium estimates, partially offset by the impact of the policy commutations in the amount of \$1.4 million.

Premiums ceded Premiums ceded were \$4.5 million during the year ended December 31, 2007 compared to \$14.0 million for the year ended December 31, 2006. The decrease in our ceded premiums written largely reflects the decrease in gross premiums written. We also purchased additional retrocessional coverage for our marine, technical risk and aviation reinsurance product line to limit our future probable maximum losses during 2007. These retrocession treaties provide us with protection on an excess of loss, quota share treaty and facultative basis for policies written in our reinsurance product lines of business. Ceded premiums are earned over the period of each insured risk.

Net premiums earned. Net premiums earned of \$0.3 million for the year ended December 31, 2007 decreased by \$46.2 million compared to \$46.5 million for the year ended December 31, 2006. The decrease reflects the decrease in earning of premiums on contracts written in prior periods, the impact of the decision to discontinue writing of new and renewal business in our reinsurance and insurance lines of business and the impact of changes in premium estimates and premiums written. Gross premiums written in our specialty reinsurance run-off segment are being earned over the periods of reinsured or underlying insured risks which are typically one year.

Other income. Other income was \$2.6 million for the year ended December 31, 2007 compared to \$0.8 million for the year ended December 31, 2006, and related to income, including fees, recognized on non-traditional reinsurance contracts.

Net losses and loss expenses. Net losses and loss expenses had a favorable impact of \$6.1 million for the year ended December 31, 2007 compared to an expense of \$40.0 million for the year ended December 31, 2006. The decrease in net losses and loss expenses incurred was due to favorable loss reserve developments, lower net earned premium in 2007 and fewer significant loss occurrences, particularly compared to those relating to the development of losses related to the 2005 hurricanes. Net losses and loss expenses are also a function of our net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of reinsurance underwritten. For the year ended December 31, 2007, we recognized favorable development of \$9.0 million relating to commutations and \$6.7 million relating to the 2004 and 2005 hurricanes.

Included in our expected ultimate losses during the year ended December 31, 2007 are specific loss estimates on contracts of reinsurance insuring claims arising from Hurricanes Katrina, Rita and Wilma. Our estimate of our specialty reinsurance run-off segment's exposure to ultimate claim costs associated with these hurricanes based on currently available information is \$72.6 million compared to \$76.6 million for the year ended December 31, 2006. Our estimate of ultimate losses from these events is primarily based on currently available information, claims notifications received to date, industry loss estimates, output from industry models, a review of affected contracts and discussion with cedants and brokers. The actual amount of losses from the hurricanes may vary significantly from the estimate.

Acquisition expenses. Acquisition expenses were favorable \$1.1 million for the year ended December 31, 2007 compared to an expense of \$12.5 million for the year ended December 31, 2006. The decrease in acquisition expenses was due to the decrease in the number of reinsurance contracts we entered into and the associated net premiums earned. These acquisition expenses primarily represented brokerage and ceding commissions.

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Lloyd's

The following table shows the results of the Lloyd's segment for the years ended December 31, 2007 and 2006:

2007	2006	Change	(\$ in thousands)	Gross premiums written	\$ 124,049	\$ 91,758	\$ 32,291	Premiums ceded	(27,654)	(30,014)	2,360	Net premiums written	\$ 96,395	\$ 61,744	\$ 34,651	Net premiums earned	\$ 80,784	\$ 65,523	\$ 15,261	Net losses and loss expenses	(53,845)	(50,382)	(3,463)	
Acquisition expenses	(27,387)	(12,043)	(15,344)	General and administrative expenses	(13,784)	(12,886)	(898)	Segment loss	\$ (14,232)	\$ (9,788)	\$ (4,444)	Ratios:	Loss and loss expense ratio	66.7 %	76.9 %	(10.2)%	Acquisition expense ratio	33.9 %	18.4 %	15.5 %	General and administrative expense ratio	17.1 %	19.7 %	(2.6)%

Premiums. Stamp capacity is the measure of the amount of premium Syndicate 4000 is authorized to write and is determined based on a business plan approved by the Council of Lloyd's and the funds provided by the capital providers. The stamp capacity of Syndicate 4000 for 2007 was £73 million (\$147 million) which equates to the amount of premium that can be written in the 2007 underwriting year (premium being defined for these purposes only as gross premium less acquisition expenses). We provided 90%, or £65.7 million (\$132 million) of the stamp capacity for the 2007 underwriting year. Syndicate 4000 had stamp capacity of £82 million (\$160 million) during 2006, all of which was provided by us.

Gross and net premiums written were \$124.0 million and \$96.4 million for the year ended December 31, 2007 compared to \$91.8 million and \$61.7 million for the year ended December 31, 2006. Despite our reduced participation in Syndicate 4000 in 2007, gross and net premiums written have increased as Syndicate 4000 was better able to attract new and secure renewal business during the year because of the provision of third party capital to the syndicate, the establishment of the Pembroke Managing Agency and the fact that Syndicate 4000, in its third year, benefited from increased market recognition. Beginning in 2007, Syndicate 4000's reported gross written premiums include estimates of unreported premiums and premiums received but not yet processed at Lloyd's because of time delays between underlying policies being written or adjusted and the inclusion of those policies or policy adjustments in the Lloyd's underwriting systems. Policy adjustments typically include reinstatement premiums or adjustment premiums related to underwriting experience or the volume of underlying insurance business.

The table below shows gross and net premiums written by product line for the years ended December 31, 2007 and 2006.

2007	2006	(\$ in thousands)	Gross premiums written	Net premiums written	Gross premiums written	Net premiums written

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written Financial institutions	\$ 59,568	\$ 44,704	\$ 52,440	\$ 34,364	Professional liability	46,011		
33,929	33,430	22,684	Specie and fine art	16,851	16,152	5,859	4,719	Kidnap and ransom
1,619	1,610	29	(22)	Total	\$ 124,049	\$ 96,395	\$ 91,758	\$ 61,744

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In the ordinary course of business, Syndicate 4000 reinsures certain insurance risks with the purpose of limiting maximum loss exposure. Premiums ceded to reinsurers were \$27.7 million during the year ended December 31, 2007, compared to premiums ceded to reinsurers of \$30.0 million for the year ended December 31, 2006. Despite the fact that gross written premium of Syndicate 4000 increased during the year ended December 31, 2007, as a percentage of written premium, the premiums ceded for the year ended December 31, 2006 was greater than the premiums ceded for the year ended December 31, 2007. This is due to the Company being subject to an excess of loss reinsurance contract that was purchased for the 2006 underwriting year which required us to cede minimum fixed amounts of premium, regardless of the amount of gross premium we actually wrote. For the 2007 underwriting year we have purchased a similar excess of loss reinsurance contract with slightly lower fixed minimum ceded premium requirements. Following a revision of the ultimate premium forecast for the 2007 underwriting year, due to market underwriting conditions, we have, however, slightly increased the proportion of ceded premium on this 2007 excess of loss treaty. The adjustment resulted in additional premium ceded of \$1.8 million for the year ended December 31, 2007.

Net premiums earned during the year ended December 31, 2007 were \$80.8 million, an increase of \$15.3 million, compared to \$65.5 million for the year ended December 31, 2006. The increase in net premiums earned was primarily due to growth in Syndicate 4000's business and the earning of premiums written in prior periods. Gross premiums written and ceded premiums are being earned over the period of each insured risk which is typically one year. There was a negligible impact on net premiums earned arising from the increase in proportion of ceded premium on the 2007 excess of loss reinsurance contract.

Net losses and loss expenses. Net losses and loss expenses were \$53.8 million for the year ended December 31, 2007, an increase of \$3.4 million, compared to \$50.4 million for the year ended December 31, 2006. Net losses and loss expenses are a function of our net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance underwritten.

Syndicate 4000 has exposure to the subprime mortgage developments in the United States through D&O and E&O policies it has written primarily in its financial institutions and professional lines of business. We expect claims activity within the D&O and E&O insurance markets to rise as a result of an increase in class action lawsuits filed against public companies due to market losses and related stock price depreciation associated with the subprime mortgage and credit crisis in the United States. As a result, the increase in net losses and loss expenses is primarily due to \$9.8 million of new losses and loss expenses recorded in relation to our estimates associated with this exposure. We have recorded specific reserves for reported claims of \$11.3 million in the results for the year ended December 31, 2007. In addition we have recorded \$12.0 million of IBNR reserves, following an actuarial review of the Syndicate's portfolio and its exposure to further claims from these subprime mortgage developments, based to a significant degree, on industry loss estimates of the total expected losses. We have also recorded a reinsurance recoverable of \$13.5 million on purchased contracts of reinsurance. Due to these loss and loss expense notifications, a premium deficiency reserve amounting to approximately \$8.0 million has been recorded. This adjustment has been reflected in the statement of operations through acquisition costs, as more fully described below.

The impact of the subprime mortgage loss and loss expenses for the year ended December 31, 2007 is partially offset by \$8.0 million of net favorable loss developments on the results of prior underwriting years, in particular, net favorable loss development has occurred in relation to the 2005 underwriting year and, to a lesser extent, in relation to the 2006 underwriting year.

Our Lloyd's segment's net loss ratio was 66.7% for the year ended December 31, 2007 as compared to a net loss ratio of 76.9% for the year ended December 31, 2006. The net loss ratio for the year ended December 31, 2007 was adversely impacted by the subprime loss and loss expenses recorded in the fourth quarter of 2007. This has been

partially offset by net favorable loss development in certain product lines for more mature accident periods, specifically in respect of the

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2005 underwriting year of account where actual loss experience has been better than expected. Additionally, the net loss ratio for the year ended December 31, 2006 and to a lesser extent for the year ended December 31, 2007 was adversely impacted by the excess of loss reinsurance contracts that we purchased for the 2006 underwriting year, which requires us to cede minimum fixed amounts of our premium regardless of the amount of gross premium we actually wrote. We expect that ceding minimum fixed amounts of premiums will continue to adversely impact, to a lesser extent, net loss ratios as the 2006 underwriting year continues to mature.

Acquisition expenses. Acquisition expenses were \$27.4 million for the year ended December 31, 2007, an increase of \$15.4 million compared to \$12.0 million for the year ended December 31, 2006. The increase in acquisition expenses was driven by the premium deficiency reserve of approximately \$8.0 million related to the subprime mortgage developments in the United States in certain professional lines. These charges relate to the write-off of deferred acquisition costs that are deemed irrecoverable from the future earning of unearned premium reserves because we expect that potential future reported losses may exceed those unearned premium reserves.

Our acquisition expense ratio was 33.9% for the year ended December 31, 2007, an increase of 15.5%, compared to 18.4% for the year ended December 31, 2006. The increase is primarily attributable to four factors. First, in connection with the above premium deficiency, the additional charge of \$8.0 million resulted in an increase in the acquisition expense ratio of 9.9%. Second, in connection with a change in the estimates of acquisition expenses, we recognized a cumulative adjustment which resulted in an increased acquisition expense ratio. We expect that this change in estimating acquisition expenses will have a lesser impact on the acquisition expense ratio in the future. Third, there was an increase in premium written in the specie and fine art and kidnap and ransom business. This business generally carries higher acquisition expenses than professional and financial institution product lines. Finally, the continuing effect of the excess of loss reinsurance contract that we purchased for the 2006 underwriting year which required us to cede minimum fixed amounts of premium regardless of the amount of gross premium we actually wrote continues to have an impact, but to a declining extent, as we continue to earn this premium throughout 2007.

General and administrative expenses. General and administrative expenses were \$13.8 million for the year ended December 31, 2007, an increase of \$0.9 million, compared to \$12.9 million for the year ended December 31, 2006. The general and administrative expense ratio for the year ended December 31, 2007 was 17.1%, compared to 19.7% for the year ended December 31, 2006. Many of the general and administrative expenses incurred by Syndicate 4000 are fixed costs such as the Lloyd's central fund contributions, managing agency fees, both of which are based on a percentage of underwriting capacity set at the start of the underwriting year, and employee related expenses. Syndicate 4000's Lloyd's central fund contribution for the 2007 underwriting year was reduced to 1% of stamp capacity from 2% for the 2006 underwriting year. In addition, the lower stamp capacity for 2007 than for 2006 also contributes to lower central fund charges. These reduced costs are partially offset by increased managing agency fees in 2007.

As a result of the sale of our interests in Syndicate 4000 on February 13, 2008, this segment, as well as the results of the period from January 1, 2008 to February 13, 2008, will be reclassified into discontinued operations in 2008.

Technical services

2007	2006	Change	(\$ in thousands)	Technical services revenues	\$ 1,707	\$ 3,331	\$ (1,624)	General and administrative expenses	(2,317)	(4,283)	1,966	Segment loss	\$ (610)	\$ (952)	\$ (342)
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Technical services revenues. Technical services revenues were \$1.7 million for the year ended December 31, 2007, compared to \$3.3 million for the year ended December 31, 2006. Technical

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services revenues are mainly derived from our environmental liability assumption programs. We expect that our technical services revenues will continue to decrease in future periods as the remediation is closer to completion.

General and administrative expenses. General and administrative expenses were \$2.3 million for the year ended December 31, 2007, compared to \$4.3 million for the year ended December 31, 2006. The decrease is due to the fact that most of the remediation work on one of our environmental liability assumption programs occurred during the first quarter of 2006. The remediation is now close to being completed and, as a result, has not generated expenses to the same extent as it did in 2006. We expect that our technical services expenses will continue to decrease in future periods as the remediation is closer to completion.

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Years ended December 31, 2006 and 2005

The following table summarizes our net underwriting results and profitability measures for our segments for the years ended December 31, 2006 and 2005.

Specialty insurance run-off

2006	2005	Change	(\$ in thousands)		Gross premiums written	\$ 60,107	\$ 311,321	\$ (251,214)
Premiums ceded	(34,126)	(116,404)	82,278	Net premiums written	\$ 25,981	\$ 194,917	\$ (168,936)	
) Net premiums earned	\$ 113,289	\$ 160,620	\$ (47,331)	Other income	2,873	1,200	1,673	
losses and loss expenses	(65,706)	(120,710)	55,004	Acquisition expenses	(18,029)	(21,836)		
3,807	General and administrative expenses	(18,440)	(21,750)	3,310	Segment income (loss)	\$ 13,987		
\$ (2,476)	\$ 16,463	Ratios:	Loss and loss expense ratio	58.0 %	75.2 %	(17.2)%		
Acquisition expense ratio	15.9 %	13.6 %	2.3 %					

Premiums. Gross and net premiums written were \$60.1 million and \$26.0 million for the year ended December 31, 2006 compared to \$311.3 million and \$194.9 million for the year ended December 31, 2005. The significant decrease in our specialty insurance run-off segment's gross and net premiums written was due to the decision to cease writing new business in 2006, our decision to run-off the majority of our businesses and the effect of premium returns to our clients and the transfer of policies to third parties.

During 2006 we returned or transferred approximately \$59.4 million of gross written premiums since our decision to run-off these product lines and to reduce the amount of our in-force policy exposures.

The table below shows gross and net premiums written by product line for the years ended December 31, 2006 and 2005, whether written on a traditional insurance, program or structured basis.

2006	2005	(\$ in thousands)		Gross		premiums		written		Net	
premiums	written	Net	premiums	written	Gross	premiums	written	Net	premiums	written	Net
4,222	49,737	33,741	Technical risk property(1)	\$ 71,591	\$ 37,329	\$ 187,474	\$ 114,377	Professional liability	5,005	23,464	Fidelity and
crime	(1,259)	(1,428)	13,197	6,654	Surety	3,645	1,843	12,041	9,370	Trade credit and	political risk
(4,128)	(5,195)	7,574	6,022	Structured insurance	(62)	(62)	1,289	1,289	Other	—	(1,126)
—	—	—	Total	\$ 60,107	\$ 25,981	\$ 311,321	\$ 194,917				

(1) The gross and net premiums written generated by our HBW program is included in our technical risk property product

line, as described below. (2) Negative premium amounts reflect the impact of premiums returned to our clients on policy cancellation.

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During the year ended December 31, 2006, we continued to write the HBW program in our technical risk property product line under the terms of the managing agency agreement which expired on December 2, 2006. This program accounted for the substantial majority of total specialty insurance run-off segment gross and net premiums written in the year ended December 31, 2006. The policies in our HBW program have been underwritten by a third-party agent which is instructed to follow our underwriting guidelines. Our HBW gross premiums written during the year ended December 31, 2006 are summarized in the table below by specialty risk class.

				(\$ in millions)	Casualty	\$
49.7	Warranty*	7.4	Property	4.8	Total	\$ 61.9

* Warranty is written as reinsurance.

Premiums ceded were \$34.1 million during the year ended December 31, 2006, a decrease of \$82.3 million compared to \$116.4 million for the year ended December 31, 2005. The decrease in premiums ceded is a result of the decrease in our gross premiums written.

Net premiums earned during the year ended December 31, 2006 were \$113.3 million, a decrease of \$47.3 million, compared to \$160.6 million for the year ended December 31, 2005, representing the reductions of premiums written and the return of premiums to our clients. Gross premiums written and ceded premiums are earned over the period of each insured risk. The terms of our insurance contracts range from between one and ten years with the majority of our contracts being for a one year period.

Other income. Other income was \$2.9 million for the year ended December 31, 2006 and related to income, including fees, recognized on non-traditional insurance contracts.

Net losses and loss expenses. Net losses and loss expenses were \$65.7 million for the year ended December 31, 2006, a decrease of \$55.0 million compared to \$120.7 million for the year ended December 31, 2005. Net losses and loss expenses are a function of our net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance and reinsurance underwritten. The decrease in net losses and loss expenses is due to:

- the decrease in significant loss occurrences, particularly compared to those related to the 2005 hurricanes and the first quarter 2005 rupture of an oil pipeline in California during a mudslide;
- a substantial decline in the number of insurance contracts we entered into and the associated net premiums earned; and
- favorable development in our ultimate loss ratio selections in certain product lines, particularly in our professional insurance product line in which our selected ultimate net loss ratio for mature accident periods has reduced to approximately 61.6% in 2006 from approximately 68.2% in 2005, resulting in a reduction of net loss and loss expense reserves of approximately \$3.5 million.

Our expected ultimate losses during the year ended December 31, 2006 also included estimated gross and net losses of \$5.2 million and \$2.6 million related to damage caused by an oil pipeline in California which ruptured during a mudslide in the first quarter of 2005, for which the damage is covered by an insurance contract issued by our

environmental liability product line.

Our specialty insurance run-off segment net loss ratio was 58.0% for the year ended December 31, 2006 a decrease of 17.2% compared to a net loss ratio of 75.2% for the year ended December 31, 2005. The decrease in the specialty insurance run-off segment net loss ratio is primarily due to the significant loss estimates arising in 2005 from Hurricanes Katrina, Rita and Wilma as well

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as to the loss estimates arising in 2005 from the ruptured oil pipeline loss. The 2005 hurricanes did not contribute any loss ratio percentage points to the specialty insurance run-off segment net loss ratio in 2006 compared to 7.0% in 2005. As discussed above, the reduction in certain of our product line's ultimate net loss ratio for mature accident periods also contributed to the lower insurance run-off segment net loss in 2006.

Acquisition expenses. Acquisition expenses were \$18.0 million for the year ended December 31, 2006 compared to \$21.8 million for the year ended December 31, 2005. The decrease in acquisition expenses was due to the substantial decline in the number of insurance contracts we entered into and the associated net premiums earned. These acquisition expenses primarily represented brokerage fees, commission fees and premium tax expenses and were net of ceding commissions earned on purchased reinsurance treaties.

Our acquisition expense ratio was 15.9% for the year ended December 31, 2006 compared to 13.6% for the year ended December 31, 2005. The increase in our acquisition expense ratio in the specialty insurance run-off segment is primarily due to the impact of purchased reinsurance protection in 2006 and 2005 which reduced net earned premium by a higher proportion in 2006 than 2005. The increase is also due, to a lesser extent, to the return of premiums to canceling policies, including, in some instances, earned premium. Deferred acquisition costs include, as of December 31, 2006, \$7.2 million of acquisition expenses on written contracts of insurance that will be amortized in future periods as the premiums written to which they relate are earned.

General and administrative expenses. General and administrative expenses totaled \$18.4 million for the year ended December 31, 2006 compared to \$21.8 million for the year ended December 31, 2005. The decrease in our general and administrative expense was due to the cost saving measures taken in response to discontinuing writing new and renewal business in 2006.

Specialty reinsurance run-off

2006	2005	Change	(\$ in thousands)	Gross assumed premiums written	\$ 6,864	\$ 216,912	\$ (210,048)
Premiums ceded	(14,035)	(83,434)	69,399	Net premiums written	\$ (7,171)	\$ 133,478	\$ (140,649)
Net premiums earned	\$ 46,487	\$ 166,944	\$ (120,457)	Other income	781	1,974	(1,193)
Net losses and loss expenses	(40,033)	(178,887)	138,854	Acquisition expenses	(12,468)	(42,714)	30,246
General and administrative expenses	(6,420)	(9,847)	3,427	Segment loss	\$ (11,653)	\$ (62,530)	\$ 50,877
Ratios:				Loss and loss expense ratio	86.1 %	107.2 %	(21.1)%
Acquisition expense ratio	26.8 %	25.6 %	1.2 %				

Premiums. Gross and net premiums written were \$6.8 million and \$(7.2) million for the year ended December 31, 2006 compared to \$216.9 million and \$133.5 million of gross and net premiums written for the year ended December 31, 2005. The decrease in our specialty reinsurance run-off segment's net premiums written reflects the decrease in our reinsurance business lines as a result of our decision to discontinue the writing of new and renewal business in our reinsurance business line. Ceded written premiums in 2006 were greater than gross premiums written because of the purchase of additional reinsurance protection for exposures in our marine, technical risk and aviation product line.

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The table below shows gross and net premiums written by product line whether written on a traditional reinsurance, programs or structured basis:

2006	2005	(\$ in thousands)		Gross							
premiums											
written	Net										
premiums											
written	Gross										
premiums											
written	Net										
premiums											
written	Property	\$ 8,673	\$ (64)	\$ 83,505	\$ 21,661	Casualty	2,236	2,236	79,376	79,376	
Marine, technical risk and aviation		(4,045)	(9,343)	54,031	32,441	Total	\$ 6,864	\$ (7,171)	\$		
216,912		\$ 133,478									

The negative gross written premium on our marine, technical risk and aviation product line was primarily due to cancellations of certain treaty contracts and reductions in estimated reinsurance premiums written on certain of our treaty quota share contracts, resulting in reduced premiums.

Ceded premiums were \$14.0 million during the year ended December 31, 2006 compared to \$83.4 million for the year ended December 31, 2005. The decrease in our ceded premiums written largely reflects our decision to discontinue writing business in our reinsurance product lines in 2006. We also purchased additional retrocessional coverage for our marine, technical risk and aviation reinsurance product line to limit our future probable maximum losses during 2006. These retrocession treaties provide us with protection on an excess of loss, quota share treaty and facultative basis for policies written in our reinsurance product lines of business. Ceded premiums also includes \$8.7 million of premium ceded to a third-party reinsurer under the October 2005 portfolio transfer of substantially all of our in-force technical risk property insurance and property reinsurance business. Ceded premiums are earned over the period of each insured risk.

Net premiums earned of \$46.5 million for the year ended December 31, 2006 decreased by \$120.5 million compared to \$167.0 million for the year ended December 31, 2005. The decrease reflects the decrease in earning of premiums on contracts written during the years ended December 31, 2006, 2005 and 2004, the impact of the decision to discontinue writing of new and renewal business in our reinsurance and insurance lines of business and the purchase of additional retrocessional protection on our marine, technical risk and aviation product line. Gross premiums written in our specialty reinsurance run-off segment are being earned over the periods of reinsured or underlying insured risks which are typically one year.

Other income. Other income was \$0.8 million for the year ended December 31, 2006 compared to \$2.0 million for the year ended December 31, 2005, and related to income, including fees, recognized on non-traditional reinsurance contracts.

Net losses and loss expenses. Net losses and loss expenses were \$40.0 million for the year ended December 31, 2006 compared to \$178.9 million for the year ended December 31, 2005. The decrease in net losses and loss expenses incurred was due to lower net earned premium in 2006 and to fewer significant loss occurrences, particularly compared to those related to the 2005 hurricanes. Net losses and loss expenses are also a function of our

net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of reinsurance underwritten.

Included in our expected ultimate losses during the year ended December 31, 2006 are specific loss estimates on contracts of reinsurance insuring claims arising from Hurricanes Katrina, Rita and Wilma. Our estimate of our specialty reinsurance run-off segment's exposure to ultimate claim costs associated with these hurricanes based on currently available information is \$76.6 million (including net reinstatement premiums), of which \$5.0 million is included in net losses and loss expenses for the year ended December 31, 2006 compared to \$71.9 million for the year ended December 31, 2005. Our estimate of ultimate losses from these events was primarily based, at the time of the estimate, on then available information, claims notifications, industry loss estimates, output from industry models, a review of affected contracts and discussion with cedants and brokers.

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The table below shows gross and net premiums written by product line for the years ended December 31, 2006 and 2005.

2006	2005	(\$ in thousands)		Gross			
premiums	Net						
written	premiums						
	written	Gross					
	premiums						
	written	Net					
	premiums						
written Professional lines	\$ 85,870	\$ 57,047	\$ 79,501	\$ 60,593	Specie and fine art	5,859	4,719
1,201	1,053	Kidnap and ransom	29	(22)	—	—	Total \$ 91,758
							\$ 61,744
							\$ 80,702
							\$ 61,646

Premiums ceded were \$30.0 million during the year ended December 31, 2006, an increase of \$10.9 million, compared to \$19.1 million for the year ended December 31, 2005. The increase in premiums ceded reflects the increase in our gross premium written described above and reflects the acceleration of minimum ceded written premium relating to our excess of loss reinsurance treaties. Minimum and deposit ceded premium is written in proportion to our expected gross written premiums.

Net premiums earned during the year ended December 31, 2006 were \$65.5 million, an increase of \$29.0 million, compared to \$36.5 million for the year ended December 31, 2005, representing amortization of premiums written and ceded during the years ended December 31, 2004, 2005 and 2006. The increase in our net premiums earned was largely due to the growth of our net premiums written from our Lloyds syndicate. This increase was partially offset by the effect of the A.M. Best's ratings downgrade and subsequent uncertainties around the business and achievements of gross premium estimates resulting in the acceleration of the minimum ceded earned premium as described above. Gross premiums written and ceded premiums are being earned over the period of each insured risk which is typically one year.

Net losses and loss expenses. Net losses and loss expenses were \$50.4 million for the year ended December 31, 2006, an increase of \$25.7 million, compared to \$24.7 million for the year ended December 31, 2005. Net losses and loss expenses are a function of our net premiums earned and our expected ultimate losses and loss expenses for reported and unreported claims on contracts of insurance underwritten. The increase in net losses and loss expenses is primarily due to the increase in our net premiums earned.

Our Lloyd's segment net loss ratio was 76.9% for the year ended December 31, 2006, an increase of 9.4% compared to a net loss ratio of 67.5% for the year ended December 31, 2005. The increase in the Lloyd's segment net loss ratio is primarily due to the effect of the excess of loss reinsurance contract we entered into that requires us to cede minimum fixed amounts of our premium, regardless of the amount of gross premium written in Syndicate 4000 in the year ended December 31, 2006.

Acquisition expenses. Acquisition expenses were \$12.0 million for the year ended December 31, 2006, an increase of \$6.9 million compared to \$5.1 million for the year ended December 31, 2005. The increase in acquisition expenses was driven by a higher level of earned premium in 2006.

Our acquisition expense ratio was 18.4% for the year ended December 31, 2006, an increase of 4.5%, compared to 13.9% for the year ended December 31, 2005. The acceleration of minimum ceded earned premium contributed to the higher ratio.

General and administrative expenses. General and administrative expenses were \$12.9 million for the year ended December 31, 2006 an increase of \$4.2 million, compared to \$8.7 million for the year ended December 31, 2005. The increase in our general and administrative expense from 2005 to 2006 was mainly due to the fact that 2005 was a start-up year for Syndicate 4000 and 2006 reflects the general and administrative expenses of a fully operating Syndicate 4000, including an additional number of employees hired throughout 2006 as well as increases in Lloyd's central fund and managing

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agent expenses. General and administrative expenses includes a number of fixed costs including the Lloyd's Central Fund contributions which are based on a percentage of underwriting capacity set at the start of the underwriting year, and employee and related expenses.

Technical services

2006	2005	Change	(\$ in thousands)	Technical services revenues	\$ 3,331	\$ 19,037	\$(15,706)	General and administrative expenses	(4,283)	(18,545)	14,262	Segment (loss) income	\$(952)	\$ 492	\$ (1,444)
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Technical services revenues. Technical services revenues were \$3.3 million for the year ended December 31, 2006, compared to \$19.0 million for the year ended December 31, 2005. The decrease is due to a significant portion of remediation of our QLT Buffalo LLC environmental liability assumption program occurring during the second and third quarters of 2005. The remediation was close to being completed and, as a result, did not generated technical services revenues to the same extent as it did in 2005.

General and administrative expenses. Direct general and administrative expenses were \$4.3 million for the year ended December 31, 2006, compared to \$18.5 million for the year ended December 31, 2005. The decrease is due to a significant portion of remediation of our QLT Buffalo LLC environmental liability assumption program occurring during the second and third quarters of 2005.

Financial Condition and Liquidity

Quanta Holdings is organized as a Bermuda holding company and as such, has no direct operations of its own. Quanta Holdings' assets currently consist of investments in our subsidiaries through which we conducted our specialty insurance and reinsurance run-off and our technical services operations. We have operations in the U.S., Bermuda and Ireland.

As a holding company, Quanta Holdings has and will continue to have funding needs for general corporate expenses, taxes and the payment of other obligations. Funds to meet these obligations are expected to come primarily from dividends, interest and other statutorily permissible payments from its operating subsidiaries. We believe that the operating subsidiaries have sufficient assets to pay their respective currently foreseen insurance liabilities as they become due. However, the ability of our operating subsidiaries to make payments to Quanta Holdings is limited by the applicable laws and regulations of the domiciles in which the subsidiaries operate. These laws and regulations subject our subsidiaries to significant restrictions and require, among other things, the maintenance of minimum solvency requirements and limitations regarding the amount of dividends, or the approval of certain regulators in the event of a return of capital, that these subsidiaries can ultimately pay to Quanta Holdings. In addition, following the withdrawal of our A.M. Best rating, the Bermuda Monetary Authority, the regulator of our most significant subsidiary, Quanta Bermuda, amended Quanta Bermuda's license to, among other things, restrict it from making any dividend payments to Quanta Holdings without the approval of the BMA or to enter into new transactions. We are working with applicable regulatory authorities to facilitate our ability, as the business we wrote expires over time, to pay dividends or return capital from our insurance operating subsidiaries to the holding company. The payment of dividends or return of capital to the holding company requires regulatory approval. In addition, because we have regulated subsidiaries which are owned by other regulated subsidiaries, which we refer to as "stacked subsidiaries," in certain instances obtaining approval to dividend funds or return capital requires the approval of a number of regulators before

the funds can be made available to Quanta Holdings. Following approval from the Bermuda Monetary Authority we declared a dividend of \$1.75 per share or approximately \$122.7 million which is payable on March 28, 2008 to shareholders of record on March 25, 2008.

We are also subject to constraints under the Bermuda Companies Act that affect our ability to pay dividends on our shares. We may not declare or pay a dividend or make a distribution if we have

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reasonable grounds for believing that we are, or will after the payment be, unable to pay our liabilities as they become due or if the realizable value of our assets will thereby be less than the aggregate of our liabilities and our issued share capital and share premium accounts. While we currently meet these requirements, there can be no assurance that we will continue to do so in the future.

As of March 3, 2008, prior to the payment of the March dividend our cash and cash equivalents and investments of approximately \$667.4 million following the sale of our interest at Lloyd's. Our cash and cash equivalents and investment balances include approximately \$96.8 million that is pledged as collateral for letters of credit, approximately \$152.5 million held in trust funds for the benefit of ceding companies and to fund our obligations associated with the assumption of an environmental remediation liability, \$37.3 million held in trust funds that are related to our deposit liabilities and \$27.9 million that is on deposit with, or has been pledged to, U.S. state insurance departments. After giving effect to these assets pledged or placed in trust, we estimate that we have unrestricted net investments of \$352.9 million, including net cash and cash equivalents of approximately \$19.0 million. This amount is held mainly by our operating subsidiaries in Bermuda, the U.S. and Europe.

Some of our insurance and many of our reinsurance contracts contain termination rights that were triggered by the A.M. Best rating downgrades. Some of these insurance and reinsurance contracts also require us to post additional security. Further, the downgrade in our rating from "B++" (very good) to "B" (Fair) triggered additional termination provisions and required the posting of additional security in certain of our other insurance and reinsurance contracts. We were required to post additional security either through the issuance of letters of credit or the placement of securities in trust under the terms of those insurance or reinsurance contracts. In addition, many of our insurance contracts and certain of our reinsurance contracts provide for cancellation at the option of the policyholder regardless of our financial strength rating. Accordingly, we may also elect to post security under these other contracts.

As of December 31, 2007, we had net cash and cash equivalent balances and other investments of approximately \$228.8 million that are available to post as security or place in trust. We currently believe that we have sufficient assets to pay our foreseen liabilities as they become due and meet our foreseen collateral requirements within our subsidiaries.

As of December 31, 2007 and February 29, 2008, to the face amounts of our fully secured outstanding letters of credit were approximately \$91.6 million and \$84.7 million.

Financial condition

Our board of directors established our investment policies and created guidelines for hiring external investment managers. Management implements our investment strategy with the assistance of the external managers. Our investment guidelines specify minimum criteria on the overall credit quality, liquidity and risk-return characteristics of our investment portfolio and include limitations on the size of particular holdings, as well as restrictions on investments in different asset classes. The board of directors monitors our overall investment returns and reviews compliance with our investment guidelines.

Our investment strategy seeks to preserve principal and maintain liquidity while trying to maximize total return through a high quality, diversified portfolio. Investment decision making is guided mainly by the nature and timing of our expected liability payouts, management's forecast of our cash flows and the possibility that we will have unexpected cash demands, for example, to satisfy claims due to catastrophic losses. Our investment portfolio currently consists mainly of highly rated and liquid fixed income securities. However, to the extent our insurance liabilities are correlated with an asset class outside our minimum criteria, our investment guidelines will allow a deviation from

those minimum criteria provided such deviations reduce overall risk. We have no immediate intent to liquidate our investment portfolios, other than in normal course of our investment management policies. However, we may be required to sell securities to satisfy return premium, to pay claims or to meet loss obligations on contracts that are cancelled or commuted.

As at December 31, 2007, the market value of our total investment portfolio including cash and cash equivalents was \$801.7 million, of which \$559.5 million related to trading fixed maturity

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investments, \$22.3 million related to cash and cash equivalents, \$131.0 million related to restricted cash and cash equivalents, \$88.9 million related to trading short-term investments. Of the above amounts, \$39.2 million related to trading investments related to deposit liabilities. The majority of our investment portfolio consists of fixed maturity and cash investments which are currently managed by Deutsche Asset Management, our external investment advisors. Custodians of our externally managed investment portfolios are Comerica Incorporated, JP Morgan Chase Bank N.A. and Citibank N.A.

Our investment guidelines require that the average credit quality of the investment portfolio is typically Aa3/AA- and that no more than 5% of the investment portfolio's market value shall be invested in securities rated below Baa3/BBB-. As of December 31, 2007, all of the fixed maturity investments were investment grade, with a weighted average credit rating of "AA+" based on ratings assigned by S&P.

Our portfolio of investment grade fixed maturity investments includes mortgage-backed and asset-backed securities and collateralized mortgage obligations. These types of securities have cash flows that are backed by the principal and interest payments of a group of underlying mortgages or other receivables. During 2007, delinquency and default rates have increased on these types of securities, and particularly on securities backed by subprime mortgages. Generally, subprime mortgages are considered to be those made to borrowers who do not qualify for market interest rates for one or more possible reasons, such as a low credit score, a limited or lack of credit history or a lack of earnings documentation. As a result of the increasing default rates of subprime borrowers, there is a greater risk of defaults on mortgage-backed and asset-backed securities and collateralized mortgage obligations, especially those that are non-investment grade. Therefore, fixed maturities securities backed by subprime mortgages have exhibited significant declines in fair value and liquidity. These factors combined with the contraction in liquidity in the principal markets for these securities makes the estimate of fair value increasingly uncertain. The fair values of our holdings in securities exposed to subprime borrowers are generally not based on quoted prices for identical securities, but are based on model-derived valuations from our independent pricing sources in which significant inputs and significant value drivers are observable in active markets. Should we need to liquidate these securities within a short period of time, the actual realized proceeds may be significantly different from the fair values estimated at December 31, 2007. We believe our exposure to subprime credit risk is limited although there can be no assurance that events in the subprime mortgage sector will not adversely affect the value of our investments. We have determined that a write-down for impairment of these securities is not necessary based on a consideration of relevant factors including prepayment rates, subordination levels, default rates, credit ratings, weighted average life, credit default insurance and historic and current cashflows. Together with our investment managers, we continue to monitor our potential exposure to subprime borrowers and we will make adjustments to the investment portfolio as necessary.

We currently believe that at December 31, 2007 our exposure to subprime mortgages was approximately \$5.4 million, which represents less than one percent of our total cash and investments, and our exposure to Alt-A mortgages was approximately \$6.2 million. Alt-A mortgages are considered to be those made to borrowers who do not qualify for market interest rates but who are considered to have less credit risk than subprime borrowers.

recognized in earnings in future periods.

Our reserves for losses and loss adjustment expenses, net of reinsurance recoverable, totaled \$376.6 million as December 31, 2007 compared to \$402.4 million as of December 31, 2006. This includes \$134.5 million and \$71.6 million as of December 31, 2007 and 2006 relating to our Lloyd's segment.

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During the year ended December 31, 2007, we commuted several assumed reinsurance contracts which resulted in a reduction of our gross loss and loss expense reserves amounting to \$47.1 million. We also experienced net favorable loss development in our insurance and reinsurance segments amounting to \$31.1 million and net favorable loss development in our Lloyd's segment amounting to \$8.0 million. We further reduced our net loss reserves by \$5.1 million through cancellation of insurance contracts with our clients, primarily as a result of cancellations in our HBW program. This was partially offset by our net losses and loss expenses incurred during the year ended December 31, 2007, which include \$9.8 million of losses incurred in our Lloyd's segment relating to our exposure to the subprime mortgage developments in the United States during the latter part of 2007.

Our reserves for losses and loss adjustment expenses as of December 31, 2007 includes our estimate of gross and net unpaid loss expenses, including incurred but not reported losses, totaling \$43.3 million and \$26.9 million relating to Hurricanes Katrina, Rita and Wilma. Our estimate of our unpaid exposure to ultimate claim costs associated with these losses is based on currently available information, claim notifications received to date, industry loss estimates, output from industry models, a review of affected contracts and discussion with clients, cedants and brokers. The actual amount of future loss payments relating to these loss events may vary significantly from this estimate.

Of our total reserves for losses and expenses of \$525.1 million as of December 31, 2007 approximately \$400.9 million or 76% is represented by our estimate of incurred but not reported reserves (IBNR). Excluding Lloyd's, approximately 74% is represented by IBNR. However, we have participated in lines of business where claims may not be reported for some period of time after those claims are incurred.

Our reinsurance recoverables as of December 31, 2007 totaled \$148.4 million, of which \$1.5 million was currently due, compared to reinsurance recoverables as of December 31, 2006 of \$221.2 million. This includes \$25.8 million and \$28.8 million as of December 31, 2007 and 2006 relating to our Lloyd's segment. The decrease in our reinsurance recoverable balance reflects cash received from reinsurers during the year and, to a lesser extent, favorable developments in our estimates of gross loss and loss expenses and our commutation activity. As of December 31, 2007, our reinsurance recoverable balances also include our estimate of unpaid loss expenses recoverable totaling \$16.4 million relating to Hurricanes Katrina, Rita and Wilma and \$10.9 million in relation to subprime mortgage developments. Our estimate of our reinsurance recoverable balance associated with these losses is based on currently available information, claim notifications received to date, industry loss estimates, output from industry models, a detailed review of affected ceded reinsurance contracts and an assessment of the credit risk to which the Company is subject. The actual amount of future loss receipts relating to these loss events may vary significantly from this estimate.

The average credit rating of the Company's reinsurers as of December 31, 2007 is "A" (excellent) by A.M. Best. As of December 31, 2007, the losses and loss adjustment expenses recoverable from reinsurers balance in the consolidated balance sheet included approximately 34.6% due from Everest Reinsurance Ltd., a reinsurer rated "A+" (superior) by A.M. Best.

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The following table lists our largest reinsurers measured by the amount of losses and loss adjustment expenses recoverable at December 31, 2007 and the reinsurers' financial strength rating from A.M. Best:

Losses and Loss

Adjustment

Expenses

Recoverable A.M. Best

Rating	(\$ in millions)	Reinsurer	Everest Reinsurance Ltd.	\$ 51.4	A +	Arch
Reinsurance Ltd.	14.3	A	Aspen Insurance Ltd.	11.3	A -	The Toa Reinsurance Company, Ltd.
(Tokyo)	9.9	A	Various Lloyd's syndicates	9.3	A	General Fidelity
7.4	A -	Odyssey America Reinsurance Corporation	5.1	A	Glacier Reinsurance AG	4.3
Peleus Reinsurance Ltd.	4.1	A -	Transatlantic Reinsurance Company	3.9	A +	Allianz Marine
& Aviation Versicherungs AG	1.7	A -	XL Capital Ltd.	1.7	A +	Other Reinsurers Rated A- or
Better	10.6	A -	All Other Reinsurers	5.1	Various	Total
						\$ 148.4

No reinsurers other than those included above accounted for more than 10% of the losses and loss adjustment expense recoverable balance as at December 31, 2007.

Our shareholders' equity was \$350.7 million as of December 31, 2007 compared to \$328.3 million as of December 31, 2006, reflecting an increase of \$22.4 million that was primarily the result of a net income to common shareholders of \$22.4 million for the year ended December 31, 2007.

We have recorded a net deferred income tax benefit of \$5.3 million related to tax operating losses generated in our Lloyd's segment for the year ended December 31, 2007. For the year ended December 31, 2007, our net valuation allowance increased by approximately \$1.8 million, to \$50.9 million. These deferred tax assets were generated primarily from net operating losses. The realization of deferred tax assets is dependent on future taxable income and future reversals of existing taxable temporary differences. Based upon our assessment of historical data and future earnings, it is our belief that it is more likely than not that the \$5.3 million net deferred tax asset established for the U.K. NOL carryforwards will be realized in future periods by Quanta 4000. We will continue to periodically assess the realizability of our net deferred tax asset and adjust the valuation allowance accordingly.

In relation to the U.S. NOL and Irish NOL, due to prior and existing operating losses, we believe that it is more likely than not that the deferred tax asset will not be realized. Accordingly, we have recorded a full valuation allowance against these net deferred tax assets as of December 31, 2007 and 2006.

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The following table shows our capitalization as of December 31, 2007 and December 31, 2006 (in thousands):

				2007	2006	(\$ in thousands)
Debt outstanding:	Revolving credit facility(1)	\$ —	\$ —	Junior subordinated debentures(2)	—	
61,857	Redeemable preference shares:			Redeemable preferred shares (\$0.01 par value; 25,000,000 shares authorized; zero issued and outstanding at December 31, 2007 and 3,130,525 issued and outstanding at December 31, 2006)(3)	—	74,998
	Shareholders' equity:			Common shares (\$0.01 par value; 200,000,000 common shares authorized; 70,133,499 issued and outstanding at December 31, 2007 and 70,008,185 issued and outstanding at December 31, 2006)(4)	701	700
	Additional paid-in capital	582,889	582,578			
Accumulated deficit	(231,399)	(263,830)	Accumulated other comprehensive income	(1,529)	8,888	
Total shareholders' equity	350,662	328,336	Total capitalization	\$ 350,662	\$ 465,191	Total debt to capital ratio(5)
	0 %	29 %				

(1)

Consisted of a secured letter of credit dated October 27, 2006. The total commitment under our letter of credit facility was \$110 million as of December 31, 2007 and was \$240 million as of December 31, 2006. As of December 31, 2007, \$91.6 million of letters of credit were outstanding under this facility. See "Liquidity" below for a discussion of our new credit facility. (2) During the year ended December 31, 2007, we repurchased all of our junior subordinated debentures for an aggregate purchase price of \$54.5 million. We originally issued and sold \$60.0 million of the junior subordinated debentures in private placements. A gain on repurchase of \$4.4 million was recognized, net of repurchase costs of \$0.5 million and write off of original deferred issuance costs of \$1.7 million. (3) During the year ended December 31, 2007, we repurchased all of our Series A preferred shares at a price of \$22.50 per share. The aggregate purchase price for the Series A preferred shares was \$70.4 million which resulted in a gain of \$2.4 million, net of repurchase costs of \$2.2 million and write off of original deferred issuance costs of \$3.3 million. (4) This table does not give effect to warrants, options, restricted shares and performance share units outstanding for 2,542,813, 573,004 and 109,882 at December 31, 2007 compared to 2,542,813, 801,066 and 184,939 at December 31, 2006. (5) The debt to total capital ratio is calculated as the sum of the revolving credit facility, junior subordinated debentures and redeemable preferred shares, or Total Debt, divided by the sum of Total Debt and Total Shareholders' Equity, or Total Capitalization.

Liquidity

Operating Cashflow; Cash and Cash Equivalents

We used net operating cash flow of approximately \$92.8 million during the year ended December 31, 2007, primarily due to the payments during the year of claims and claim expenses, general and administrative expenses partially offset by reinsurance recoverable received. During the same period, net cash of \$209.4 million was provided by receipts from sales of investments, net of purchases, and net cash of \$127.1 million was used in the repurchase of the Series A preferred shares and junior subordinated debentures. Our cash flows from investing activities for the year ended December 31, 2007 provided us with sufficient liquidity to meet operating cash requirements during that period. A description of our cash, cash equivalents, investments and restricted assets is provided in "Financial Condition and Liquidity" above.

Sources of cash

Our sources of cash consist primarily of existing cash and cash equivalents, premiums written, proceeds from sales and redemptions of investment assets, capital or debt issuances, investment

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income, reinsurance recoveries, and, to a lesser extent, our secured bank credit facility and collections of receivables for technical services rendered to third parties. As a result of the A.M. Best rating actions in 2006, the resulting loss of business and business opportunities, our decision to cease writing new business in all our product lines, excluding business written at Lloyd's, cash flows associated with the receipt of premiums written in our run-off segments will continue to decrease substantially. Due to the sale of our interest in Syndicate 4000, the receipt of premiums written by Syndicate 4000 will cease during the first quarter of 2008. A description of our cash, cash equivalents, investments and restricted assets is provided in "Financial Condition and Liquidity" above.

The cash flows from discontinued operations are combined, in the statement of cash flows, with the cash flows from continuing operations within each category. We do not expect the absence of cash flows from our discontinued operations to significantly affect our future liquidity and capital resources.

The A.M. Best rating action discussed above caused a default under our credit facility led by JPMorgan (the "JPMorgan credit facility") during 2006. The lenders waived the default under the JPMorgan credit facility until October 27, 2006 and on that date we entered into a new credit facility described below.

On October 27, 2006, we entered into a Credit Agreement with a syndicate of lenders and ING Bank N.V., London Branch, as the mandated lead arranger, providing for a secured bank letter of credit facility (the "ING credit facility"). The ING credit facility provides for an aggregate commitment of \$240.0 million for a period of three years terminating on October 27, 2009. During the course of the year we reduced the aggregate commitment under the ING facility from \$240.0 million to \$110.0 million at December 31, 2007. Effective February 11, 2008, the ING credit facility was reduced by a further \$15.0 million to \$95.0 million. As of December 31, 2007 we had approximately \$91.6 million of letters of credit outstanding under the ING credit facility.

Under the ING credit facility, the lenders issue from time to time, for the account of the designated subsidiary borrowers, one or more back-to-back letters of credit naming JPMorgan Chase Bank, N.A. as beneficiary in the face amount equal to the face amount of the outstanding letters of credit under the JPMorgan Credit Agreement, and other letters of credit in an aggregate face amount up to the aggregate commitment. The facility is secured by specified investments of the borrowers. Availability for issuances of letters of credit on account of any borrower is based on the amount of eligible investments pledged by the applicable borrower(s) and no material adverse change provisions. Regulatory restrictions will also limit the amount of investments that may be pledged by certain U.S. insurance borrowers and, consequently, the amount available for letters of credit under the facility on account of those borrowers. Quanta Holdings unconditionally and irrevocably guaranteed all of the obligations of our subsidiaries to the lenders under the ING credit facility.

The ING credit facility includes customary representations and warranties, affirmative and negative covenants, and events of default. The ING credit facility has a financial covenant requiring us to maintain a minimum consolidated tangible net worth, as well as covenants restricting our activities, such as the incurrence of additional indebtedness and liens, the sale of assets, and the payment of dividends and other restricted payments.

Uses of cash and liquidity

Some of our insurance and many of our reinsurance contracts contained termination rights that were triggered by the A.M. Best rating action. Some of these insurance and reinsurance contracts also required us to post additional security either through the issuance of letters of credit or the placement of securities in trust under the terms of those insurance or reinsurance contracts. We may also elect to post security under other insurance contracts in order to maintain that business. As of December 31, 2007, we had cash and cash equivalent and investment balances of approximately

\$228.8 million that were available to post as security or place in trust.

In the near term, our other principal cash requirements are expected to be losses and loss adjustment expenses and other policy holder benefits, including those related to policy cancellations and commutations, expenses to implement our run-off plans, including legal, professional, severance

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and incentive payments, other operating expenses, premiums ceded, capital expenditures and taxes. We may also be required or choose to place capital in our operating subsidiaries. Following the sale of Syndicate 4000 we are no longer committed to provide any of the Syndicate's capital requirements for any underwriting years of account.

Quanta Holdings is dependent on dividends and other payments from its operating subsidiaries to satisfy its obligations. The potential for a large claim under one of our insurance or reinsurance contracts means that we may need to make substantial and unpredictable payments within relatively short periods of time. As a result of our decision to cease underwriting or seeking new business and to place most of our remaining specialty insurance and reinsurance lines into orderly run-off, we have incurred substantial costs, including severance payments, in connection with the implementation of changes based on such decision. This decision also involves significant risks that may result in restructuring charges and unforeseen expenses and costs associated with exiting lines of business and complications or delays, including, among others things, the risk of failure. Additionally, we have entered into agreements with Peter D. Johnson and Jonathan J.R. Dodd, and a number of other key employees that provide for specified severance payments in the event of termination without cause or following a change of control. In the event of payout to all employees covered by these agreements, our cash requirements would include payments in an aggregate amount of up to approximately \$5.9 million. Of this amount, \$0.7 million is included within our accounts payable and accrued expenses at December 31, 2007. During the year ended December 31, 2007, we have incurred severance charges of \$0.3 million.

Under the 2007 LTIP, if any participant is involuntarily terminated without cause, then the participant will receive a pro-rata portion of the total amount available to participants under the 2007 LTIP. In the event specified change of control events are completed prior to 2010, participants will become immediately vested in their payouts under the 2007 LTIP and will receive an award based on the share price received by our shareholders in the change of control transaction, plus any dividends previously paid to the shareholders. For the year ended December 31, 2007, the amount expensed in relation to the 2007 LTIP was \$0.6 million.

We expect that our cash requirements for the payment of claims will be significant in future periods as we receive and settle claims, including those relating to the claims for the hurricanes that occurred in 2005.

We incurred an insignificant amount of capital expenditure during the year ended December 31, 2007. As we continue to manage the run-off of our specialty insurance and reinsurance business, we are unable to quantify the amounts of future capital expenditures we may have to incur.

Dividends and Redemptions

Quanta Holdings depends on future dividends and other permitted payments from its subsidiaries to pay any dividends. Approval from regulatory authorities is required and we will continue to work with applicable regulatory authorities to facilitate dividends or capital return from our subsidiaries to Quanta Holdings. Further, our ability to pay dividends is subject to regulatory and contractual constraints, including the terms of the ING credit facility. Working with these regulators will take a long period of time and require the Company to meet many conditions. Following approval from the Bermuda Monetary Authority we declared a dividend of \$1.75 per share or approximately \$122.7 million which is payable on March 28, 2008 to shareholders of record on March 25, 2008.

For additional discussion concerning risks relating to our dividend policy and our holding company structure and its effect on our ability to receive and pay dividends, see "Item 1A.—Risk Factors—Risks Related to the Runoff—Our holding company structure and certain regulatory and other constraints, including our credit facility, affect our ability to pay dividends on our shares and return capital".

Off-Balance Sheet Arrangements

As of December 31, 2007, we do not have any off-balance sheet arrangements with special purpose entities or variable interest entities.

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Posting of Security by Our Non-U.S. Operating Subsidiaries

Our Bermuda and Irish operating subsidiaries are not licensed, accredited or otherwise approved as reinsurers anywhere in the United States. Many U.S. jurisdictions do not permit insurance companies to take credit on their U.S. statutory financial statements for reinsurance to cover unpaid liabilities, such as loss and loss adjustment expense and unearned premium reserves, obtained from unlicensed or non-admitted insurers without appropriate security acceptable to U.S. insurance commissioners. Typically, this type of security will take the form of a letter of credit issued by an acceptable bank, the establishment of a trust, funds withheld or a combination of these elements.

As described under “Liquidity” above we entered into the ING credit facility providing for the issuance of letters of credit for a period of three years terminating on October 27, 2009. Regulatory restrictions also limit the amount of investments that may be pledged by our U.S. insurance borrowers and, consequently, the amount available for letters of credit and borrowings under the facility to those borrowers. As of December 31, 2007 and December 31, 2006, we had approximately \$91.6 million and \$235.4 million of secured letters of credit issued and outstanding under the facility. If we fail to maintain or enter into adequate letter of credit facilities on a timely basis, we may be unable to provide necessary security to cedant companies that have the right to require the posting of additional security by reason of the downgrade of our A.M. Best rating.

As of March 3, 2008, we have approximately \$96.8 million that was pledged as collateral for letters of credit, approximately \$152.5 million held in trust funds for the benefit of ceding companies and to fund our obligations associated with the assumption of an environmental remediation liability, \$37.3 million held in trust funds that are related to our deposit liabilities and \$27.9 million that is on deposit with, or has been pledged to, U.S. state insurance departments.

Some of our insurance and many of our reinsurance contracts contain termination rights that were triggered by the A.M. Best rating downgrade. Some of these insurance and reinsurance contracts also require us to post additional security. As a result, we may be required to post additional security either through the issuance of letters of credit or the placement of securities in trust under the terms of those insurance or reinsurance contracts. We may also elect to post security under other insurance contracts. We currently have net cash and cash equivalent balances of approximately \$22.3 million that are available to post as security or place in trust. However, the distribution of these funds from each of our operating subsidiaries is subject to significant legal, regulatory and compliance requirements.

Critical Accounting Policies and Estimates

Our significant accounting policies are described in Note 2 of our consolidated financial statements.

Our consolidated financial statements contain certain amounts that are inherently subjective in nature and require management to make certain judgments, estimates and assumptions in the application of accounting policies used to determine inherently subjective amounts reported in the consolidated financial statements. The use of different assumptions and estimates could produce materially different estimates of the reported amounts. In addition, if actual events differ materially from management’s assumptions used in applying the relevant accounting policy, there could be a material adverse effect on our results of operations and financial condition and liquidity.

We believe that the following critical accounting policies affect significant estimates used now or to be used in the future in the preparation of our consolidated financial statements.

Premiums Written, Ceded and Earned

Insurance and reinsurance premiums written are earned over the terms of the associated insurance policies and reinsurance contracts in proportion to the amount of insurance protection provided. Typically this results in the earning of premium on a pro rata over time basis over the term of the related insurance or reinsurance coverage. Premiums written on risks attaching reinsurance contracts are recorded in the period in which the underlying policies or risks are expected to incept

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and are earned on a pro rata over time basis over the expected term of the underlying policies. As a result, premiums earned on risks attaching reinsurance contracts usually extend beyond the original term of the reinsurance contract resulting in recognition of premium earnings over an extended period, typically up to 24 months. The term of the insurance or reinsurance coverage provided may be cancelled by the insured or ceding company resulting in a return of written premium.

Premiums written and ceded on certain types of contracts include estimates based on information received from the ceding companies, brokers or insureds. Estimates of written premiums are re-evaluated over the term of the associated contracts as underwriting information becomes available and as actual premiums are reported by the ceding companies, brokers or insureds. Subsequent changes to the premium estimates and cancellations are recorded as adjustments to premiums written in the period in which they become known. Such adjustments to estimated premium may be significant.

Adjustments related to retrospective rating provisions that adjust estimated premiums or acquisition expenses are recognized over contract periods in accordance with the underlying contract terms based on current experience under the contracts. Reinstatement premiums that reinstate coverage limits under pre-defined contract terms are written and earned at the time the associated loss event occurs. The original premium is earned over the remaining exposure period of the contract. Profit commissions are expenses that vary with and are directly related to acquiring new and renewal insurance and reinsurance business. Profit commission accruals are recorded as acquisition costs and are adjusted at the end of each reporting period based on the experience of the underlying contract. No claims bonuses are accrued as a reduction of earned premium and are adjusted at the end of each reporting period based on the experience of the underlying contract. Such adjustments related to retrospective rating provisions, reinstatement premiums, profit commissions and no claims bonuses may be significant.

Ceded reinsurance or retrocessional coverage is used to increase our underwriting capacity and to limit individual and aggregate exposures to risks of losses arising from contracts of insurance or reinsurance that it underwrites. Reinsurance premiums ceded to reinsurers are recorded and earned in a manner consistent with that of the original contracts or policies written and the terms of the reinsurance agreements.

Premiums written and ceded relating to the unexpired periods of coverage or policy terms are recorded on the consolidated balance sheet as unearned premiums and deferred reinsurance premiums.

Prior to commencing our self-managed run-off, in the normal course of operations, we entered into certain contracts that do not meet the risk transfer provisions of Statement of Financial Accounting Standards (“SFAS”) No. 113, “Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts” (“SFAS 113”) for financial reporting purposes either due to insufficient underwriting risk or insufficient timing risk or do not provide the indemnification required for insurance accounting under SFAS No. 60, “Accounting and Reporting by Insurance Enterprises” (“SFAS 60”). For these contracts we follow the deposit method of accounting as prescribed in American Institute of Certified Public Accountants (“AICPA”) Statement of Position 98-7, “Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk” (“SOP 98-7”). The deposit method of accounting requires that the premium we receive or pay, less any explicitly defined fees retained or paid, is accounted for as a deposit asset or a deposit liability on the consolidated balance sheet. Explicitly defined fees retained or paid are deferred and earned to other income in the consolidated statement of operations and according to the nature of, and in proportion to, the product or service provided.

For those contracts that transfer significant underwriting risk only and for reinsurance contracts where it is not reasonably possible that we can realize a significant loss even though it assumes significant insurance risk, the deposit

asset or liability is measured based on the unexpired portion of the coverage provided. The deposit asset or liability is adjusted for any losses incurred or recoverable based on the present value of the expected future cash flows arising from the loss event with the adjustment being recorded in net losses and loss expenses within our results of operations.

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For those contracts that transfer neither significant underwriting risk nor significant timing risk and for contracts that transfer significant timing risk only, the deposit asset or liability is adjusted, and corresponding interest income or expense recognized within our results of operations, by using the interest method to calculate the effective yield on the deposit based on the estimated amount and timing of cash flows. If a change in the actual or estimated timing or amount of cash flows occurs, the effective yield is recalculated and the deposit is adjusted to the amount that would have existed had the new effective yield been applied since the inception of the insurance or reinsurance contract. The adjustment is recorded as interest income or interest expense.

Commutations

We report commutations in accordance with SFAS No. 113, "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts" ("SFAS 113").

As we actively run off our business lines, we seek to mitigate our exposures to historical underwriting risks through early settlement of our obligations to policyholders or ceding companies by entering into commutations or other arrangements. These negotiated commutation agreements eliminate the risk of adverse claim experience as they provide for full and final settlement of all current and future policy obligations with respect to the transaction to which they relate.

A commutation generally results in a single net payment to, or receipt from, a policyholder or ceding company. This payment or receipt settles all applicable outstanding balances with the policyholder or ceding company, including reserves for loss and loss expenses, unearned premiums, reinsurance balances payable, premiums receivable, deferred acquisition costs and funds withheld. Typically, the settlement of existing loss and loss expenses reserves is recorded as a paid claim, and settlement of unearned premiums is recorded as an adjustment to gross written and earned premiums, and acquisition expenses. Net gains or losses arising on commutation arrangements are primarily recorded within either net losses incurred, premiums earned, or a combination of both.

Non-traditional contracts

We wrote non-traditional contracts of insurance and reinsurance that were deemed not to meet risk transfer criteria and accordingly we have accounted for these transactions as deposits held on behalf of clients. During the years ended December 31, 2007, 2006 and 2005, we recognized within other income \$(0.1) million, \$3.5 million and \$2.5 million of fees and revenues relating to non-traditional contracts which were accounted for using the deposit method. If these contracts were deemed to transfer risk, gross premium relating to these contracts would total approximately \$43.5 million, \$87.2 million and \$110.7 million in the years ended December 31, 2007, 2006 and 2005.

In the fourth quarter of 2004, we entered into a surplus relief life reinsurance arrangement with a U.S. insurance company and assumed several life reinsurance contracts, through novation agreements. When we assumed these underlying contracts, the client, who is subject to insurance regulation in the United States and therefore is required to maintain a certain amount of statutory capital, was able to reduce its statutory capital requirements. In exchange for our assumption of the contracts we received a fee. The arrangement, among other things, provides that on certain dates and during specific periods, the client has the right but not the obligation to recapture the life reinsurance contracts we have assumed, provided that the underlying cedants do not reasonably withhold their consent to this recapture. Of the \$(0.1) million, \$3.5 million and \$2.5 million, \$0.1 million, \$0.6 million and \$0.7 million of other income recognized during the years ended December 31, 2007, 2006 and 2005 relate to fees earned from this surplus relief life reinsurance arrangement with a U.S. insurance company that meets our definition of a non-traditional contract. As of December 31, 2007, 2006 and 2005, we provided approximately \$8.4 million, \$10.8 million and \$13.1 million

(unaudited) of statutory surplus relief to the U.S. insurance company under this contract.

We believe the arrangement, including the client's option to recapture, and the assumption of the life insurance contracts constitute one contract with minimal mortality, credit or other insurance or economic risk which results in deposit accounting. If our client does not recapture the underlying

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insurance contracts in the future, we may be viewed as having had the risks described above and, as a result, we could be deemed to have retained life reinsurance risk and, as a result, may be required to account for some or all of the underlying insurance contracts as life insurance, recognizing life premiums written and life benefit reserves in the consolidated statement of operations. If deposit accounting had not been used with respect to this particular arrangement, we would have recognized gross life reinsurance premiums written of approximately \$33.6 million, \$62.6 million and \$16.8 million for the years ended December 31, 2007, 2006 and 2005.

In respect of life reinsurance arrangements written on a coinsurance basis, where investment assets have been transferred to us, such assets have been recorded within our trading investment portfolio. A deposit liability has been recorded in the consolidated balance sheet in accordance with SFAS 97 "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments" for non-risk investment contracts as an interest bearing instrument using the effective yield method. The investments related to the deposit liability are held in trust funds and are pledged to the ceding companies.

In respect of the life reinsurance arrangements written on a modified coinsurance basis, the ceding company's net statutory reserves and assets are withheld and remain legally owned by the ceding company. These modified coinsurance contracts represent "non-cash" financial reinsurance transactions, whereby, in accordance with the contract terms, there are no net cash flows at inception of contracts, nor are there expected to be net cash flows through the life of the contracts, other than our explicitly defined fees. Notional contract assets and liabilities contemplated by the contract terms are partially offset in accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 39 ("FIN 39") "Offsetting of Amounts Related to Certain Contracts" and as such we do not present such assets or deposit liabilities in our consolidated balance sheet.

Certain of our coinsurance and modified coinsurance agreements may contain provisions that qualify as embedded derivatives under Derivatives Implementation Group Issue No. B36 "Embedded Derivatives: Modified Coinsurance Arrangements and Debt Instruments That Incorporate Credit Risk Exposures That Are Unrelated or Only Partially Related to the Creditworthiness of the Obligor under Those Instruments" ("DIG Issue B36"). The value of embedded derivatives in these contracts is currently considered immaterial. We monitor the performance of these treaties on a quarterly basis. Significant adverse performance or changes in our expectations of future cashflows on these treaties could result in losses associated with the embedded derivative.

Included in other income is \$1.5 million, \$0.6 million and \$0.2 million of other income recognized during the years ended December 31, 2007, 2006 and 2005 relate to explicitly defined margins on one short duration contract written by our specialty reinsurance segment that did not meet the risk transfer provisions of SFAS 113. The contract was commuted during the year ended December 31, 2007, resulting in a gain on commutation of \$0.8 million, but was originally written on a funds withheld basis, such that a deposit liability of \$21.3 million and \$21.7 million at December 31, 2006 and 2005 was recorded and was equal to a funds withheld asset according to the contract terms. In accordance with FIN 39, the funds withheld asset and the deposit liability have been offset in the consolidated balance sheet.

Also included in other income is an amount of \$3.7 million (net of commission of \$0.8 million), which has been recorded as the return of all fee income received to date as a result of our decision to rescind a surplus life relief insurance contract. As of December 31, 2007, 2006 and 2005, we have provided approximately \$29.3 million, \$30.1 million and \$33.2 million (unaudited) of statutory surplus relief to a U.S. insurance company under this contract. This contract is further discussed in Note 13(h) to the financial statements.

The remaining other income is derived from a limited number of non-traditional contracts relating to revenues earned on reinsurance contracts accounted for as deposits. Although these contracts did possess some underwriting and timing risks as prescribed by SFAS No. 113, we do not believe we are exposed to a reasonable possibility of significant loss.

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Acquisition Expenses and Ceding Commission Income

Acquisition expenses are policy issuance related costs that vary with and are directly related to the acquisition of insurance and reinsurance business, and primarily consist of commissions, third party brokerage and insurance premium taxes. Ceding commission income consists of commissions we receive on business that we cede to our reinsurers. Acquisition expenses also include the sliding scale net contingent commissions relating to one program which generate either additional net commission expense or net commission returns based on loss ratio development. Acquisition expenses and commission income are recorded and deferred at the time the associated premium is written or ceded and are subsequently amortized in earnings as the premiums to which they relate are earned or expensed. Acquisition expenses are reflected in the consolidated statement of operations net of ceding commission income from reinsurers. Acquisition costs relating to unearned premiums are deferred in the consolidated balance sheet as deferred acquisition costs and reported net of commission income relating to deferred reinsurance premiums ceded.

Net deferred acquisition costs are carried at their estimated realizable value and are limited to the amount expected to be recovered from future net earned premiums, after deducting anticipated losses and other costs and considering anticipated investment income. Any limitation is referred to as a premium deficiency.

Reinsurance Recoverables

Reinsurance recoverable, under the terms of ceded reinsurance contracts, includes loss and loss adjustment expenses recoverable and deferred reinsurance premiums. We estimate loss and loss adjustment expenses recoverable using methodologies and assumptions consistent with those used in estimating reserves for losses and loss adjustment expenses. The estimation of loss and loss adjustment expenses recoverable is a significant judgment made by management and is inherently subject to significant uncertainties. We are subject to credit risk with respect to the reinsurance ceded because the ceding of risk does not relieve us from our original obligations to our insureds. To the extent reinsurers default, we must settle these obligations without the benefit of reinsurance protection. Failure of our reinsurers to honor their obligations could result in credit losses. We establish allowances for amounts recoverable that are considered potentially uncollectible from our reinsurers. The valuation of this allowance for uncollectible reinsurance recoverable includes a review of the credit ratings of the reinsurance recoverables by reinsurer, an analysis of default probabilities as well as identifying whether coverage issues exist. These factors require management judgment and the impact of any adjustments to those factors is reflected in net income in the period that the adjustment is determined.

Income Taxes

Income taxes have been recognized in accordance with the provisions of SFAS No. 109, "Accounting for Income Taxes", on those operations that are subject to income taxes. Deferred tax assets and liabilities result from temporary differences between the carrying amounts of existing assets and liabilities recorded in the consolidated financial statements and their respective tax bases. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of operations in the period that includes the enactment date. A valuation allowance for a portion or all of deferred tax assets is recorded as a reduction to deferred tax assets if it is more likely than not that such portion or all of such deferred tax assets will not be realized.

We adopted the provisions of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109" ("FIN 48") on January 1, 2007. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on derecognition, classification, interest and penalties, accounting in

interim periods, disclosure, and transition. During May 2007, the FASB issued FASB Staff Position No. FIN 48-1, "Definition of Settlement in FASB Interpretation No.48" ("FSP FIN 48-1"). FSP FIN 48-1 amends FIN 48 to provide guidance on how an enterprise should determine whether a tax position is

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effectively settled for the purpose of recognizing previously unrecognized tax benefits. The adoption of FIN 48 and FSP FIN48-1 has not affected our financial position or results of operations.

Investments

In February 2007, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities” (“SFAS 159”). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value, with changes in fair value recorded in net income. The statement is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. Early adoption was permitted as of the beginning of a fiscal year that begins on or after November 15, 2006, provided the entity also elects to apply the provisions of FASB Statement No. 157, “Fair Value Measurements” (“SFAS 157”). SFAS 157 established a hierarchy for inputs in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs are used when available.

Commencing January 1, 2007, we elected for early adoption of the fair value option for all fixed maturity investments and therefore also adopted SFAS 157. We elected to early adopt the fair value option to simplify the accounting, as this adoption reduces the burden of the monitoring of differences between the cost and fair value of our investments, including the assessment as to whether declines in value are temporary in nature, mitigates a potential volatility in earnings and further removes an element of management judgment. SFAS 159 has been applied to our entire investment portfolio but not to any other assets or liabilities. Prior to January 1, 2007, investments were considered “Available for Sale” and were carried at fair value, except those investments held in relation to our deposit liabilities. This adoption requires all investments to now be reported as “Trading” under SFAS 115, although it does not amend the carrying value of fixed maturity investments as they continue to be carried at fair value. As a result all unrealized gains and losses, amounting to approximately \$10.0 million, in our investment portfolio were reclassified from accumulated other comprehensive loss within shareholders’ equity on the consolidated balance sheets to retained earnings as of January 1, 2007.

Following the adoption of SFAS 159, all investments are now classified as “Trading” and all subsequent changes to the fair value of the investment portfolio are recorded as net gains (losses) on investments in the consolidated statements of operations. Prior to January 1, 2007, unrealized gains and losses were included within accumulated other comprehensive income as a separate component of shareholders’ equity.

Realized gains and losses on sales of investments continue to be determined on a first-in, first-out basis. Net investment income includes interest income on fixed maturity investments, recorded when earned, and the amortization of premiums and discounts on investments, net of investment management and custody expenses.

Beginning January 1, 2007, assets and liabilities recorded at fair value in the consolidated balance sheet are categorized based upon the level of judgment associated with the inputs used to measure their fair value. An asset or a liability’s categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation. Hierarchical levels—defined by SFAS 157 and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities—are as follows:

- Level I —

Valuations based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.

• Level II — Valuations based on quoted prices in active markets for similar assets or liabilities, quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

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- Level III —

Valuations based on inputs that are significant to the overall fair value measurement but are not observable. These are generally company generated inputs and are not market based inputs.

Prior to adoption of SFAS 159, we periodically reviewed our investments to determine whether an impairment, being a decline in fair value of a security below its amortized cost, was other than temporary. If such a decline was classified as other than temporary, we wrote down, to fair value, the impaired security resulting in a new cost basis of the security and the amount of the write-down was charged to the consolidated statement of operations as a realized loss. Some of the factors that we considered in determining whether an impairment was other than temporary included (i) the amount of the impairment, (ii) the period of time for which the fair value has been below the amortized cost, (iii) specific reasons or market conditions which could affect the security, including the financial condition of the issuer and relevant industry conditions or rating agency actions, and (iv) our ability and intent to hold the security for sufficient time to allow for possible recovery.

Prior to the adoption of SFAS 159 and due to our decision to place our insurance and reinsurance lines, except Syndicate 4000, into orderly run-off, we concluded that we may no longer have the ability or intent to hold our securities for a sufficient period of time to allow recovery. Accordingly, during the years ended December 31, 2006 and 2005, we recorded \$16.9 million and \$10.2 million in other than temporary impairment losses. The realization of these losses represents the maximum amount of potential losses in our investment securities if we sold all of these securities at the time the impairments were recorded and was primarily attributable to changes in interest rates and not changes in credit quality. As a result of this decision, the affected investments were reduced to their estimated fair value, which became their new cost basis. The recognition of the losses had no effect on our shareholders' equity, the market value of our investments, our cash flows or liquidity.

Short-term investments include highly liquid debt instruments and commercial paper that are generally due within one year of the date of purchase and are held as part of the investment portfolios that are managed by independent investment managers.

Capitalization of Software Costs

We capitalize software costs when the preliminary project stage is completed and management commits to fund the software project which it deems probable will be completed and used to perform the intended function. This policy is in accordance with AICPA Statement of Position 98-1 "Accounting for the costs of computer software developed or obtained for internal use" ("SOP 98-1"). Software costs that are capitalized include only external direct costs of materials and services consumed in developing, or obtained for internal use computer software.

Capitalization of costs ceases as soon as the project is substantially complete and ready for its intended purpose. The carrying value of software costs is reviewed by us whenever events or changes in circumstances indicate that its carrying amount may not be recoverable, and a loss is recognized when the value of estimated undiscounted cash flow benefit related to the asset falls below the unamortized cost.

Reserve for losses and loss adjustment expenses

We establish reserves for losses and loss expenses for estimates of future amounts to be paid in settlement our ultimate liabilities for claims arising under our contracts of insurance and reinsurance that have occurred at or before the consolidated balance sheet date. The estimation of ultimate loss and loss expense liabilities is a significant judgment made by management and is inherently subject to significant uncertainties.

Our loss reserves fall into two categories: case reserves for reported losses and loss expenses and reserves for losses and loss expenses incurred but not reported, or IBNR reserves. Case reserves are based initially on claim reports received from insureds, brokers or ceding companies, and may be supplemented by our claims professionals with estimates of additional ultimate settlement costs. IBNR reserves are estimated by management using generally accepted statistical and actuarial techniques

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and are reviewed by independent actuaries. In applying these techniques, management uses estimates as to ultimate loss emergence, severity, frequency, settlement periods and settlement costs. In making these estimates, we rely on the most recent information available, including pricing information, industry information and on our historical loss and loss expense experience.

As of December 31, 2007 the primary reserving method used by us to estimate the ultimate cost of losses for our specialty reinsurance run-off lines and professional, environmental, fidelity and technical risk property specialty insurance run-off business lines was the Bornhuetter-Ferguson actuarial method for which we use both historical paid and historical reported data. The Bornhuetter-Ferguson actuarial method utilizes the expected loss (initial expected loss and loss expense ratio multiplied by earned premium) multiplied by loss development factors derived by our internal actuaries from our own actual loss and loss expense experience in each product line and also from industry statistics. Our initial expected loss and loss expense ratio for the specialty reinsurance business lines is derived from loss exposure information provided by brokers and ceding companies and from loss and loss expense ratios established during the pricing of individual contracts. Our initial expected losses and loss expense ratios selected for the professional, environmental, fidelity and technical risk property specialty insurance lines are based on benchmarks derived by our underwriters and actuaries during the initial pricing of the business and from comparable market information. These benchmarks are then adjusted for any rating increases and changes in terms and conditions that have been observed in the market.

Since we ceased writing business in 2006, we believe that the reported and paid loss data in our specialty runoff business is mature enough to further rely on the following actuarial methods: Reported Development Method, Paid Development Method, Paid Bornhuetter-Ferguson Method and Reported Bornhuetter-Ferguson Method. In our Lloyd's business, for the non-subprime exposure, for the 2006 underwriting year and prior we relied on the Bornhuetter-Ferguson actuarial method and for 2007 underwriting year we used an expected loss ratio methodology. For the subprime exposure, multiple methods were used to derive an estimate of the ultimate cost of losses. For example one method used was related to the industry estimates of ultimate losses and calculating our ultimate cost of losses based on Syndicates 4000's share of the market premium. Another method considered an internal loss exposure analysis commissioned by Syndicate 4000 based on the risk characteristics of the Syndicate 4000 portfolio of policies written.

Even though our reserving techniques represent a reasonable and appropriate basis for estimating ultimate claim costs and management believes that the reserves for losses and loss expenses are sufficient to cover claims from losses occurring up to the consolidated balance sheet date, ultimate losses and loss expenses may be subject to significant volatility as a result of significant uncertainties. These uncertainties are driven by many variables that are difficult to quantify. These uncertainties include, for example, the period of time between the occurrence of an insured loss and actual settlement, fluctuations in inflation, prevailing economic, social and judicial trends, legislative changes, internal and third party claims handling procedures, the lack of complete historical data on which to base loss expectations and the run-off status of our operations, except Syndicate 4000. Accordingly, ultimate liabilities may differ materially from the amounts recorded in the consolidated financial statements.

The estimation of unpaid loss liabilities will be affected by the type or structure of the policies that we have written. For specialty insurance run-off business, we often assumed risks for which claims experience will tend to be frequency driven. As a result, historical loss development data may be available and traditional actuarial methods of loss estimation may be used. Conversely, the available amount of relevant loss experience used to quantify the emergence, severity and payout characteristics of loss liabilities is limited for policies written where we expect that potential losses will be characterized by lower frequency but higher severity claims.

The estimation of unpaid loss liabilities will also vary in subjectivity depending on the lines or classes of business involved. Short-tail business describes lines of business for which losses become known and paid in a relatively short period of time after the loss actually occurs. Typically, there will be less variability in the estimates of ultimate amount of losses from claims incurred in the short-tail

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lines that we wrote such as property, marine, and aviation. Long-tail business describes lines of business for which actual losses may not be known for some time or for which the actual amount of loss may take a significantly longer period of time to emerge or develop. We wrote casualty, professional and environmental lines of business that are generally considered longer tail in nature. Due to the fact that loss emergence and settlement periods can be many years in duration, these lines of business will have more variability in the estimates of their loss and loss expense reserves.

We continually review and adjust our reserve estimates and reserving methodologies taking into account all currently known information and updated assumptions related to unknown information. Loss and loss expense reserves established in prior periods are adjusted in current operations as claim experience develops and new information becomes available. Any adjustments to previously established reserves may significantly impact current period underwriting results and net income by reducing net income.

Environmental liabilities assumed, technical services remediation revenues and costs

We have assumed environmental liabilities in exchange for remediation fees and contracts to perform the required remediation in accordance with the underlying remediation agreements.

We estimate our initial and ongoing ultimate liabilities for environmental remediation obligations based upon actual experience, past experience with similar remediation projects, technical engineering examinations of the contaminated sites and state, local and federal guidelines. However, there can be no assurance that actual remediation costs will not significantly differ from the estimated amounts.

As of December 31, 2007 and 2006, environmental liabilities assumed includes two environmental remediation projects, for which estimated liabilities of \$1.5 million and \$3.3 million have been recorded. The assumed environmental remediation obligations for the projects are contractually defined pursuant to a site specific remediation plan.

The amount of consideration received for the assumption of remediation liabilities in excess of the expected environmental remediation liability is initially deferred and recorded in deferred income on the consolidated balance sheet and subsequently recognized in earnings over the remediation period using the cost recovery or percentage-of-completion method. These methods are based on the ratio of remediation expenses actually incurred and paid to total estimated remediation costs. As of December 31, 2007 and 2006, we had deferred approximately \$0.1 million and \$0.2 million of technical services remediation revenues. Anticipated remediation losses, if any, are recorded in the period in which we become aware of such losses.

Stock-Based Compensation

We have a long-term stock-based incentive plan (the "Incentive Plan"), which is described more fully in Note 17. Prior to January 1, 2006, we accounted for the Incentive Plan under the recognition and measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25") and related Interpretations, as permitted by FASB Statement No. 123, Accounting for Stock-Based Compensation ("SFAS 123"). No stock-based employee compensation cost was recognized in the Statement of Operations for the year ended December 31, 2005, as all options granted under the Incentive Plan had an exercise price equal to the market value of the underlying common stock on the date of grant. Effective January 1, 2006, we adopted the fair value recognition provisions of FASB Statement No. 123(R), Share-Based Payment ("SFAS 123(R)"), using the modified-prospective-transition method. Under that transition method, compensation cost recognized in 2006 also includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value

estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). Results for prior periods have not been restated.

As a result of adopting SFAS 123(R) on January 1, 2006, our net income for the year ended December 31, 2007 is \$0.3 million lower and the net loss for the year ended December 31, 2006, is

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\$0.7 million higher than if it had continued to account for share-based compensation under APB 25. Basic and diluted income (loss) per share for the years ended December 31, 2007 and December 31, 2006, would have been \$0.33 and \$(0.92), if we had not adopted SFAS 123(R), compared to reported basic and diluted loss per share of \$0.32 and \$(0.93).

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS 123 to options granted under the Company's stock option plans in the period prior to January 1, 2006. For purposes of this pro forma disclosure, the value of the options is estimated using a Black-Scholes-Merton option-pricing formula and amortized to expense over the options' vesting periods.

	Year ended	
December 31,		
2005 (\$ in thousands)	As reported	Pro forma
Stock compensation expense	\$ —	\$ (3,028)
Additional stock-based employee compensation expense determined under fair value based method	(3,028)	(3,028)
Net loss	As reported	Pro forma
	\$ (105,952)	\$ (108,980)
Additional stock-based employee compensation expense determined under fair value based method	(3,028)	(3,028)
Basic loss per share	As reported	Pro forma
	\$ (1.85)	\$ (1.91)
Diluted loss per share	As reported	Pro forma
	\$ (1.85)	\$ (1.91)

Included in the pro-forma stock-based employee compensation expense for the year ended December 31, 2005 is \$1.0 million related to the accelerated vesting of 649,830 options granted to the Company's former Chief Executive Officer that were modified upon his resignation.

Derivative Instruments and Hedging Activities

We engage in certain derivative related activities and have adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133") and SFAS 149, "Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities."

Although we do not currently hold any derivative instruments, we expect we would primarily enter into investment related derivative transactions, as permitted by our investment guidelines, and typically for the purposes of managing investment duration, interest rate and foreign currency exposure, and enhancing total investment returns. We may also, as part of our business, enter into derivative transactions for the purpose of replicating approved investment, insurance or reinsurance transactions that meet our investment or our underwriting guidelines. As of December 31, 2004, we held in our available-for-sale fixed maturity portfolio a mortality-risk-linked security for which the repayment of principal was dependent on the performance of a specified mortality index. The component of the bond that was linked to the mortality index had been determined, under SFAS 133, to be an embedded derivative that was not clearly and closely related to its host contract (a debt

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security) and was therefore bifurcated and accounted for as a derivative under SFAS 133. This security was sold during the year ended December 31, 2005. We have not designated any of our derivative instruments as hedging instruments.

We recognize all standalone derivative instruments as either other assets or liabilities and embedded derivatives as part of their host instruments in our consolidated balance sheet and we measure all derivative instruments at their fair value. The fair values of derivative instruments are based on market prices and equivalent data provided by independent third parties. When market data is not readily available, we use analytical models to estimate the fair values of these instruments based on their structure, terms and conditions and prevailing market conditions. We recognize changes in the fair value of derivative instruments in our consolidated statement of operations in other income. The nature of derivative instruments and estimates used in estimating their fair value, changes in fair value of derivatives and realized gains and losses on settled derivative instruments may create significant volatility in our results of operations in future periods.

DIG Issue B36 indicates that our life financial reinsurance contracts where we notionally receive a financial instrument with an investment return based on our underlying referenced pool of assets may contain an embedded derivative that must be bifurcated and accounted for in accordance with SFAS 133 since the economic characteristics are not clearly and closely related to the host instrument. Although our life financial reinsurance arrangements may contain embedded derivatives we believe that due to the terms of these contracts, including the experience refund provisions contained within the treaties, the value of embedded derivatives contained in these contracts is currently considered to be immaterial.

In September 2006, the FASB issued FASB Statement No. 155, "Accounting for certain hybrid financial instruments" ("SFAS 155"). SFAS 155 amends FASB Statements No. 133, ("Accounting for Derivative Instruments and Hedging Activities," and No. 140, ("Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". SFAS 155 was effective for financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of SFAS 155 on January 1, 2007 has not affected our financial position or results of operations.

Incentive Plans

During the year ended December 31, 2004, we adopted an Annual Variable Cash Compensation Plan (the "Annual Variable Cash Incentive Plan") which was generally available to employees in 2004 and 2005. Awards paid under this plan were dependent on performance measured at an individual and line of business level for the years ended December 31, 2004 and 2005. In general, the Annual Variable Cash Incentive Plan provided for an annual bonus award to employees that was based on a sharing of profit in excess of a minimum return on capital to shareholders (as calculated under the Annual Variable Cash Incentive Plan). Profit for each calendar year was measured by estimating the ultimate net present value of after-tax profit generated from business during that calendar year and, up until December 31, 2006, was re-estimated on an annual basis through the vesting period. Annual Incentive Plan awards for 2004 and 2005 have now fully vested and all amounts have been paid.

Following the determination to engage in a self-managed run-off, employees will generally receive a bonus based on individual performance that was comprised of a guaranteed and variable element for the 2006 financial year and that is 100% discretionary for the 2007 financial year. The bonus based on the 2006 financial year was paid in the second quarter of 2007. The bonus based on the 2007 financial year is expected to be paid on or around March 15, 2008.

During the first quarter of 2007, we adopted the 2007 Long Term Incentive Plan (the “2007 LTIP”). The 2007 LTIP is intended to motivate and reward our Chief Executive Officer, Chief Financial Officer and certain key employees for the successful management of the run-off of the business and insurance operations. The 2007 LTIP is also intended to help us retain certain key employees by providing benefits that do not vest for up to three years except in the event of a change of control or termination of a participant’s employment by us without cause, or due to death,

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permanent disability or normal retirement. Under the 2007 LTIP, if any participant voluntarily terminates his or her employment (other than by retirement) or that person is terminated for cause prior to December 31, 2009, the entire award will be forfeited by that participant. If any participant is involuntarily terminated without cause, then the participant will receive a pro-rata portion of the total amount available to participants under the 2007 LTIP. In the event specified change of control events are completed prior to 2010, participants will become immediately vested in their payouts under the 2007 LTIP and will receive an award based on the share price received by our shareholders in the change of control transaction, plus any dividends previously paid to the shareholders.

Expenses related to the Annual Variable Cash Incentive Plan and the 2007 LTIP awards are recognized by applying provisions of FASB Statement No. 123(R), "Share-Based Payment" ("SFAS 123(R)"). We continually review and adjust our provisions for Annual Variable Cash Incentive Plan awards, 2007 LTIP awards and other bonus awards by taking into account known information and updated assumptions related to unknown information. Award provisions are an estimate and amounts established in prior periods are adjusted in current operations as new information becomes available. Any adjustments to previously established provisions or the establishment of new provisions may significantly impact current period results and net income. We expense the vested portion of the 2007 LTIP plan using the fair value recognition provisions of SFAS 123(R). In order to do this we utilize the Black-Scholes valuation model which uses various assumptions, including stock price volatility and interest rates.

Recent Accounting Pronouncements

See Note 2(y) to the consolidated financial statements which are included in "Item 8. Financial Statements and Supplementary Data" for a discussion of recent accounting pronouncements.

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Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Market risk can be described as the risk of change in fair value of a financial instrument due to changes in interest rates, creditworthiness, foreign exchange rates or other factors. We are exposed to potential loss from these factors. Our most significant financial instruments are our investment assets which consist primarily of fixed maturity securities and cash equivalents that are denominated in both U.S. and foreign currencies. External investment professionals manage our investment portfolios in accordance with our investment guidelines. Our investment guidelines also permit our investment managers to use derivative instruments in very limited circumstances. We will seek to mitigate market risks by a number of actions, as described below.

Derivative Valuation Risk

Subject to Board approval, our derivative policy permits the use of derivatives to manage our portfolio's duration, yield curve, currency exposure, credit exposure, exposure to volatility and to take advantage of inefficiencies in derivatives markets. We may also enter into derivative transactions (1) to hedge capital market risks that may be present in our contracts of insurance or reinsurance and (2) as replication transactions which we define as a set of derivative, insurance and/or securities transactions that, when combined, produce the equivalent economic result of an investment security or insurance or reinsurance contract that meets our investment or underwriting guidelines.

We utilize derivative instruments only when we believe the terms and structure of the contracts are thoroughly understood and its total return profile and risk characteristics can be fully analyzed. Also, any single derivative or group of derivatives in the aggregate cannot create risk characteristics that are inconsistent with our overall risk profile and investment portfolio guidelines.

As of December 31, 2007 we did not hold any derivative instruments in our investment portfolio.

Foreign Currency Risk and Functional Currency

Our reporting currency is the U.S. dollar. Although we have not experienced any significant net exposures to foreign currency risk, we expect that in the future our exposure to market risk for changes in foreign exchange rates will be concentrated in our investment assets, investments in foreign subsidiaries, premiums receivable and insurance reserves arising from known or probable losses that are denominated in foreign currencies. We generally manage our foreign currency risk by maintaining assets denominated in the same currency as our insurance liabilities resulting in a natural hedge or by entering into foreign currency forward derivative contracts in an effort to hedge against movements in the value of foreign currencies against the U.S. dollar. These contracts are not designated as specific hedges for financial reporting purposes and therefore realized and unrealized gains and losses on these contracts are recorded in income in the period in which they occur. These contracts generally have maturities of three months or less. A foreign currency forward contract results in an obligation to purchase or sell a specified currency at a future date and price specified at the time of the contract. Foreign currency forward contracts will not eliminate fluctuations in the value of our assets and liabilities denominated in foreign currencies but rather allow us to establish a rate of exchange for a future point in time. We have not and do not expect to enter into such contracts with respect to a material amount of our assets or liabilities.

Our non-U.S. subsidiaries maintain both assets and liabilities in their functional currencies, principally Euro and Sterling. Assets and liabilities denominated in foreign currencies are exposed to changes in currency exchange rates. Exchange rate fluctuations in Euro and sterling functional currencies against our U.S. dollar reporting currency are reported as a separate component of other comprehensive income (loss) in shareholders' equity. Foreign exchange risk

associated with non-US dollar functional currencies of our foreign subsidiaries is reviewed as part of our risk management process and we employ foreign currency risk management strategies, as described above, to manage our exposure. Exchange rate fluctuations against non-U.S. dollar functional currencies may materially impact our consolidated statement of operations and financial position.

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Our investment guidelines limit the amount of our investment portfolio that may be denominated in foreign currencies to 20% (as measured by market value). Furthermore, our guidelines limit the amount of foreign currency denominated investments that can be held without a corresponding hedge against the foreign currency exposure to 5% (as measured by market value). As of December 31, 2007, our investment portfolio included \$48.9 million, or 7.5%, of our total net invested assets, of securities that were denominated in foreign currencies and were purchased on behalf of Syndicate 4000, in which we sold our interest in February 13, 2008. These securities were all rated AAA. At December 31, 2007, the net fair market value of foreign currency forward contracts relating to foreign currency denominated investments was zero.

Interest Rate Risk

Our exposure to market risk for changes in interest rates is concentrated in our investment portfolio. Our investment portfolio primarily consists of fixed income securities. Accordingly, our primary market risk exposure is to changes in interest rates. Fluctuations in interest rates have a direct impact on the market valuation of fixed income securities. As interest rates rise, the market value of our fixed-income portfolio falls, and the converse is also true.

Our strategy for managing interest rate risk includes maintaining a high quality investment portfolio that is actively managed by our managers in accordance with our investment guidelines in order to balance our exposure to interest rates with the requirement to tailor the duration, yield, currency and liquidity characteristics to the anticipated cash outflow characteristics of claim reserve liabilities. As of December 31, 2007, assuming parallel shifts in interest rates, the impact of an immediate 100 basis point increase in market interest rates on our net invested assets, including cash and cash equivalents, of approximately \$801.7 million would have been an estimated decrease in market value of approximately \$15.1 million, or 1.9%, and the impact on our net invested assets, including cash and cash equivalents, under management by third-party investment managers of an immediate 100 basis point decrease in market interest rates would have been an estimated increase in market value of approximately \$13.0 million, or 1.6%.

As of December 31, 2007, our investment portfolio included AAA rated mortgage-backed securities with a market value of \$163.9 million, or 25.3%, excluding trading investments related to deposit liabilities. As with other fixed income investments, the fair market value of these securities fluctuates depending on market and other general economic conditions and the interest rate environment. Changes in interest rates can also expose us to prepayment and extension risks on these investments. In periods of declining interest rates, the frequency of mortgage prepayments generally increase as borrowers seek to refinance at a lower interest rate cost. Mortgage prepayments result in the early repayment of the underlying principal of mortgage-backed securities requiring us to reinvest the proceeds at the then current market rates. When interest rates increase, these assets are exposed to extension risk, which occurs when holders of underlying mortgages reduce the frequency on which they prepay the outstanding principal before the maturity date and delay any refinancing of the outstanding principal.

Credit Risk

We have exposure to credit risk primarily as a holder of fixed income securities. This risk is defined as the default or the potential loss in market value resulting from adverse changes in the borrower's ability to repay the debt. Our risk management strategy and investment policy is to invest in debt instruments of high credit quality issuers and to limit the amount of credit exposure with respect to particular ratings categories and to any one issuer. We attempt to limit our overall credit exposure by purchasing fixed income securities that are generally rated investment grade by Moody's Investors Service, Inc. and/or S&P. Our investment guidelines require that the average credit quality of our portfolio will be Aa3/AA- and that no more than 5% of our investment portfolio's market value shall be invested in securities rated below BBB-/Baa3. We also limit our exposure to any single issuer to 5% or less of our portfolio's market value

at the time of purchase, with the exception of U.S. government and agency securities. As of December 31, 2007, the average credit quality of our investment portfolio was AAA, and all of the fixed income securities held were investment grade.

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Our portfolio of investment grade fixed maturity investments includes mortgage-backed and asset-backed securities and collateralized mortgage obligations. These types of securities have cash flows that are backed by the principal and interest payments of a group of underlying mortgages or other receivables. During 2007, delinquency and default rates have increased on these types of securities, and particularly on securities backed by subprime mortgages. Generally, subprime mortgages are considered to be those made to borrowers who do not qualify for market interest rates for one or more possible reasons, such as a low credit score, a limited or lack of credit history or a lack of earnings documentation. As a result of the increasing default rates of subprime borrowers, there is a greater risk of defaults on mortgage-backed and asset-backed securities and collateralized mortgage obligations, especially those that are non-investment grade. Therefore, fixed maturities securities backed by subprime mortgages have exhibited significant declines in fair value and liquidity. These factors combined with the contraction in liquidity in the principal markets for these securities makes the estimate of fair value increasingly uncertain. The fair values of our holdings in securities exposed to subprime borrowers are generally not based on quoted prices for identical securities, but are based on model-derived valuations from our independent pricing sources in which significant inputs and significant value drivers are observable in active markets. Should we need to liquidate these securities within a short period of time, the actual realized proceeds may be significantly different from the fair values estimated at December 31, 2007. We believe our exposure to subprime credit risk is limited although there can be no assurance that events in the subprime mortgage sector will not adversely affect the value of our investments. We have determined that a write-down for impairment of these securities is not necessary based on a consideration of relevant factors including prepayment rates, subordination levels, default rates, credit ratings, weighted average life, credit default insurance and historic and current cashflows. Together with our investment managers, we continue to monitor our potential exposure to subprime borrowers and we will make adjustments to the investment portfolio as necessary.

We currently believe that at December 31, 2007 our exposure to subprime mortgages was approximately \$5.4 million, which represents less than one percent of our total cash and investments, and our exposure to Alt-A mortgages was approximately \$6.2 million, which represents less than one percent of our total cash and investments. Alt-A mortgages are considered to be those made to borrowers who do not qualify for market interest rates but who are considered to have less credit risk than subprime borrowers.

We are also exposed to the credit risk of our insurance and reinsurance brokers to whom we make claims payments for insureds and our reinsureds, as well as to the credit risk of our reinsurers and retrocessionaires who assume business from us. As of December 31, 2007, our loss and loss adjustment expenses recoverable from reinsurers balance was \$148.4 million, of which \$1.5 million was due on that date. To mitigate the risk of nonpayment of amounts due under these arrangements, we have established business and financial standards for reinsurer and broker approval, incorporating ratings by major rating agencies and considering the financial condition of the counterparty and the current market information. In addition, we monitor concentrations of credit risk arising from our reinsurers, regularly review our reinsurers' financial strength ratings and obtain letters of credit to collateralize balances due.

We are also exposed to credit risk relating to our premiums receivable balance. As of December 31, 2007, our premiums receivable balance was \$57.9 million. We believe that credit risk exposure related to these balances is mitigated by several factors, including but not limited to credit monitoring controls performed as part of the underwriting process and monitoring of aged receivable balances. In addition, as the majority of our insurance and reinsurance contracts provide the right to partially offset the premiums receivable against losses payable, we believe that the credit risk in this area is substantially reduced.

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Effects of Inflation

We do not believe that inflation has had a material effect on our consolidated results of operations. The effects of inflation could cause the severity of claim costs to increase in the future. Our estimates for losses and loss expenses include assumptions, including those relating to inflation, about future payments for settlement of claims and claims handling expenses. To the extent inflation causes these costs to increase above our estimated reserves that are established for these claims, we will be required to increase reserves for losses and loss expenses with a corresponding reduction in our earnings in the period in which the deficiency is identified. The actual effects of inflation on our results cannot be accurately determined until claims are ultimately settled.

Item 8. Financial Statements and Supplementary Data

Reference is made to Item 15(a) of this annual report for the Consolidated Financial Statements of Quanta Capital Holdings Ltd. and the Notes thereto, as well as the Schedules to the Consolidated Financial Statements.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In connection with the preparation of this annual report, we have carried out an evaluation under the supervision of our management, including our chief executive officer and chief financial officer, of the design and operational effectiveness of our disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) of the Exchange Act as of December 31, 2007.

Based upon that evaluation, our chief executive officer and chief financial officer concluded that, as of December 31, 2007, our disclosure controls and procedures are effective in verifying and allowing information required to be disclosed in reports filed under the Exchange Act to be recorded, processed, summarized and reported within time periods specified in the rules and forms of the Securities and Exchange Commission.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act). Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

There are inherent limitations to the effectiveness of any system of internal control over financial reporting, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of change in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Under the supervision and with the participation of our chief executive officer and chief financial officer, our management conducted an assessment of our internal control over financial reporting as of December 31, 2007, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). Based on that assessment, management has concluded that the Company’s internal control over financial reporting was effective as of December 31, 2007.

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The effectiveness of our internal control over financial reporting as of December 31, 2007 has been audited by Johnson Lambert & Co., LLP, an independent registered public accounting firm, as stated in their report which appears herein.

Changes in Internal Control Over Financial Reporting

In the course of managing our on-going business and executing our self-managed run-off strategy, we review our systems of internal control over financial reporting and make changes to our systems and processes to improve controls and increase operating efficiency and effectiveness. Changes may include such activities as implementing new, more efficient systems, automating manual processes and outsourcing certain activities.

During the quarter ended December 31, 2007, we made the following changes:

- We expanded our database, which was initially implemented during the fourth quarter of 2006, to automate the recording of journal entries for losses and IBNR Reserves and the related asset and liability balances. This expansion improved the effectiveness of several key processes by eliminating manual procedures.
- We outsourced the administration of all of our run-off direct insurance claims processing activities, including programs, to a Third Party Administrator (TPA). These functions had been previously managed by a combination of in-house claims staff and by another TPA. The day-to-day oversight and approval of case reserves and claims settlements over an established threshold are managed by Quanta's VP of Claims. As a result of this consolidation, we expect improved effectiveness, greater consistency and tighter control over these functions.

There were no other significant changes in our internal control over financial reporting during the quarter ended December 31, 2007 that materially affected, or are reasonably likely to affect, our internal control over financial reporting.

Item 9B. Other Information

On March 11, 2008, the Compensation Committee of our Board of Directors approved the award of a bonus of \$175,000 to our Chief Executive Officer and a bonus of \$480,000 to our Chief Financial Officer.

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PART III

Item 10. Directors and Executive Officers of the Registrant and Corporate Governance

Reference is made to the sections entitled “Executive Officers,” “Election of Directors” and “Audit Committee” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders, which sections are incorporated herein by reference.

Reference is made to the section entitled “Section 16(a) Beneficial Ownership Reporting Compliance” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders, which section is incorporated herein by reference.

We have adopted a Code of Business Conduct and Ethics, which applies to all employees, including our chief executive officer and our chief financial officer and principal accounting officer. The full text of our Code of Business Conduct and Ethics is published on our website, at www.quantaholdings.com, under the “Investor Information” caption. We intend to disclose future amendments to, or waivers from, certain provisions of our Code of Business conduct and Ethics by filing a Current Report on Form 8-K with the U.S. Securities and Exchange Commission.

Item 11. Executive Compensation

Information responsive to Item 11 is incorporated by reference from the sections entitled “Compensation Disclosure and Analysis” and “Non-Employee Director Compensation” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders, which sections are incorporated herein by reference.

The portion of the incorporated material from the Compensation Committee Report and references to the independence of directors are not deemed to be “soliciting material” or “filed” with the SEC, are not subject to the liabilities of Section 18 of the Exchange Act and shall not be deemed incorporated by reference into any of the filings previously made or made in the future by our company under the Exchange Act or the Securities Act of 1933, as amended (except to the extent our company specifically incorporates any such information into a document that is filed).

Item 12.

Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information responsive to Item 12 is incorporated by reference from the section entitled “Security Ownership” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders.

Securities Authorized for Issuance Under Equity Compensation Plan

Our shareholders and our board approved our 2003 long term incentive plan in July 2003. The plan is intended to advance our interests and those of our shareholders by providing a means to attract, retain and motivate employees and directors. The compensation committee of our board of directors administers the plan and makes all decisions with respect to the plan. The compensation committee is composed solely of independent directors. The persons eligible to receive awards under the plan include our directors, officers, employees and consultants and those of our affiliated entities.

The plan provides for the grant to eligible employees, directors and consultants of stock options, stock appreciation rights, restricted shares, restricted share units, performance awards, dividend equivalents and other share-based awards. The plan also provides our directors with the opportunity to receive their annual retainer fee for board of director service in shares.

The compensation committee selects the recipients of awards granted under the plan and determines the dates, amounts, exercise prices, vesting periods and other relevant terms of the awards. The maximum number of shares reserved for issuance under the plan is 9,350,000. The maximum number of shares with respect to which options and stock appreciation rights may be granted during a calendar year to any eligible employee is 700,000 shares. The maximum number of shares that may be

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granted with respect to performance awards, restricted shares and restricted share units intended to qualify as performance-based compensation within the meaning of Section 162(m)(4)(C) of the Internal Revenue Code is the equivalent of 250,000 shares during a calendar year to any eligible employee.

The compensation committee determines the pricing of awards granted under the plan as of the date the award is granted. The compensation committee determines the vesting schedule of awards granted under the plan. Recipients of awards may exercise awards at any time after they vest and before they expire, except that no awards may be exercised after ten years from the date of grant. Awards are generally not transferable by the recipient during the recipient's life. Awards granted under the plan are evidenced by either an agreement that is signed by us and the recipient or a confirming memorandum issued by us to the recipient setting forth the terms and conditions of the awards. Award recipients and beneficiaries of award recipients have no right, title or interest in or to any shares subject to any award or to any rights as a shareholder, unless and until shares are actually issued to the recipient.

Plan category Number of securities to be issued upon exercise of outstanding options, warrants and rights
 (a) Weighted average exercise price of outstanding options, warrants and rights
 (b) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))

(c) Equity compensation plans approved by security holders	682,886	(1)	\$ 5.62	3,837,819	Equity
compensation plans not approved by security holders	—	—	—	Total 682,886	\$ 5.62 3,837,819

(1) These

securities were granted to employees and directors between September 3, 2003 and June 7, 2007. Of the 682,886 securities granted, a total of 573,004 are options which have a term of either seven or ten years, vest in equal installments over four years starting on the first anniversary of the grant and range in exercise price from \$1.88 to \$12.50, 14,419 are performance shares which will not vest because the contingency related to attaining an average ROE of 20% per year in the three year period ending on December 31, 2007 was not met and 95,463 are restricted stock awards to directors.

Item 13. Certain Relationships and Related Transactions, and Director Independence

Additional information responsive to Item 13 is incorporated by reference from the section entitled “Certain Transactions” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference from the section entitled “Independent Registered Public Accounting Firm” of the Company’s Proxy Statement for its 2008 Annual General Meeting of Shareholders.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)

Financial Statements

(1) The financial statements and schedules listed in the accompanying index to financial statements and schedules are filed as part of this annual report.

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(2) All other schedules for which provision is made in the applicable accounting regulations of the SEC are not required under the related instructions or are not applicable and therefore have been omitted.

(b) Exhibits
3.1

Memorandum of Association of the Company (incorporated by reference from Exhibit 3.1 to the Company's Registration Statement on Form S-1 (No. 333-111535) filed on December 24, 2003) 3.2 Amended and Restated Bye-Laws of the Company (incorporated by reference from Exhibit 4.2 to the Company's Quarterly Report on Form 10-Q filed on August 9, 2007) 4.1 Memorandum of Association of the Company (included as Exhibit 3.1) 4.2 Amended and Restated Bye-Laws of the Company (included as Exhibit 3.2) 4.3 Form of Common Share Certificate (incorporated by reference from Exhibit 4.1 to the Company's Amendment No. 1 to Registration Statement on Form S-1/A (No. 333-111535) filed on February 13, 2004) 10.1† Quanta Capital Holdings Ltd. 2003 Long Term Incentive Plan, as amended on June 2, 2005 (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated June 8, 2005) 10.2† Form of Non-Qualified Stock Option Agreement for recipients of options under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006) 10.3† Form of Performance-Based Share Unit Agreement for recipients of performance-based share units under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006) 10.4† Employment Agreement of Jonathan J.R. Dodd dated December 22, 2004 (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated July 26, 2005) 10.5 Technical Property Binder of Reinsurance dated November 18, 2005, between Quanta Indemnity Company, Quanta Specialty Lines Insurance Company and Quanta Reinsurance US Ltd. and Arch Reinsurance Ltd. (incorporated by reference from Exhibit 10.30 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006) 10.6 Treaty Property Reinsurance Binder dated November 18, 2005, between Quanta Reinsurance Ltd., Quanta Indemnity Company, Quanta Reinsurance US Ltd., and Quanta Specialty Lines Insurance Company and Arch Reinsurance Ltd. (incorporated by reference from Exhibit 10.31 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006) 10.7 Commutation and Mutual Release Agreement dated November 21, 2005, between Quanta Reinsurance Limited and Houston Casualty Company and certain of its subsidiaries (incorporated by reference from Exhibit 10.32 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006) 10.8† Separation Agreement and General Release, effective January 3, 2006, between Quanta Capital Holdings Ltd. and Tobey J. Russ (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated January 9, 2006)

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	10.9†
Retention Agreement between Quanta Capital Holdings Ltd. and Jonathan J.R. Dodd, dated March 30, 2006 (incorporated by reference from Exhibit 10.35 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10.10†
Form of Restricted Share Agreement for recipients of restricted shares under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.1 to the Company's Amendment No. 1 on Form 10-K/A for the year ended December 31, 2005 filed on March 31, 2006)	10.11†
Separation Agreement and General Release dated July 25, 2006 between the Company and Michael J. Murphy (incorporated by reference from Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 filed on August 9, 2006)	10.12†
Separation Agreement and General Release dated August 7, 2006 between the Company and Gary G. Wang (incorporated by reference from Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 filed on August 9, 2006)	10.13†
Letter Agreement dated September 14, 2006 between the Company and Peter Johnson (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated September 15, 2006)	10.14†
Employment Agreement dated September 14, 2006 between the Company and James J. Ritchie (incorporated by reference from Exhibit 10.2 to the Company's Current Report on Form 8-K dated September 15, 2006)	10.15†
Amendment to Employment Agreement dated March 1, 2007 between the Company and James J. Ritchie (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated March 5, 2007)	10.16
Credit Agreement dated as of July 13, 2004 and Amended and Restated as of July 11, 2005, between Quanta Capital Holdings Ltd., various designated subsidiary borrowers, the lenders party thereto, BNP Paribas, Calyon, New York Branch, Comerica Bank, and Deutsche Bank AG New York Branch, as Co-Documentation Agents, and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated July 15, 2005)	10.17
Fourth Consent and Amendment to Credit Agreement dated October 25, 2006, between Quanta Capital Holdings Ltd., various designated subsidiary borrowers, the lenders party thereto, BNP Paribas, Calyon, New York Branch, Comerica Bank, and Deutsche Bank AG New York Branch, as Co-Documentation Agents, and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference from Exhibit 10.2 to the Company's Current Report on Form 8-K dated October 27, 2006)	10.18
Credit Agreement dated October 27, 2006 among the Company, ING Bank N.V., London Branch, Barclays Private Clients International Limited, Comerica Bank, HSH Nordbank AG, London Branch, designated subsidiary borrowers, and other lenders party thereto (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated October 30, 2006)	10.19
Amended and Restated Retention Agreement dated December 13, 2007 between the Company and Jonathan J.R. Dodd (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated December 13, 2007)	

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	10.20
Stock Purchase Agreement, dated as of February 7, 2008, among Quanta Capital Holdings Ltd., Chaucer Holdings Plc and Quanta 4000 Holding Company Ltd. (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated February 7, 2008)	10.21
Letter Agreement dated March 11, 2008 between the Company and Peter Johnson.	12*
Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Dividends	16
Letter from PricewaterhouseCoopers LLP dated August 15, 2006 (incorporated by reference from Exhibit 16.1 to the Company's Current Report on Form 8-K dated August 17, 2006)	21*
List of subsidiaries of the Company	23*
Consent of Johnson Lambert & Co. LLP	31.1*
Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	31.2*
Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	32.1*
Certification of Principal Executive Officer of Quanta Capital Holdings Ltd. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	32.2*
Certification of Principal Financial Officer of Quanta Capital Holdings Ltd. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	32.2*

* Filed

herewith † Represents a management contract or compensatory plan arrangement

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 13th day of March 2008.

Quanta

Capital Holdings Ltd.

By: /s/ Peter D. Johnson Peter D. Johnson (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report is signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature

Title Date /s/ Peter D. Johnson Chief Executive Officer (Principal Executive Officer) March 13, 2008 Peter D. Johnson /s/ Jonathan J.R. Dodd Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer) March 13, 2008 Jonathan J.R. Dodd /s/ James J. Ritchie Chairman of the Board of Directors March 13, 2008 James J. Ritchie /s/ Robert Lippincott III Deputy Chairman of the Board of Directors March 13, 2008 Robert Lippincott III /s/ Susan F. Cabrera Director March 13, 2008 Susan F. Cabrera /s/ William H. Bolinder Director March 13, 2008 William H. Bolinder /s/ Roland C. Baker Director March 13, 2008 Roland C. Baker /s/ Robert B. Shapiro Director March 13, 2008 Robert B. Shapiro /s/ John C. McKenna Director March 13, 2008 John C. McKenna /s/ Peter D. Johnson Authorized Representative in the United States March 13, 2008 Peter D. Johnson

QUANTA CAPITAL HOLDINGS LTD.

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No. FINANCIAL INFORMATION	
Financial Statements	Reports of Independent Registered Public Accounting Firms
F-2 Consolidated Balance Sheets at December 31, 2007 and 2006	F-5 Consolidated Statements of Operations for the years ended December 31, 2007, 2006 and 2005
F-6 Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2007, 2006 and 2005	F-7 Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2007, 2006 and 2005
F-8 Consolidated Statements of Cash Flows for the years ended December 31, 2007, 2006 and 2005	F-9 Notes to the Consolidated Financial Statements
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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Quanta Capital Holdings Ltd.

We have audited the accompanying consolidated balance sheets of Quanta Capital Holdings Ltd. (the “Company”) as of December 31, 2007 and 2006, and the related consolidated statements of operations, comprehensive income (loss), changes in shareholders’ equity, and cash flows for each of the years in the two-year period ended December 31, 2007. Our audits also included the financial statement schedules listed in Item 15. We also have audited the Company’s internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control— Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the company’s internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Quanta Capital Holdings Ltd. (the “Company”) as of December 31, 2007 and 2006, and the results of its operations

and its cash flows for each of the years in the two-year period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, such financial statement schedules, when considered in relation to the basic financial statements as a whole, present fairly, in all material respects, the information set forth therein. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on

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criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

As discussed in Note 2k, effective January 1, 2007, the Company adopted Statement of Financial Accounting Standards (“SFAS”) 159, “The Fair Value Option for Financial Assets and Financial Liabilities” and SFAS 157, “Fair Value Measurements”.

As described in Note 1 to the consolidated financial statements, except for its operations in the Lloyd’s market, the Company is conducting a self managed run-off of its remaining insurance and reinsurance business. As described in Note 21 to the consolidated financial statements, on February 13, 2008 the Company’s operations in the Lloyd’s market were sold.

/s/ Johnson Lambert & Co. LLP

Falls Church, Virginia
March 13, 2008

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of Quanta Capital Holdings Ltd.

In our opinion, the consolidated statements of operations, comprehensive income (loss), changes in shareholders' equity and cash flows for the year ended December 31, 2005 present fairly, in all material respects, the financial results of operations and cash flows of Quanta Capital Holdings Ltd. and its subsidiaries (the "Company") for the year ended December 31, 2005 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed on the index on page S-1 for the year ended December 31, 2005 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audit. We conducted our audit of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1 to the consolidated financial statements, following losses in the 2005 hurricane season and the resulting A.M. Best rating action, the Company is now conducting a self-managed run-off of its specialty insurance and reinsurance lines.

/s/ PricewaterhouseCoopers

New York, New York

March 31, 2006, except for Notes 3 and 4, as to which the date is March 14, 2007

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QUANTA CAPITAL HOLDINGS LTD.
CONSOLIDATED BALANCE SHEETS

(Expressed in thousands of U.S. dollars except for share and per share amounts)

December 31,

2007 December 31,

2006 Assets	Investments at fair value (amortized cost: December 31, 2007, \$645,205; December 31, 2006, \$838,096)																																																													
	Trading investments	\$ 648,384	\$ 37,273	Available for sale investments	—	809,902																																																								
Total investments at fair value	648,384	847,175	Cash and cash equivalents	22,314	32,894	Restricted cash and cash equivalents	131,013	68,143	Accrued investment income	4,719	6,833	Premiums receivable	57,912	34,587	Funds withheld by cedants	443	25,204	Losses and loss adjustment expenses recoverable	148,440	221,228	Net receivable for investments sold	—	134	Deferred acquisition costs, net	4,988	12,124	Deferred reinsurance premiums	20,011	35,259	Software, property and equipment, net of accumulated depreciation and amortization of \$7,863 (December 31, 2006: \$7,208)	747	1,112	Other intangible assets	7,175	7,350	Net deferred tax asset	5,277	—	Other assets	29,932	37,183	Total assets	\$ 1,081,355	\$ 1,329,226																		
Liabilities	Reserve for losses and loss expenses	\$ 525,088	\$ 623,618	Unearned premiums	95,586	119,197	Environmental liabilities assumed	1,456	3,346	Reinsurance balances payable	40,027	37,070	Net payable for investments purchased	4	—	Accounts payable and accrued expenses	22,144	38,511	Deposit liabilities	36,867	37,014	Deferred income and other liabilities	1,758	5,279	Income taxes payable	5,277	—	Junior subordinated debentures	—	61,857	Contingencies (Note 13h)	2,486	—	Total liabilities	730,693	925,892	Mandatorily redeemable preferred shares	(\$0.01 par value; 25,000,000 shares authorized; 0 issued and outstanding at December 31, 2007 and 3,130,525 issued and outstanding at December 31, 2006)		—	74,998	Shareholders' equity	Common shares	(\$0.01 par value; 200,000,000 shares authorized; 70,133,499 issued and outstanding at December 31, 2007 and 70,008,185 issued and outstanding at December 31, 2006)		701	700	Additional paid-in capital	582,889	582,578	Accumulated deficit	(231,399)	(263,830)	Accumulated other comprehensive (loss) income	(1,529)	8,888	Total shareholders' equity	350,662	328,336	Total liabilities, mandatorily redeemable preferred shares and shareholders' equity	\$ 1,081,355	\$ 1,329,226

The accompanying notes are an integral part of these consolidated financial statements

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QUANTA CAPITAL HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF OPERATIONS

(Expressed in thousands of U.S. dollars except for share and per share amounts)

For the year
ended

December 31,

2007 For the year
ended

December 31,

2006 For the year
ended

December 31,

2005 Revenues

				Gross premiums written	\$ 106,587	\$ 158,729	\$ 608,935	Premiums ceded	
(28,645)	(78,175)	(218,894)	Net premiums written	77,942	80,554	390,041	Change in net		
unearned premiums	9,305	144,745	(25,966)	Net premiums earned	87,247	225,299	364,075		
Technical services revenues	1,707	3,331	19,037	Net investment income	41,900	45,934	27,181		
Net gains (losses) on investments	5,818	(15,945)	(13,020)	Net foreign exchange gains (losses)	850				
(3,790)	331	Gain on repurchase of junior subordinated debentures	4,421	—	—	Other income	447		
3,654	3,561	Total revenues	142,390	258,483	401,165	Expenses		Net losses and loss	
expenses	31,077	156,121	324,249	Acquisition expenses	26,728	42,540	69,624	General and	
administrative expenses	59,866	100,006	109,607	Interest expense	3,632	5,458	4,165		
Depreciation of fixed assets and impairment of intangible assets	1,024	4,999	3,001	Total expenses					
122,327	309,124	510,646	Income (loss) from continuing operations before income taxes	20,063					
(50,641)	(109,481)	Income tax expense	12	14	232	Net income (loss) from continuing operations			
20,051	(50,655)	(109,713)	Discontinued operations:			(Loss) income from operations of			
discontinued operations	—	(12,953)	3,761	Income on disposal of discontinued operations	—	704	—		
Net (loss) income from discontinued operations	—	(12,249)	3,761	Net income (loss)	20,051	(62,904)			
(105,952)	—	Gain on repurchase of Series A preferred shares	2,364	—	—	Dividends on preferred shares	—		
(1,916)	—	Net income (loss) to common shareholders	\$ 22,415	\$ (64,820)	\$ (105,952)	Weighted average			
common share and common share equivalents:				Basic	70,076,562	69,971,646	57,205,342		
Diluted	70,118,100	69,971,646	57,205,342	Basic income (loss) from continuing operations per common					
share	\$ 0.29	\$ (0.72)	\$ (1.92)	Basic (loss) income from discontinued operations per common share	—				
(0.19)	0.07	Basic income from disposal of discontinued operations per common share	—	0.01	—	Basic			
gain on repurchase of preferred shares per common share	0.03	—	—	Basic dividends on preferred share per					
common share	—	(0.03)	—	Basic income (loss) per common share	\$ 0.32	\$ (0.93)	\$ (1.85)		
Diluted				income (loss) from continuing operations per common share	\$ 0.29	\$ (0.72)	\$ (1.92)		
income (loss) from discontinued operations per common share	—	(0.19)	0.07	Diluted (loss) income					
operations per common share	—	0.01	—	Diluted gain on repurchase of preferred shares per common share					
0.03	—	—	Diluted dividends on preferred share per common share	—	(0.03)	—	Diluted income (loss) per		
common share	\$ 0.32	\$ (0.93)	\$ (1.85)						

The accompanying notes are an integral part of these consolidated financial statements

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QUANTA CAPITAL HOLDINGS LTD.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Expressed in thousands of U.S. dollars except for share and per share amounts)

For the year
 ended
 December 31,
 2007 For the year
 ended
 December 31,
 2006 For the year
 ended
 December 31,

2005 Net income (loss)	\$ 20,051	\$ (62,904)	\$ (105,952)	Other comprehensive income (loss)
Net unrealized investment losses arising during the period, net of income taxes	—	(6,222)	(12,429)	Foreign
currency translation adjustments	(401)	(1,381)	327	Reclassification of net realized losses on available for
sale investments included in net income (loss), net of income taxes	—	15,945	13,020	Other comprehensive
(loss) income	(401)	8,342	918	Comprehensive income (loss)
	\$ 19,650	\$ (54,562)	\$ (105,034)	

The accompanying notes are an integral part of these consolidated financial statements

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QUANTA CAPITAL HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in thousands of U.S. dollars)

For the year ended December 31, 2007	For the year ended December 31, 2006	For the year ended December 31, 2005	Cash flows from operating activities	Net income (loss) from continuing operations	\$ 20,051
\$ (50,655)	\$ (109,713)	\$ (50,655)	Adjustments to reconcile net income (loss) from continuing operations to net cash (used in) provided by continuing operating activities	Depreciation of property and equipment	849
3,277	3,001	3,277	Amortization & impairment of intangible assets (discounts) premiums on investments	175	1,722
15,945	13,020	15,945	Net change in fair value of investments	(3,024)	—
—	88	—	Gain on repurchase of junior subordinated debentures	(4,421)	—
—	—	—	Loss on disposal of fixed assets	106	472
—	—	—	Non-cash stock compensation expense	312	649
—	—	—	Changes in assets and liabilities:	Restricted cash and cash equivalents	(62,870)
—	—	—	Accrued investment income	2,114	(1,429)
—	—	—	Funds withheld by cedants	24,761	(925)
—	—	—	Deferred acquisition costs, net	72,788	(30,875)
—	—	—	Deferred reinsurance premiums	15,248	76,837
—	—	—	Other accounts receivable	619	9,040
—	—	—	Net deferred tax asset	(5,277)	—
—	—	—	Other assets	3,392	(23,248)
—	—	—	Reserve for losses and loss adjustment expenses	(98,530)	89,635
—	—	—	Environmental liabilities assumed	(1,890)	(2,565)
—	—	—	Reinsurance balances payable	2,957	(20,430)
—	—	—	Accounts payable and accrued expenses	(15,806)	1,635
—	—	—	Deferred income and other liabilities	(3,521)	(4,438)
—	—	—	Income taxes payable	5,277	—
—	—	—	Contingencies	2,486	—
—	—	—	Net cash (used in) provided by continuing operating activities	(92,806)	(50,154)
—	—	—		155,117	

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QUANTA CAPITAL HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

(Expressed in thousands of U.S. dollars)

For the year
ended
December 31,
2007 For the year
ended
December 31,
2006 For the year
ended
December 31,
2005

Cash flows from discontinued operations				Net (loss) income from discontinued operations	—
(12,249)	3,761	Adjustments to reconcile net (loss) income from discontinued operations to net cash provided by discontinued operations		Depreciation of property and equipment	— 131 248
		Amortization of intangible assets	— 516 740	Impairment of goodwill	— 12,561 —
		Income on disposal of discontinued operations	— (704) —	Changes in assets and liabilities of discontinued operations	— 6,804 (3,850)
		Purchase of property and equipment	— (70) (198)	Net cash provided by discontinued operations	—
6,989	701	Net cash (used in) provided by operating activities	(92,806)	(43,165)	155,818
		Cash flows provided by (used in) investing activities		Investment in equity investment, recorded at cost in other assets	(118) — —
		Purchases of fixed maturities and short-term investments	(894,592)	(2,697,430)	
(1,564,491)		Proceeds from sale or maturity of fixed maturities and short-term investments		1,104,661	
2,589,620	1,407,597	Contingent consideration paid on acquisition of subsidiary	— (5,000)	—	
		Proceeds from disposal of discontinued operations, net of costs and net of cash disposed of	— 9,317 —	Proceeds from sale of property and equipment	61 416 —
		Purchases of property and equipment	(651)	(243)	(3,210)
		Net cash provided by (used in) investing activities	209,361	(103,320)	(160,104)
		Cash flows (used in) provided by financing activities		Proceeds from issuance of common shares, net of offering costs	— —
		Proceeds from issuance of preferred shares, net of offering costs	— 3,160	71,838	
		Dividends on Preferred shares	— (1,916)	—	
		Repurchase of preferred shares, net of repurchase costs	(72,634)	—	
		Proceeds from junior subordinated debentures, net of issuance costs	— —	19,591	
		Repurchase of junior subordinated debentures, net of repurchase costs	(54,501)	—	
		Net cash (used in) provided by financing activities	(127,135)	1,244	149,646
		(Decrease)/increase in cash and cash equivalents	(10,580)		
(145,241)	145,360	Cash and cash equivalents at beginning of period	32,894	178,135	32,775
		Cash and cash equivalents at end of period	\$ 22,314	\$ 32,894	\$ 178,135

Supplemental information:
Interest paid \$ 4,823 \$ 4,071 \$ 3,937 Taxes paid \$ 2 \$ 40 \$ 244

The accompanying notes are an integral part of these consolidated financial statements

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QUANTA CAPITAL HOLDINGS LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars except for share amounts, or as otherwise stated)

1. Description of business

Quanta Capital Holdings Ltd. (“Quanta Holdings” or the Company), incorporated on May 23, 2003, is a holding company organized under the laws of Bermuda. Quanta Holdings and its subsidiaries, collectively referred to as the “Company” were formed to provide specialty insurance, reinsurance, risk assessment and risk technical services and products on a global basis.

Following losses in the 2005 hurricane season and the resulting A.M. Best rating action in 2006, the Company started running off its insurance and reinsurance businesses, other than its participation in Syndicate 4000 in the Lloyd’s market, and sold its interest in Environmental Strategies Consulting LLC (“ESC”), a wholly owned environmental risk management subsidiary.

On May 28, 2007, Quanta Holdings created QCH Acquisition Ltd., a wholly-owned subsidiary as an exempted company limited by shares in Bermuda. QCH Acquisition Ltd. was formed to purchase any and all of the Company’s 10.25% Series A Preferred Shares (“Series A Preferred Shares”) pursuant to the terms of a tender offer which was commenced on July 11, 2007. The tender offer expired on August 10, 2007 and more than 96% of the outstanding Series A Preferred Shares were repurchased. On September 25, 2007, the Company repurchased all of the remaining Series A Preferred Shares and on September 29, 2007, the Series A Preferred Shares were cancelled. The Series A Preferred Shares were repurchased for an aggregate price of \$72.6 million, including costs, resulting in a gain of \$2.4 million, net of repurchase costs and the write off of original deferred issuance costs. Please see Note 16 regarding further information relating to the repurchase of the Series A Preferred Shares. QCH Acquisition Ltd was liquidated on December 21, 2007.

On August 22, 2007, the Company purchased all of the outstanding junior subordinated debentures (the “Trust Preferred Securities”) of (i) Quanta Capital Statutory Trust I, an affiliated Delaware trust formed on December 21, 2004 (the “Trust I”), and (ii) Quanta Capital Statutory Trust II, an affiliated Delaware trust formed on February 22, 2005 (the “Trust II” and together with Trust I, the “Trusts”), for an aggregate purchase price of \$54.5 million, including costs, resulting in a gain of \$4.4 million, net of repurchase costs and the write off of original deferred issuance costs. The Company originally issued and sold \$60 million of the Trust Preferred Securities in private placements. Following the purchase of the Trust Preferred Securities, the Company cancelled the Trust Preferred Securities, dissolved the Trusts and terminated the Declarations, the Guarantees, the Debentures and the Indentures. Please see Note 12 regarding further information relating to the repurchase of the Trust Preferred Securities.

On February 13, 2008, the Company sold Quanta 4000 Ltd. (“Quanta 4000”), which provides 90% of the capital for the 2007 underwriting year for Syndicate 4000, and its interest in Pembroke JV Ltd. (“Pembroke JV”) to Chaucer Holdings Plc. (“Chaucer”) and has since received the return of approximately \$117.2 million of cash and investment assets which had previously been pledged to Lloyd’s as capital support for the business being written by Syndicate 4000. Syndicate 4000 is managed by Pembroke Managing Agency Limited (“Pembroke”) of which the Company owned 15% through its share ownership in its parent, Pembroke JV, in a transaction that was closed on March 2, 2007. Pembroke provides technical and administrative support and oversight to Syndicate 4000 and was a joint venture among Quanta Holdings, Chaucer, the specialist Lloyd’s insurer, and the Syndicate 4000 underwriting team. See Note 21 for further details on the subsequent event in relation to Quanta 4000.

The Company maintains offices in Bermuda, Ireland and the United States of America (the “U.S.”).

2. Significant accounting policies

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”), which

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QUANTA CAPITAL HOLDINGS LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars except for share amounts, or as otherwise stated)

require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities reported at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. While management believes the amounts included in the consolidated financial statements reflect management's best estimates and assumptions, the actual results could ultimately be materially different from the amounts currently provided for in the consolidated financial statements. The Company's principal estimates relate to the development or determination of the following:

- reserves
- for losses and loss adjustment expenses;
- reinsurance
- balances recoverable and payable;
- deposit liabilities;
- certain
- estimated premiums written, unearned premiums and receivables;
- contingent
- commissions receivable and payable;
- provision for
- non-collectible reinsurance balances recoverable and premiums receivable;
- the valuation of
- investments and determination of hierarchical inputs used to measure fair value of investments;
- the valuation of
- intangible assets;
- litigation and other
- contingent liabilities;
- annual incentive
- plan provisions and severance accruals;
- environmental
- liabilities assumed; and
- deferred income
- taxes and liabilities.

a) Basis of presentation

The Company's consolidated financial statements include the financial statements of the Company and all of its wholly-owned subsidiaries. All significant balances and transactions among related companies have been eliminated on consolidation. The results of subsidiaries have been included from either their dates of acquisition or their dates of incorporation and up to their date of disposal. For the years ended December 31, 2005 and 2006 and the period ended August 22, 2007, the consolidated financial statements also included the earnings of Quanta Trust and Quanta Trust II which were formed in relation to the issuance of Trust Preferred Securities as further described in Note 12. As noted above in Note 1, these Trust Preferred Securities were repurchased on August 22, 2007 and the Trusts were dissolved.

ESC was a wholly owned subsidiary of Quanta Holdings until its sale on September 15, 2006. ESC provided diversified environmental risk management services to assist customers in environmental remediation, regulatory analyses, technical support for environmental claims, merger and acquisition due diligence, environmental audits and risk assessments, and engineering and information management services. ESC also provided risk assessment and technical services support to the Company's environmental underwriters. Following the sale of ESC, the results of operations of ESC, up to the date of sale, are reported as a discontinued operation. Consequently, prior period Statements of Operations and Statements of Cash Flows have been reclassified for all periods presented to reflect ESC as a discontinued operation, as further described in Note 3.

Lloyd's syndicates use cash basis accounting to determine results by underwriting year over a three year period. The Company makes adjustments to convert from Lloyd's cash basis accounting to

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QUANTA CAPITAL HOLDINGS LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars except for share amounts, or as otherwise stated)

accrual basis accounting in accordance with U.S. GAAP. Generally, adjustments are made to recognize underwriting results on an accrual basis, including estimated written and earned premiums and estimated losses and expenses incurred.

Certain balances included in the consolidated financial statements for the years ended December 31, 2006 and 2005 have been reclassified to conform with the presentation for the year ended December 31, 2007.

b) Premiums written, ceded and earned

Insurance and reinsurance premiums written are earned over the terms of the associated insurance policies and reinsurance contracts in proportion to the amount of insurance protection provided. Typically this results in the earning of premium on a pro rata over time basis over the term of the related insurance or reinsurance coverage. Premiums written on risks attaching reinsurance contracts are recorded in the period in which the underlying policies or risks are expected to incept and are earned on a pro rata over time basis over the expected term of the underlying policies. As a result, premiums earned on risks attaching reinsurance contracts usually extend beyond the original term of the reinsurance contract resulting in recognition of premium earnings over an extended period, typically up to 24 months. The term of the insurance or reinsurance coverage provided may be cancelled by the insured or ceding company resulting in a return of written premium.

Premiums written and ceded on certain types of contracts include estimates based on information received from the ceding companies, brokers or insureds. Estimates of written premiums are re-evaluated over the term of the associated contracts as underwriting information becomes available and as actual premiums are reported by the ceding companies, brokers or insureds. Subsequent changes to the premium estimates and cancellations are recorded as adjustments to premiums written in the period in which they become known. Such adjustments to estimated premium may be significant.

Adjustments related to retrospective rating provisions that adjust estimated premiums or acquisition expenses are recognized over contract periods in accordance with the underlying contract terms based on current experience under the contracts. Reinstatement premiums that reinstate coverage limits under pre-defined contract terms are written and earned at the time the associated loss event occurs. The original premium is earned over the remaining exposure period of the contract. Profit commissions are expenses that vary with and are directly related to acquiring new and renewal insurance and reinsurance business. Profit commission accruals are recorded as acquisition costs and are adjusted at the end of each reporting period based on the experience of the underlying contract. No claims bonuses are accrued as a reduction of earned premium and are adjusted at the end of each reporting period based on the experience of the underlying contract. Such adjustments related to retrospective rating provisions, reinstatement premiums, profit commissions and no claims bonuses may be significant.

Ceded reinsurance or retrocessional coverage is used to increase the Company's underwriting capacity and to limit individual and aggregate exposures to risks of losses arising from contracts of insurance or reinsurance that it underwrites. Reinsurance premiums ceded to reinsurers are recorded and earned in a manner consistent with that of the original contracts or policies written and the terms of the reinsurance agreements.

Premiums written and ceded relating to the unexpired periods of coverage or policy terms are recorded on the consolidated balance sheet as unearned premiums and deferred reinsurance premiums.

Prior to commencing its self-managed run-off, in the normal course of its operations, the Company entered into certain contracts that do not meet the risk transfer provisions of Statement of

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Financial Accounting Standards (“SFAS”) No. 113, “Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts” (“SFAS 113”) for financial reporting purposes either due to insufficient underwriting risk or insufficient timing risk or do not provide the indemnification required for insurance accounting under SFAS No. 60, “Accounting and Reporting by Insurance Enterprises” (“SFAS 60”). For these contracts the Company follows the deposit method of accounting as prescribed in American Institute of Certified Public Accountants (“AICPA”) Statement of Position 98-7, “Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk” (“SOP 98-7”). The deposit method of accounting requires that the premium the Company receives or pays, less any explicitly defined fees retained or paid, is accounted for as a deposit asset or a deposit liability on the consolidated balance sheet. Explicitly defined fees retained or paid are deferred and earned to other income in the consolidated statement of operations and according to the nature of, and in proportion to, the product or service provided.

For those contracts that transfer significant underwriting risk only and for reinsurance contracts where it is not reasonably possible that the Company can realize a significant loss even though it assumes significant insurance risk, the deposit asset or liability is measured based on the unexpired portion of the coverage provided. The deposit asset or liability is adjusted for any losses incurred or recoverable based on the present value of the expected future cash flows arising from the loss event with the adjustment being recorded in net losses and loss expenses within the Company’s results of operations.

For those contracts that transfer neither significant underwriting risk nor significant timing risk and for contracts that transfer significant timing risk only, the deposit asset or liability is adjusted, and corresponding interest income or expense recognized within the Company’s results of operations, by using the interest method to calculate the effective yield on the deposit based on the estimated amount and timing of cash flows. If a change in the actual or estimated timing or amount of cash flows occurs, the effective yield is recalculated and the deposit is adjusted to the amount that would have existed had the new effective yield been applied since the inception of the insurance or reinsurance contract. The adjustment is recorded as interest income or interest expense.

c) Acquisition expenses and ceding commission income

Acquisition expenses are policy issuance related costs that vary with and are directly related to the acquisition of insurance and reinsurance business, and primarily consist of commissions, third party brokerage and insurance premium taxes. Ceding commission income consists of commissions the Company receives on business that it cedes to its reinsurers. Acquisition expenses also include the sliding scale net contingent commissions relating to one program which generate either additional net commission expense or net commission returns based on loss ratio development. Acquisition expenses and commission income are recorded and deferred at the time the associated premium is written or ceded and are subsequently amortized in earnings as the premiums to which they relate are earned or expensed. Acquisition expenses are reflected in the consolidated statement of operations net of ceding commission income from reinsurers. Acquisition costs relating to unearned premiums are deferred in the consolidated balance sheet as deferred acquisition costs and reported net of commission income relating to deferred reinsurance premiums ceded.

Net deferred acquisition costs are carried at their estimated realizable value and are limited to the amount expected to be recovered from future net earned premiums, after deducting anticipated losses and other costs and considering anticipated investment income. Any limitation is referred to as a premium deficiency.

In accordance with SFAS60, a premium deficiency reserve is recognized if the sum of expected losses and loss expenses, unamortized acquisition costs and administrative expenses exceeds related

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unearned premiums. A premium deficiency reserve is recognized by charging unamortized acquisition costs to expense to the extent required in order to eliminate the deficiency. If the premium deficiency reserve exceeds unamortized acquisition costs then a liability is accrued for the excess deficiency.

d) Reserve for losses and loss adjustment expenses

The Company establishes reserves for losses and loss expenses for estimates of future amounts to be paid in settlement of its ultimate liabilities for claims arising under its contracts of insurance and reinsurance that have occurred at or before the consolidated balance sheet date. The estimation of ultimate loss and loss expense liabilities is a significant judgment made by management and is inherently subject to significant uncertainties.

The Company's loss reserves fall into two categories: case reserves for reported losses and loss expenses and reserves for losses and loss expenses incurred but not reported, or IBNR reserves. Case reserves are based initially on claim reports received from insureds, brokers or ceding companies, and may be supplemented by the Company's claims professionals with estimates of additional ultimate settlement costs. IBNR reserves are estimated by management using generally accepted statistical and actuarial techniques and are reviewed by independent actuaries. In applying these techniques, management uses estimates as to ultimate loss emergence, severity, frequency, settlement periods and settlement costs. In making these estimates, the Company relies on the most recent information available, including pricing information, industry information and on its historical loss and loss expense experience.

As of December 31, 2007, the primary reserving method used by the Company to estimate the ultimate cost of losses for its specialty reinsurance run-off lines and professional, environmental, fidelity and technical risk property specialty insurance run-off business lines was the Bornhuetter-Ferguson actuarial method for which the Company uses both historical paid and historical reported data. The Bornhuetter-Ferguson actuarial method utilizes the expected loss (initial expected loss and loss expense ratio multiplied by earned premium) multiplied by loss development factors derived by the Company's internal actuaries from its own actual loss and loss expense experience in each product line and also from industry statistics. The Company's initial expected loss and loss expense ratio for the specialty reinsurance business lines is derived from loss exposure information provided by brokers and ceding companies and from loss and loss expense ratios established during the pricing of individual contracts. The Company's initial expected losses and loss expense ratios selected for its professional, environmental, fidelity and technical risk property specialty insurance lines are based on benchmarks derived by its underwriters and actuaries during the initial pricing of the business and from comparable market information. These benchmarks are then adjusted for any rating increases and changes in terms and conditions that have been observed in the market.

Since the company ceased writing business, it is presently believed that the data in the specialty insurance and specialty reinsurance run off business is mature enough to rely on the following actuarial methods: Reported Development Method, Paid Development Method, Paid Bornhuetter-Ferguson Method and Reported Bornhuetter-Ferguson Method. The initial expected losses and loss expense ratios selected are based on benchmarks derived by its underwriters and actuaries during the initial pricing of the business and from comparable market information. These benchmarks are then adjusted for any rating increases and changes in terms and conditions that have been observed in the market. In the Company's Lloyd's business, for the non-subprime exposure, for the 2006 underwriting year and prior it relied on the Bornhuetter-Ferguson actuarial method and for 2007 underwriting year it

used an expected loss ratio methodology. For the subprime exposure, multiple methods were used to derive an estimate of the ultimate cost of losses. For example one method used was related to the industry estimate of ultimate losses and calculating the Company's ultimate cost of losses based on Syndicates 4000's share of the market premium. Another method was

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based on an internal loss exposure analysis commissioned by Syndicate 4000 based on the risk characteristics of the Syndicate 4000 Portfolio of policies written. Based on these analyses and actuarial judgment, the Company selected an estimate of Syndicate's 4000 exposure to the subprime event.

Even though the Company's reserving techniques represent a reasonable and appropriate basis for estimating ultimate claim costs and management believes that the reserves for losses and loss expenses are sufficient to cover claims from losses occurring up to the consolidated balance sheet date, ultimate losses and loss expenses may be subject to significant volatility as a result of significant uncertainties. These uncertainties are driven by many variables that are difficult to quantify. These uncertainties include, for example, the period of time between the occurrence of an insured loss and actual settlement, fluctuations in inflation, prevailing economic, social and judicial trends, legislative changes, internal and third party claims handling procedures, the lack of complete historical data on which to base loss expectations and the run-off status of the Company's operations, except Syndicate 4000. Accordingly, ultimate liabilities may differ materially from the amounts recorded in the consolidated financial statements.

The estimation of unpaid loss liabilities will be affected by the type or structure of the policies the Company has written. For specialty insurance run-off business, the Company often assumes risks for which claims experience will tend to be frequency driven. As a result, historical loss development data may be available and traditional actuarial methods of loss estimation may be used. Conversely, the available amount of relevant loss experience used to quantify the emergence, severity and payout characteristics of loss liabilities is limited for policies written where the Company expects that potential losses will be characterized by lower frequency but higher severity claims.

The estimation of unpaid loss liabilities will also vary in subjectivity depending on the lines or classes of business involved. Short-tail business describes lines of business for which losses become known and paid in a relatively short period of time after the loss actually occurs. Typically, there will be less variability in the estimates of ultimate amount of losses from claims incurred in the short-tail lines that the Company writes such as property, marine, and aviation. Long-tail business describes lines of business for which actual losses may not be known for some time or for which the actual amount of loss may take a significantly longer period of time to emerge or develop. The Company writes casualty, professional and environmental lines of business that are generally considered longer tail in nature. Because loss emergence and settlement periods can be many years in duration, these lines of business will have more variability in the estimates of their loss and loss expense reserves.

The Company continually reviews and adjusts its reserve estimates and reserving methodologies taking into account all currently known information and updated assumptions related to unknown information. Loss and loss expense reserves established in prior periods are adjusted in current operations as claim experience develops and new information becomes available. Any adjustments to previously established reserves may significantly impact current period underwriting results and net income by reducing net income.

e) Reinsurance recoverable

Reinsurance recoverable, under the terms of ceded reinsurance contracts, includes loss and loss adjustment expenses recoverable and deferred reinsurance premiums. The Company estimates loss and loss adjustment expenses recoverable using methodologies and assumptions consistent with those used in estimating reserves for losses and loss

adjustment expenses. The estimation of loss and loss adjustment expenses recoverable is a significant judgment made by management and is inherently subject to significant uncertainties. The Company is subject to credit risk with respect to the reinsurance ceded because the ceding of risk does not relieve the Company from its original

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obligations to its insureds. To the extent reinsurers default, the Company must settle these obligations without the benefit of reinsurance protection. Failure of the Company's reinsurers to honor their obligations could result in credit losses. The Company establishes allowances for amounts recoverable that are considered potentially uncollectible from its reinsurers. The valuation of this allowance for uncollectible reinsurance recoverable includes a review of the credit ratings of the reinsurance recoverables by reinsurer, an analysis of default probabilities as well as identifying whether coverage issues exist. These factors require management judgment and the impact of any adjustments to those factors is reflected in net income in the period that the adjustment is determined.

f) Non-traditional contracts

The Company wrote non-traditional contracts of insurance and reinsurance that were deemed not to meet risk transfer criteria and accordingly the Company has accounted for these transactions as deposits held on behalf of clients. During the years ended December 31, 2007, 2006 and 2005, the Company recognized within other income \$(0.1) million, \$3.5 million and \$2.5 million of fees and revenues relating to non-traditional contracts which were accounted for using the deposit method. As part of its overall runoff strategy, the Company is currently reviewing the performance of all of its non-traditional contracts of insurance and reinsurance.

In the fourth quarter of 2004, the Company entered into a surplus relief life reinsurance arrangement with a U.S. insurance company and assumed, through novation agreements, several life reinsurance contracts it had made. The client, being the company assuming these contracts, which is subject to insurance regulation in the United States and therefore is required to maintain a certain amount of statutory capital, may reduce its statutory capital requirements. In exchange for the Company's assumption of the contracts it received a fee. The arrangement, among other things, provides that on certain dates and during specific periods, the client has the right but not the obligation to recapture the life reinsurance contracts the Company has assumed, provided that the underlying cedants do not reasonably withhold their consent to this recapture. Of the \$(0.1) million, \$3.5 million and \$2.5 million, \$0.1 million, \$0.6 million and \$0.7 million of other income recognized during the years ended December 31, 2007, 2006 and 2005 relate to fees earned from this surplus relief life reinsurance arrangement with a U.S. insurance company that meets the Company's definition of a non-traditional contract. As of December 31, 2007, 2006 and 2005, the Company provided approximately \$8.4 million, \$10.8 million and \$13.1 million (unaudited) of statutory surplus relief to the U.S. insurance company under this contract.

The Company believes the arrangement, including the client's option to recapture, and the assumption of the life insurance contracts constitute one contract with minimal mortality, credit or other insurance or economic risk which results in deposit accounting. If the Company's client does not recapture the underlying insurance contracts in the future, the Company may be viewed as having had the risks described above and, as a result, the Company could be deemed to have retained life reinsurance risk and, as a result, may be required to account for some or all of the underlying insurance contracts as life insurance, recognizing life premiums written and life benefit reserves in the consolidated statement of operations.

In respect of life reinsurance arrangements written on a coinsurance basis, where investment assets have been transferred to the Company, such assets have been recorded within the Company's trading investment portfolio. A deposit liability has been recorded in the consolidated balance sheet in accordance with SFAS 97 "Accounting and

Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments'' for non-risk investment contracts as an interest bearing instrument using the effective yield method. The investments related to the deposit liability are held in trust funds and are pledged to the ceding companies.

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In respect of the life reinsurance arrangements written on a modified coinsurance basis, the ceding company's net statutory reserves and assets are withheld and remain legally owned by the ceding company. These modified coinsurance contracts represent "non-cash" financial reinsurance transactions, whereby, in accordance with the contract terms, there are no net cash flows at inception of contracts, nor are there expected to be net cash flows through the life of the contracts, other than the Company's explicitly defined fees. Notional contract assets and liabilities contemplated by the contract terms are offset in accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 39 ("FIN 39") "Offsetting of Amounts Related to Certain Contracts" and as such the Company does not present such assets or deposit liabilities in its consolidated balance sheet.

Certain of the Company's coinsurance and modified coinsurance agreements may contain provisions that qualify as embedded derivatives under Derivatives Implementation Group Issue No. B36 "Embedded Derivatives: Modified Coinsurance Arrangements and Debt Instruments That Incorporate Credit Risk Exposures That Are Unrelated or Only Partially Related to the Creditworthiness of the Obligor under Those Instruments" ("DIG Issue B36"). The value of embedded derivatives in these contracts is currently considered immaterial. The Company monitors the performance of these treaties on a quarterly basis. Significant adverse performance or changes in the Company's expectations of future cashflows on these treaties could result in losses associated with the embedded derivative.

Included in other income is \$1.5 million, \$0.6 million and \$0.2 million of other income recognized during the years ended December 31, 2007, 2006 and 2005 relate to explicitly defined margins on one short duration contract written by the Company's specialty reinsurance segment that did not meet the risk transfer provisions of SFAS 113. The contract was commuted during the year ended December 31, 2007, resulting in a gain on commutation of \$0.8 million, but was originally written on a funds withheld basis, such that a deposit liability of \$21.3 million and \$21.7 million at December 31, 2006 and 2005 was recorded and was equal to a funds withheld asset according to the contract terms. In accordance with FIN 39, the funds withheld asset and the deposit liability have been offset in the consolidated balance sheet.

Also included in other income is an amount of \$3.7 million (net of commissions of \$0.8 million), which has been recorded as the return of all fee income received to date as a result of the Company's decision to rescind a surplus life relief insurance contract. As of December 31, 2007, 2006 and 2005, the Company has provided approximately \$29.3 million, \$30.1 million and \$33.2 million (unaudited) of statutory surplus relief to a U.S. insurance company under this contract. This contract is further discussed in Note 13(h).

The remaining other income is derived from revenues on a limited number of non-traditional reinsurance contracts accounted for as deposits. Although these contracts did possess some underwriting and timing risks as prescribed by SFAS No. 113, the Company does not believe it is exposed to a reasonable possibility of significant loss.

g) Environmental liabilities assumed, technical services remediation revenues and costs

The Company has assumed environmental liabilities in exchange for remediation fees and contracts to perform the required remediation in accordance with the underlying remediation agreements. The Company estimates its initial and ongoing ultimate liabilities for environmental remediation obligations based upon actual experience, past experience with similar remediation projects, technical engineering examinations of the contaminated sites and state,

local and federal guidelines. However, there can be no assurance that actual remediation costs will not significantly differ from the estimated amounts.

As of December 31, 2007 and 2006, environmental liabilities assumed includes two environmental remediation projects, for which estimated liabilities of \$1.5 million and \$3.3 million have been

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recorded. The assumed environmental remediation obligations for the projects are contractually defined pursuant to a site specific remediation plan.

The amount of consideration received for the assumption of remediation liabilities in excess of the expected environmental remediation liability is initially deferred and recorded in deferred income on the consolidated balance sheet and subsequently recognized in earnings over the remediation period using the cost recovery or percentage-of-completion method. These methods are based on the ratio of remediation expenses actually incurred and paid to total estimated remediation costs. As of December 31, 2007 and 2006, the Company had deferred approximately \$0.1 million and \$0.2 million of technical services remediation revenues. Anticipated remediation losses, if any, are recorded in the period in which the Company becomes aware of such losses.

In December 2007, the Company cancelled an environmental insurance policy issued by one of its insurance affiliates related to certain remediation liabilities assumed by the Company. The cancelled policy was replaced by a similar environmental insurance policy issued by a third-party insurance company.

h) Derivative Instruments and Hedging Activities

The Company had entered into certain derivative instruments and adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133") and SFAS 149, "Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities."

The Company may enter into investment related derivative transactions, as permitted by its investment guidelines, for the purposes of managing investment duration, interest rate and foreign currency exposure, and enhancing total investment returns. The Company may also, as part of its business, enter into derivative instruments for the purpose of replicating approved investment, insurance or reinsurance transactions that meet the Company's investment or underwriting guidelines. The Company has carried within its available-for-sale fixed maturity portfolio a mortality-risk-linked security for which the repayment of principal was dependent on the performance of a predefined mortality index over a fixed period of time. The Company determined that the component of the bond that is linked to the specified mortality index was, under SFAS 133, an embedded derivative that was not clearly and closely related to its host contract (a debt security) and was therefore bifurcated and accounted for as a derivative under SFAS 133. This instrument was sold during 2005. The Company has not designated any of its derivative instruments as hedging instruments for financial reporting purposes.

The Company recognizes all standalone derivative instruments as either other assets or liabilities and recognizes embedded derivatives as part of their host instruments in the consolidated balance sheet. The Company measures all derivative instruments at their fair values, which are based on market prices and equivalent data provided by independent third parties. When market data is not readily available, the Company uses analytical models to estimate the fair values of these instruments based on their structure, terms and conditions and prevailing market conditions. The Company recognizes changes in the fair value of derivative instruments and realized gains and losses on derivative instruments in its consolidated statement of operations as part of other income and net realized (losses) gains on investments, respectively. The nature of derivative instruments and the estimates used in estimating their fair value, changes in fair value of derivative instruments and realized gains and losses on settled derivative instruments

may create significant volatility in the Company's results of operations in future periods.

DIG Issue B36 indicates that the Company's life financial reinsurance contracts where the Company notionally receives a financial instrument with an investment return based on its underlying referenced pool of assets may contain an embedded derivative that must be bifurcated and accounted

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for in accordance with SFAS 133 since the economic characteristics are not clearly and closely related to the host instrument. Although the Company's life financial reinsurance arrangements may contain embedded derivatives the Company believes that due to the terms of these contracts, including the experience refund provisions contained within the treaties, the value of embedded derivatives contained in these contracts is currently considered to be immaterial.

In September 2006, the FASB issued FASB Statement No. 155, "Accounting for certain hybrid financial instruments" ("SFAS 155"). SFAS 155 amends FASB Statements No. 133, "Accounting for Derivative Instruments and Hedging Activities," and No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". SFAS 155 was effective for financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of SFAS 155 on January 1, 2007 has not affected the Company's financial position or results of operations.

i) Incentive Plans

During the year ended December 31, 2004, the Company adopted an Annual Variable Cash Compensation Plan (the "Annual Variable Cash Incentive Plan") which was generally available to employees in 2004 and 2005. Awards paid under this plan were dependent on performance measured at an individual and line of business level for the years ended December 31, 2004 and 2005. In general, the Annual Variable Cash Incentive Plan provided for an annual bonus award to employees which was based on a sharing of profit in excess of a minimum return on capital to shareholders (as calculated under the Annual Variable Cash Incentive Plan). Profit for each calendar year was measured by estimating the ultimate net present value of after-tax profit generated from business during that calendar year and, up until December 31, 2006, was re-estimated on an annual basis through the vesting period. Annual Incentive Plan awards for 2004 and 2005 have now fully vested and all amounts have been paid.

Following the Company's determination to engage in a self-managed run-off, employees will generally receive a bonus based on individual performance that was comprised of a guaranteed and variable element for the 2006 financial year and that is 100% discretionary for the 2007 financial year. The bonus based on the 2006 financial year was paid in the second quarter of 2007. The bonus based on the 2007 financial year is expected to be paid on or around March 15, 2008.

During the first quarter of 2007, the Company adopted the 2007 Long Term Incentive Plan (the "2007 LTIP"). The 2007 LTIP is intended to motivate and reward its Chief Executive Officer, Chief Financial Officer and certain key employees of the Company and its subsidiaries for the successful management of the run-off of the Company's business and insurance operations other than the Lloyd's business. The 2007 LTIP is also intended to help the Company retain certain key employees by providing benefits that do not vest for up to three years except in the event of a change of control or termination of a participant's employment by the Company without cause, or due to death, permanent disability or normal retirement. Under the 2007 LTIP, if any participant voluntarily terminates his or her employment (other than by retirement) or that person is terminated for cause prior to December 31, 2009, the entire award will be forfeited by that participant. If any participant is involuntarily terminated without cause, then the participant will receive a pro-rata portion of the total amount available to participants under the 2007 LTIP. In the event specified change of control events are completed prior to 2010, participants will become immediately vested in

their payouts under the 2007 LTIP and will receive an award based on the share price received by the shareholders of the Company in the change of control transaction, plus any dividends previously paid to the shareholders.

Expenses related to the Annual Variable Cash Incentive Plan awards and 2007 LTIP are recognized by applying provisions of FASB Statement No. 123(R), "Share-Based Payment"

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(“SFAS 123(R)”). The Company continually reviews and adjusts its provisions for Annual Variable Cash Incentive Plan awards, 2007 LTIP awards and other bonus awards by taking into account known information and updated assumptions related to unknown information. Award provisions are an estimate and amounts established in prior periods are adjusted in current operations as new information becomes available. Any adjustments to previously established provisions or the establishment of new provisions may significantly impact current period results and net income. The Company expenses the vested portion of the 2007 LTIP plan using the fair value recognition provisions of SFAS 123(R). In order to do this the Company utilizes the Black-Scholes valuation model which uses various assumptions, including stock price volatility and interest rates.

j) Cash and cash equivalents

Cash equivalents include highly liquid instruments such as liquidity funds, money market funds and other time deposits with commercial banks and financial institutions which have maturities of less than three months from the date of purchase. Please see Note 13(a) in relation to concentrations of credit risk.

k) Investments and net investment income

In February 2007, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities” (“SFAS 159”). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value, with changes in fair value recorded in net income. The statement is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or after November 15, 2006, provided the entity also elects to apply the provisions of FASB Statement No. 157, “Fair Value Measurements” (“SFAS 157”). SFAS 157 established a hierarchy for inputs in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs are used when available.

Commencing January 1, 2007, the Company elected for early adoption of the fair value option for all fixed maturity investments and therefore also adopted SFAS 157. The Company elected to early adopt the fair value option to simplify the accounting, as this adoption reduces the burden of the monitoring of differences between the cost and fair value of its investments, including the assessment as to whether declines in value are temporary in nature, mitigates a potential volatility in earnings and further removes an element of management judgment. SFAS 159 has been applied to the Company’s entire investment portfolio but not to any other assets or liabilities. Prior to January 1, 2007, investments were considered “Available for Sale” and were carried at fair value, except those investments held in relation to the Company’s deposit liabilities. This adoption requires all investments to now be reported as “Trading” under SFAS 115, although it does not amend the carrying value of fixed maturity investments as they continue to be carried at fair value. As a result all unrealized gains and losses, amounting to approximately \$10.0 million in net unrealized gains, in the Company’s investment portfolio were reclassified from accumulated other comprehensive loss within shareholders’ equity on the consolidated balance sheets to retained deficit as of January 1, 2007.

Following the adoption of SFAS 159, all investments are now classified as “Trading” and all subsequent changes to the fair value of the Company’s investment portfolio are recorded as change in fair market value of investments within net

gains (losses) on investments in the consolidated statements of operations. Prior to January 1, 2007, unrealized gains and losses in the “Available for Sale” securities were included within accumulated other comprehensive income as a separate component of shareholders’ equity and unrealized gains and losses in the “Trading” securities were included within net realized gains on investments in the consolidated statement of operations.

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Realized gains and losses on sales of investments continue to be determined on a first-in, first-out basis and is shown within net gains (losses) on investments on the statement of operations. Net investment income includes interest income on fixed maturity investments, recorded when earned, and the amortization of premiums and discounts on investments, net of investment management and custody expenses.

Beginning January 1, 2007, assets and liabilities recorded at fair value in the consolidated balance sheet are categorized based upon the level of judgment associated with the inputs used to measure their fair value. An asset or a liability's categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation. Hierarchical levels—defined by SFAS 157 and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities—are as follows:

Level I — Valuations based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.

Level II — Valuations based on quoted prices in active markets for similar assets or liabilities, quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

Level III — Valuations based on inputs that are unobservable and significant to the overall fair value measurement. These are generally company generated inputs and are not market based inputs.

Prior to adoption of SFAS 159, the Company periodically reviewed its investments to determine whether an impairment, being a decline in fair value of a security below its amortized cost, was other than temporary. If such a decline was classified as other than temporary, the Company wrote down, to fair value, the impaired security resulting in a new cost basis of the security and the amount of the write-down was charged to the consolidated statement of operations as a realized loss. Some of the factors that the Company considered in determining whether an impairment was other than temporary included (i) the amount of the impairment, (ii) the period of time for which the fair value has been below the amortized cost, (iii) specific reasons or market conditions which could affect the security, including the financial condition of the issuer and relevant industry conditions or rating agency actions, and (iv) the Company's ability and intent to hold the security for sufficient time to allow for possible recovery.

Prior to the adoption of SFAS 159 and due to the Company's decision to place its insurance and reinsurance lines, except Syndicate 4000, into orderly run-off, the Company concluded that it may no longer have the ability or intent to hold its securities for a sufficient period of time to allow recovery. Accordingly, during the years ended December 31, 2006 and 2005, the Company recorded \$16.9 million and \$10.2 million in other than temporary impairment losses. The realization of these losses represents the maximum amount of potential losses in the Company's investment securities if it sold all of these securities at the time the impairments were recorded and was primarily attributable to changes in interest rates and not changes in credit quality. As a result of this decision, the affected investments were reduced to their estimated fair value, which became their new cost basis. The recognition of the losses had no effect on the Company's shareholders' equity, the market value of the Company's investments, the Company's cash flows or the Company's liquidity.

Short-term investments include highly liquid debt instruments and commercial paper that are generally due within one year of the date of purchase and are held as part of the Company's investment portfolios that are managed by independent investment managers.

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l) Property and equipment

Property and equipment, which consist of furniture, equipment, and leasehold improvements, are stated at cost less accumulated depreciation. Depreciation is computed using an accelerated method over the estimated useful lives of the related assets, ranging from three to seven years. Depreciation of leasehold improvements is computed using the straight-line method over the shorter of the estimated useful lives of the assets or the terms of the leases.

Repairs and maintenance are expensed as incurred. At the time of retirement or other disposal of property or equipment, the cost and related accumulated depreciation are deducted from their respective accounts and any resulting gain or loss is included in the consolidated statement of operations.

m) Capitalization of software costs

The Company capitalizes software costs when the preliminary project stage is completed and management commits to fund the software project which it deems probable will be completed and used to perform the intended function. This policy is in accordance with AICPA Statement of Position 98-1 “Accounting for the costs of computer software developed or obtained for internal use” (“SOP 98-1”). Software costs that are capitalized include only external direct costs of materials and services consumed in developing, or obtained for internal use computer software.

Capitalization of costs ceases as soon as the project is substantially complete and ready for its intended purpose. The carrying value of software costs is reviewed by the Company whenever events or changes in circumstances indicate that its carrying amount may not be recoverable, and a loss is recognized when the value of estimated undiscounted cash flow benefit related to the asset falls below the unamortized cost.

n) Other intangible assets

Other identifiable intangible assets that arise from business combinations are accounted for in accordance with SFAS No. 141, “Business Combinations” (“SFAS 141”) and SFAS No. 142, “Goodwill and Other Intangible Assets” (“SFAS 142”).

Identifiable amortizable intangible assets are amortized in accordance with their useful lives. Intangible assets with indefinite useful lives are not amortized but are tested annually for impairment by a comparison to estimated fair market value or more often if impairment indicators arise. If the carrying amounts of intangible assets are greater than their fair values established during impairment testing, the carrying value is immediately written-down to the fair value with a corresponding impairment loss recognized in the consolidated statement of operations.

o) Offering costs

Costs incurred in connection with, and that are directly attributable to common share offerings, are charged to additional paid-in capital. Costs incurred in connection with, and that are directly attributable to preferred share offerings, are charged to the preferred shares balance.

p) Foreign currency translation

Generally, the U.S. dollar is the functional currency of the Company and its subsidiaries. For entities where the U.S. dollar is the functional currency, all foreign currency asset and liability amounts are translated into U.S. dollars at end-of-period exchange rates, except for prepaid expenses, property and equipment, goodwill, intangible assets, deferred acquisition costs, deferred reinsurance

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premiums and unearned premiums which are translated at historical rates. Foreign currency income and expenses are translated at average exchange rates in effect during the period, except for expenses related to balance sheet amounts translated at historical exchange rates. Exchange gains and losses arising from the translation of foreign currency-denominated monetary assets and liabilities are included in the consolidated statement of operations.

For subsidiaries where the local currency is the functional currency, assets and liabilities denominated in local currencies are translated prior to consolidation into U.S. dollars at end of period exchange rates, and the resultant translation adjustments are reported, net of their related income tax effects, as a component of accumulated other comprehensive income (loss) in shareholders' equity. Subsidiary assets and liabilities denominated in other than the local currency are translated into the local currency prior to translation into U.S. dollars, and the resultant exchange gains or losses are included in the consolidated statement of operations in the period in which they occur. Subsidiary income and expenses are translated prior to consolidation into U.S. dollars at average exchange rates in effect during the period.

q) Stock-based compensation

The Company has a long-term stock-based incentive plan (the "Incentive Plan"), which is described more fully in Note 17. Prior to January 1, 2006, the Company accounted for the Incentive Plan under the recognition and measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25") and related Interpretations, as permitted by FASB Statement No. 123, Accounting for Stock-Based Compensation ("SFAS 123"). No stock-based employee compensation cost was recognized in the Statement of Operations for the year ended December 31, 2005, as all options granted under the Incentive Plan had an exercise price equal to the market value of the underlying common stock on the date of grant. Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), Share-Based Payment ("SFAS 123(R)"), using the modified-prospective-transition method. Under that transition method, compensation cost recognized in 2006 also includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). Results for prior periods have not been restated.

As a result of adopting SFAS 123(R) on January 1, 2006, the Company recorded share-based compensation expense of \$0.3 million and \$0.7 million for the years ended December 31, 2007 and December 31, 2006. This resulted in a reduction to basic and diluted income per share of \$0.01 for the year ended December 31, 2007 and an increase to basic and diluted loss per share of \$0.01 for the year ended December 31, 2006.

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The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123 to options granted under the Company's stock option plans in the period prior to January 1, 2006. For purposes of this pro forma disclosure, the value of the options is estimated using a Black-Scholes option-pricing formula and amortized to expense over the options' vesting periods.

	Year	
ended		
December 31,		
2005 Stock compensation expense	As reported	\$ —
Additional stock-based employee compensation expense determined under fair value based method	(3,028) Pro forma	\$ (3,028)
Net loss	As reported	\$ (105,952)
Additional stock-based employee compensation expense determined under fair value based method	(3,028) Pro forma	\$ (108,980)
Basic loss per share	As reported	\$ (1.85)
Pro forma	\$ (1.91)	Diluted loss per share
As reported	\$ (1.85)	Pro forma
	\$ (1.91)	

Included in the pro forma stock-based employee compensation expense for the year ended December 31, 2005 is \$1.0 million related to the accelerated vesting of 649,830 options granted to the Company's former Chief Executive Officer that were modified upon his resignation.

r) Income taxes

Income taxes have been recognized in accordance with the provisions of SFAS No. 109, "Accounting for Income Taxes", on those operations that are subject to income taxes. Deferred tax assets and liabilities result from temporary differences between the carrying amounts of existing assets and liabilities recorded in the consolidated financial statements and their respective tax bases. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of operations in the period that includes the enactment date. A valuation allowance for a portion or all of deferred tax assets is recorded as a reduction to deferred tax assets if it is more likely than not that such portion or all of such deferred tax assets will not be realized.

The Company adopted the provisions of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109" ("FIN 48") on January 1, 2007. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. During May 2007, the FASB issued FASB Staff Position No. FIN 48-1, "Definition of Settlement in FASB Interpretation No.48" ("FSP FIN 48-1"). FSP FIN 48-1 amends FIN 48 to provide guidance on how an enterprise should determine whether a

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tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. The adoption of FIN 48 and FSP FIN48-1 has not affected the Company's financial position or results of operations.

s) Debt issuance costs

Prior to the repurchase of the junior subordinated debentures, the Company had capitalized debt issuance costs associated with the issuance of this debt. These costs were initially capitalized within other assets in the consolidated balance sheet and subsequently amortized over the term of the related outstanding debt using the interest method. Upon repurchase of the junior subordinated debentures on August 22, 2007, these costs were recognized in the statement of operations.

At December 31 2006, the amortized value of these capitalized costs was \$1.7 million and was recorded in other assets. At December 31, 2007 there was no amount of amortized value of these capitalized costs.

t) Legal expenses

In the event of a dispute in the ordinary course of business, the Company expenses legal costs as they are estimated to have been incurred.

In the event of a specific litigation, when it is reasonably probable that the legal costs are going to be incurred, the Company accrues legal costs in line with the estimated incurred expenses.

u) Earnings per share

Basic earnings per share is computed using the weighted average number of common shares outstanding during the period. All potentially dilutive securities, including stock options, warrants and restricted shares are excluded from the basic earnings per share computation.

In calculating diluted earnings per share, the weighted average number of shares outstanding for the period is increased to include all potentially dilutive securities using the treasury stock method. Any common stock equivalent shares are excluded from the computation if their effect is antidilutive.

Basic and diluted earnings per share are calculated by dividing income available to common shareholders by the applicable weighted average number of shares outstanding during the year.

v) Segment reporting

The Company reports segment results in accordance with SFAS No. 131, "Segment Reporting" ("SFAS 131"). Under SFAS 131, reportable segments represent an aggregation of operating segments that meet certain criteria for aggregation specified in SFAS 131.

During 2005, the Company was comprised of four reportable segments and provided a number of products which are operating segments for purposes of GAAP. The Company's products included technical risk property, professional liability, environmental liability, fidelity and crime, surety, trade credit and political risk, property, casualty, marine and aviation, life surplus relief and technical services. The Company organized these products into five product lines: specialty insurance, specialty reinsurance, programs, structured products and technical services. Except for technical services, the products the Company offered to its clients were written either as traditional insurance or reinsurance policies or were provided as a program, a structured product or a combination of a traditional policy with a program or a structured product. These product lines were aggregated as reportable segments into specialty insurance, specialty reinsurance, and technical services. The attribution of insurance and reinsurance results to these reportable segments was based upon where the business was sourced and not necessarily where the business was recorded.

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During the year ended December 31, 2006, following the decision of the Company's Board of Directors in May 2006 to place most of its business in run-off, the Company changed the composition of its reportable segments and renamed its specialty insurance segment and specialty reinsurance segment to specialty insurance run-off segment and specialty reinsurance run-off segment. The Company created the Lloyd's segment for its Syndicate 4000 business, which was previously aggregated with its specialty insurance reportable segment. The inclusion of the results of Syndicate 4000 with the specialty insurance run-off operating segments is no longer appropriate given the different economic characteristics and the fact that the specialty insurance run-off segment is no longer writing new or renewal business while the Company's Lloyd's syndicate continues to seek to write new and renewal business. The Company also continues to earn premium in its insurance and reinsurance run-off segments related to business written in prior periods and related to extensions and renewals of policies which the Company is legally required to write in business lines the Company has exited.

As a result of the disposal of ESC, the technical services segment now consists only of the two environmental liability assumption programs, but without the results of ESC. The results of the technical services segment for the year ended December 31, 2005 have been reclassified to conform with the presentation of ESC in discontinued operations for the year ended December 31, 2006 resulting in the results of ESC for the years ending December 31, 2006 and 2005 no longer forming part of the reportable segments.

In determining how to aggregate its business lines, the Company considers many factors including the lines of business products, production and distribution strategies, geographic source of business and regulatory environments.

The Company has three geographic segments—Bermuda, the U.S. and Europe. These geographic segments represent the aggregation of legal entity locations where revenues, expenses, assets and liabilities are recorded.

The Company's specialty insurance run-off, specialty reinsurance run-off and Lloyd's (collectively referred to herein as "underwriting") reportable segments represent the Company's income and expenses from underwriting risks it retains. The technical services segment represents the Company's income and expenses from the provision of remediation services in respect of the assumed environmental liabilities.

The accounting policies of the segments are the same as those used in the preparation of the consolidated financial statements. The Company measures and evaluates each segment based on net underwriting or technical services income including other items of revenue and general and administrative expense directly attributable to each segment.

Because the Company does not manage its assets by segment, net investment income, depreciation and amortization and total assets are not evaluated at the segment level.

w) Self managed run-off

As part of its self-managed run-off, the Company intends to actively pursue certain transactions including but not limited to, commutations of assumed and ceded reinsurance transactions and loss portfolio transfers, that could materially affect the ultimate realized value of assets and liabilities recorded at December 31, 2007. The impact of the execution of these plans on the December 31, 2007 balance sheet cannot be determined at this time.

x) Commutations

The Company reports commutations in accordance with SFAS No. 113, “Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts” (“SFAS 113”).

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As the Company actively runs off its business lines it seeks to mitigate its exposures to historical underwriting risks through early settlement of its obligations to policyholders or ceding companies by entering into commutations or other arrangements. These negotiated commutation agreements eliminate the risk of adverse claim experience as they provide for full and final settlement of all current and future policy obligations with respect to the transaction to which they relate.

A commutation generally results in a single net payment to, or receipt from, a policyholder or ceding company. This payment or receipt settles all applicable outstanding balances with the policyholder or ceding company, including reserves for loss and loss expenses, unearned premiums, reinsurance balances payable, premiums receivable, deferred acquisition costs and funds withheld. Typically, the settlement of existing loss and loss expenses reserves is recorded as a paid claim, and settlement of unearned premiums is recorded as an adjustment to gross written and earned premiums, and acquisition expenses. Net gains or losses arising on commutation arrangements are primarily recorded within either net losses incurred, premiums earned, or a combination of both.

y) Recent accounting pronouncements

In December 2007, the FASB issued SFAS No. 141 (R), "Business Combinations" ("SFAS No. 141 (R)"). This standard establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. SFAS No. 141 (R) also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The guidance will become effective as of the beginning of the Company's fiscal year beginning after December 15, 2008. The Company is currently evaluating the effects of this statement on its financial reporting.

In December 2007, the FASB issued FASB Statement No. 160, "Noncontrolling Interests in Consolidated Financial Statements" ("SFAS 160"). SFAS 160 is an amendment of Accounting Research Bulletin No. 51 ("ARB No. 51") and its objective is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 is effective for both public and private companies for fiscal years beginning on or after December 15, 2008. The Company is currently evaluating the effects of this statement on its financial reporting.

In April 2007, the FASB issued Amendment of FASB Interpretation No. 39 ("FIN39-1"), "Offsetting of Amounts Related to Certain Contracts" ("Amendment to FIN 39"). This amendment to FIN 39 addresses whether a reporting entity that is party to a master netting arrangement can offset fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral against fair value amounts recognized for derivative instruments that have been offset under the same master netting arrangement in accordance with paragraph 10 of FASB Interpretation No. 39. FIN39-1 is effective for fiscal years beginning after November 15, 2007, with early application permitted. The Company is currently evaluating the effects of this Amendment on its financial reporting.

3. Disposal of ESC

Effective September 15, 2006, the Company sold all of its equity interests in ESC, which was part of the Company's technical services segment, to WSP Environmental Holdings, Inc. ("WSP") for total consideration of \$12.5 million represented by \$11.5 million in cash, after certain post-closing adjustments, plus forgiveness of intercompany debt of approximately \$1.0 million.

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The Company determined that the disposal of ESC should be presented as a discontinued operation in accordance with FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets" ("SFAS 144") and EITF 03-13, "Applying the conditions in Paragraph 42 of SFAS 144 in Determining whether to report Discontinued Operations" ("EITF 03-13"). In the third quarter of 2006, the Company has reclassified the results of operations related to ESC from its continuing operations to discontinued operations for all periods presented in accordance with SFAS 144 and EITF 03-13. These results are reflected in the Consolidated Statement of Operations as (loss) Income from operations of discontinued operations. The presentation of the reclassified segmental footnote and the reclassified statements of operations includes the previously eliminated inter-company transactions between ESC and the Company. The Company has separately disclosed the operating, investing and financing portions of the cash flows attributable to its discontinued operations, for which it reclassified amounts from the prior periods.

Following the disposal of ESC, ESC continued to provide technical services to the Company's two environmental liability assumption programs. The provision of technical services by ESC to the Company is expected to end during 2008, when the environmental sites are expected to be fully remediated. Therefore the Company's cash flows generated from the continuation of activities with ESC after the disposal are not expected to be significant and the Company is deemed not to have any continuing involvement in the operations of ESC after the disposal. During the period from September 16, 2006 to December 31, 2006, ESC provided technical services to the Company of \$0.2 million and for the year ended December 31, 2007 it provided technical services amounting to \$2.2 million.

The Company recognized income on disposal of ESC of \$0.7 million related to this transaction during the third quarter of 2006. This income is presented in the Consolidated Statement of Operations as Income on disposal of discontinued operations, a component of discontinued operations. The components of this income are summarized below.

				Cash proceeds from WSP(1)	\$ 11,484	Debt forgiveness
1,000	Total consideration	12,484	Less:	Carrying value of ESC(2)	(11,140)	Estimated transaction
costs	(640)	Income on disposal of ESC	\$ 704			

(1) Total

proceeds from WSP include post closing adjustments. (2) Net assets of ESC at September 15, 2006, prior to the impact of the sale transaction.

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As of September 15, 2006, the disposed assets and liabilities of ESC were as follows:

accounts receivable	7,581	Property and equipment	423	Assets: Cash and cash equivalents	\$ 1,527	Other	
assets	1,324	Total assets	13,582	Goodwill and other intangible assets	2,727	Other	
income and other liabilities	81	Total liabilities	2,442	Liabilities: Accounts payable and accrued expenses	2,361	Deferred	
		Net assets			\$ 11,140		

The following table details the inter-company costs charged by ESC to the Company for all periods presented. Prior to its disposal, ESC was included in the Company's technical services segment and ESC charged the Company's two environmental assumption liability programs ("QLT's"), also included in the Company's technical services segment, costs which were previously eliminated on consolidation at the technical services segment level. ESC also charged the Company's insurance run-off and reinsurance run-off segments, with costs related to technical services rendered and loss adjustment expenses, which previously eliminated on consolidation.

Period from
January 1,
2006 to
September 15,
2006 For the year
ended
December 31,

2005 Technical services revenues charged to QLT's	\$ 3,058	\$ 17,737	Technical services revenues charged to underwriting segment	506	3,234	Total inter-company revenues charged by ESC	\$ 3,564	\$ 20,971	Net losses and loss expenses	\$ (149)	\$ (165)	General and administrative expenses	(3,415)	(20,806)	Total inter-company costs charged to the Company	\$ (3,564)	\$ (20,971)
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The Company's (loss)/income from operations of discontinued operations generated by ESC, previously included in the technical services segment, now reported in discontinued operations were as follows:

Period from
January 1,
2006 to
September 15,
2006 For the year
ended
December 31,

2005 Technical services revenues	\$ 21,954	\$ 50,752	Other income	14	165	Direct technical services costs	(13,968)	(37,027)	General and administrative expenses	(7,725)	(9,129)	Impairment of goodwill	(12,561)	—	Depreciation of fixed assets and amortization of intangible assets	(647)	(988)	Income tax expense	(20)	(12)	(Loss) income from operations of discontinued operations	\$ (12,953)	\$ 3,761
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Technical services revenue, included in discontinued operations, is recognized when evidence of an arrangement for services exists, services have been rendered, the price is fixed or determinable, and collectability is reasonably assured. Technical services are rendered under various short-term contractual arrangements, primarily on a time and materials basis. From time to time, ESC retained subcontractors to perform certain remediation services under its contracts with customers.

Technical services revenue, included in discontinued operations, includes amounts related to services performed but not yet billed to customers at the period end. Accounts receivable include technical services revenues receivable that are settled within the Company's normal collection cycle.

Revenue is recognized on a gross basis in discontinued operations, which includes subcontractor remediation services, when the Company is the primary obligor in the arrangement. For the years ended December 31, 2006 and 2005, approximately \$6.2 million and \$24.9 million of direct costs, exclusive of profit mark-ups, related to these subcontractor arrangements was recorded as direct technical services costs in discontinued operations in the consolidated statement of operations.

Direct technical services costs, included in discontinued operations, consist of ESC's payroll costs associated with direct labor incurred on technical services engagements, other direct costs such as travel and subsistence, subcontracting and other contract expenses. ESC maintained a team of in-house technical services consultants that assisted in technical services engagements. The costs associated with the time spent by such technical services consultants on engagements are included in direct technical services costs in discontinued operations in the consolidated statement of operations.

The impairment of goodwill related to the discontinued operations is discussed further in Note 10.

ESC's technical services revenues include the inter-company revenues charged by ESC to the QLT's and to the Company's underwriting segments.

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4. Segment

information

The following tables summarize the Company's results before income taxes for each reportable segment for the years ended December 31, 2007, 2006 and 2005 based on the reportable segments in effect during the year ended December 31, 2007.

Year ended December 31, 2007 Statement of operations by segment									
Specialty	Specialty	Specialty	Specialty	Specialty	Specialty	Specialty	Specialty	Specialty	Specialty
insurance	run-off	Specialty	reinsurance	run-off	Lloyd's Underwriting	total	Technical	services	Consolidated
									Direct insurance
									\$ (20,973)
									\$ —
									\$ 124,049
									\$ 103,076
									\$ —
									\$ 103,076
									Reinsurance assumed
									69
									3,442
									—
									3,511
									—
									3,511
									Total gross premiums written
									(20,904)
									3,442
									124,049
									106,587
									—
									106,587
									Premiums ceded
									3,487
									(4,478)
									(27,654)
									(28,645)
									—
									Net premiums written
									\$ (17,417)
									\$ (1,036)
									\$ 96,395
									\$ 77,942
									\$ —
									\$ 77,942
									Net
									premiums earned
									\$ 6,127
									\$ 336
									\$ 80,784
									\$ 87,247
									\$ —
									\$ 87,247
									Technical services revenues
									—
									—
									—
									Other income
									(2,155)
									2,602
									—
									447
									—
									447
									Net losses and loss expenses
									16,621
									6,147
									(53,845)
									(31,077)
									—
									(31,077)
									Acquisition expenses
									(441)
									1,100
									(27,387)
									(26,728)
									—
									(26,728)
									General and administrative expenses
									(7,369)
									(1,357)
									(13,784)
									(22,510)
									(2,317)
									(24,827)
									Segment income (loss)
									\$ 12,783
									\$ 8,828
									\$ (14,232)
									\$ 7,379
									\$ (610)
									\$ 6,769
									Depreciation of fixed assets and impairment of intangible assets
									\$ (1,024)
									Interest expense
									(3,632)
									Net investment income
									41,900
									Net
									gains on investments
									5,818
									Corporate general and administrative expenses
									(35,039)
									Gain on repurchase of junior subordinated debentures
									4,421
									Net
									foreign exchange gains
									850
									Income from continuing operations before income taxes
									\$ 20,063

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Year ended December 31, 2006 Statement of operations by segment										
	Specialty		Specialty		Specialty		Specialty		Specialty	
	run-off	reinsurance	run-off	reinsurance	run-off	reinsurance	run-off	reinsurance	run-off	reinsurance
	Specialty	run-off	Specialty	run-off	Specialty	run-off	Specialty	run-off	Specialty	run-off
	Technical	Lloyd's	Technical	Lloyd's	Technical	Lloyd's	Technical	Lloyd's	Technical	Lloyd's
	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting	Underwriting
	Consolidated	Direct	Consolidated	Direct	Consolidated	Direct	Consolidated	Direct	Consolidated	Direct
	insurance	insurance	insurance	insurance	insurance	insurance	insurance	insurance	insurance	insurance
	services	services	services	services	services	services	services	services	services	services
assumed	12,194	6,864	—	19,058	—	19,058	Total gross premiums written	60,107	6,864	
91,758	158,729	—	158,729	Premiums ceded	(34,126)	(14,035)	(30,014)	(78,175)	—	
(78,175)	Net premiums written	\$ 25,981	\$ (7,171)	\$ 61,744	\$ 80,554	\$ —	\$ 80,554	Net premiums		
earned	\$ 113,289	\$ 46,487	\$ 65,523	\$ 225,299	\$ —	\$ 225,299	Technical services revenues	—	—	—
—	3,331	3,331	Other income	2,873	781	—	3,654	—	3,654	Net losses and loss expenses
(65,706)	(40,033)	(50,382)	(156,121)	—	(156,121)	Acquisition expenses	(18,029)	(12,468)		
)	(12,043)	(42,540)	—	(42,540)	General and administrative expenses	(18,440)	(6,420)			
(12,886)	(37,746)	(4,283)	(42,029)	Segment income (loss)	\$ 13,987	\$ (11,653)	\$ (9,788)	\$		
(7,454)	\$ (952)	\$ (8,406)	Depreciation of fixed assets and amortization and impairment of intangibles							
	\$ (4,999)	Interest expense	(5,458)	Net investment income			45,934	Net		
losses on investments	(15,945)	Corporate general and administrative expenses								
(57,977)	Net foreign exchange losses	(3,790)	Loss from continuing operations before income							
taxes	\$ (50,641)									

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		Year ended December 31, 2005 Statement of operations by segment				Specialty	
insurance							
run-off	Specialty						
reinsurance							
run-off	Lloyd's Underwriting						
total	Technical						
services	Consolidated Direct insurance	\$ 287,188	\$ —	\$ 80,702	\$ 367,890	\$ —	\$ 367,890
assumed	24,133	216,912	—	241,045	—	241,045	Total gross premiums written
216,912	80,702	608,935	—	608,935	Premiums ceded	(116,404)	(83,434)
(218,894)	—	(218,894)	Net premiums written	\$ 194,917	\$ 133,478	\$ 61,646	\$ 390,041
390,041	Net premiums earned	\$ 160,620	\$ 166,944	\$ 36,511	\$ 364,075	\$ —	\$ 364,075
services	revenues	—	—	19,037	19,037	Other income	1,200
3,174	Net losses and loss expenses	(120,710)	(178,887)	(24,652)	(324,249)	—	(324,249)
Acquisition	expenses	(21,836)	(42,714)	(5,074)	(69,624)	—	(69,624)
administrative	expenses	(21,750)	(9,847)	(8,716)	(40,313)	(18,545)	(58,858)
income	\$ (2,476)	\$ (62,530)	\$ (1,931)	\$ (66,937)	\$ 492	\$ (66,445)	Segment (loss)
	\$ (3,001)	Interest expense	(4,165)	Net investment income			27,181
Net losses on investments	(13,020)	Corporate general and administrative expenses					
(50,749)	Other income	387	Net foreign exchange gains			331	Loss from continuing
operations before income taxes		\$ (109,481)					

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The following tables summarize the Company's gross premiums written by geographic location for the years ended December 31, 2007, 2006 and 2005. The geographical segments represent the aggregation of legal entity locations where revenues, expenses, assets and liabilities are recorded.

2007	2006	2005	United States	\$ (11,403)	\$ 75,280	\$ 359,474	Bermuda	(4,742)	(8,705)
155,758	Europe	122,732	92,154	93,703	Total	\$ 106,587	\$ 158,729	\$ 608,935	

5. Income (loss) per share

The following table sets forth the computation of basic and diluted income (loss) per share.

2007	2006	2005	Net income (loss) from continuing operations	\$ 20,051	\$ (50,655)	\$ (109,713)
			Net (loss) income from discontinued operations	— (12,249)	3,761	Net income (loss)
(62,904)	\$ (105,952)		Gain on repurchase of preferred shares	2,364		Dividends on preferred shares
—	1,916	—	Net income (loss) to common shareholders	\$ 22,415	\$ (64,820)	\$ (105,952)
			Weighted average common shares outstanding – basic	70,076,562	69,971,646	57,205,342
			Weighted average common share equivalents:			
			Options	41,538	—	—
			Warrants	—	—	—
			Weighted average common shares outstanding – diluted	70,118,100	69,971,646	57,205,342
			Basic income (loss) per common share		Basic income (loss) from continuing operations per common share	\$ 0.29
(0.72)	\$ (1.92)		Basic net income (loss) from discontinued operations per common share	—	(0.18)	0.07
			Basic gain on repurchase of preferred shares per common share	0.03	—	—
			Basic dividends on preferred shares per common share	—	(0.03)	—
(1.85)			Basic income (loss) per common share	\$ 0.32	\$ (0.93)	\$
			Diluted income (loss) per common share		Diluted income (loss) from continuing operations per common share	\$ 0.29
			Diluted net income (loss) from discontinued operations per common share	—	(0.18)	0.07
			Diluted gain on repurchase of preferred shares per common share	0.03	—	—
			Diluted dividends on preferred shares per common share	—	(0.03)	—
			Diluted income (loss) per common share	\$ 0.32	\$ (0.93)	\$ (1.85)

For the year ended December 31, 2007, the calculation of weighted average common shares outstanding on a diluted basis excludes 573,004 options, 2,542,813 warrants and 14,419 performance share units, as the effect would have been anti-dilutive. For the years ended December 31, 2006 and

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2005, due to a net loss presented, the assumed net exercise of options, warrants and restricted shares under the treasury stock method has been excluded, as the effect would have been anti-dilutive. Accordingly, for the year ended December 31, 2006, the calculation of weighted average common shares outstanding on a diluted basis excludes 801,066 options, 2,542,813 warrants, 157,719 restricted shares and 27,219 performance share units. For the year ended December 31, 2005, the calculation of weighted average common shares outstanding on a diluted basis excludes 3,402,194 options, 2,542,813 warrants and 148,335 restricted shares.

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6. Investments

The cost or amortized cost, gross unrealized gains, gross unrealized losses and fair value of fixed maturity and short-term investments as of December 31, 2007 and 2006, are as follows:

December 31, 2007	Amortized								
cost or cost	Gross								
unrealized	gains								
unrealized	losses								
	Fair value	Trading:		Fixed maturities:		U.S. government and government			
sponsored agencies	\$ 263,320	\$ 4,223	\$ (55)	\$ 267,488	Foreign governments	11,486	134	(124)
11,496	Tax-exempt municipal	1,036	2	—	1,038	Corporate	62,827	1,040	(555)
Asset-backed securities	51,724	99	(420)	51,403	Mortgage-backed securities	165,932	383		
(1,548)	164,767	Total fixed maturities	556,325	5,881	(2,702)	559,504	Short-term investments		
88,880	—	88,880	Total trading investments	\$ 645,205	\$ 5,881	\$ (2,702)	\$ 648,384	Total	
investments	\$ 645,205	\$ 5,881	\$ (2,702)	\$ 648,384					

December 31, 2006	Amortized								
cost or cost	Gross								
unrealized	gains								
unrealized	losses								
	Fair value	Trading:		Fixed maturities:		U.S. government and government			
sponsored agencies	\$ 4,574	\$ 9	\$ (203)	\$ 4,380	Corporate	19,772	458	(1,494)	18,736
Asset-backed securities	4,571	18	(34)	4,555	Mortgage-backed securities	9,723	28	(582)	
9,169	Total fixed maturities	38,640	513	(2,313)	36,840	Short-term investments	433	—	—
433	Total trading investments	\$ 39,073	\$ 513	\$ (2,313)	\$ 37,273	Available for sale:			
Fixed maturities:						U.S. government and government sponsored agencies	\$ 363,142	\$ 3,719	
\$ —	\$ 366,861	Foreign governments	26,632	157	—	26,789	Tax-exempt municipal	1,039	—
1,039	Corporate	88,494	1,551	—	90,045	Asset-backed securities	37,656	239	—
Mortgage-backed securities	192,174	5,194	—	197,368	Total fixed maturities	709,137	10,860	—	
719,997	Short-term investments	89,886	19	—	89,905	Total available for sale securities	\$ 799,023		
\$ 10,879	\$ —	\$ 809,902	Total investments	\$ 838,096	\$ 11,392	\$ (2,313)	\$ 847,175		

With the early adoption of SFAS 159, all investments are now classified as trading at December 31, 2007, whereas at December 31, 2006 they were classified as available for sale with the exception of investments held in relation to the Company's deposit liabilities. Prior to the adoption of SFAS 159, due to the Company's decision to place most of its specialty insurance and reinsurance lines

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into orderly run-off, the Company concluded that it may no longer have the ability or intent to hold its available for sale securities for a sufficient period of time to allow recovery. Accordingly, during the years ended December 31, 2006 and 2005, the Company recorded \$16.9 million and \$10.2 million in other than temporary impairment losses in the consolidated statement of operations related to securities with any unrealized losses. Since the adoption of SFAS 159, both unrealized gains and losses are recognized in the consolidated statement of operations.

The following table shows how our fixed maturity investments are categorized in accordance with SFAS 157 at December 31, 2007:

	2007 Quoted prices in active market (Level I)	\$
88,880 Significant other observable inputs (Level II)	559,504 Fair value	\$ 648,384

The Company made its determination of appropriate categorization of investments based on descriptions of pricing practices provided by the Company's investment managers.

Short-term investments are categorized as Level I due to availability of an active market. All other fixed maturity investments are stated at fair value as determined by the broker-quoted market price of these securities and as provided either by independent pricing services or, when such prices are not available, by reference to broker or underwriter bid indications. Although the Company believes the majority of these securities could be classified as quoted on active markets they are not quoted on a public exchange and we can not be sure that there was an active market for each security on December 31, 2007. Therefore, the Company is classifying them as Level II.

Included in Level II is approximately \$5.4 million and \$6.2 million relating to the Company's exposure to subprime and Alt-A mortgages which represents 1.5% of total cash and investments at December 31, 2007. Alt-A mortgages are considered to be those made to borrowers who do not qualify for market interest rates but who are considered to have less credit risk than subprime borrowers. At December 31, 2007, the Company believes that although the market appeared to have been illiquid, all significant inputs relating to the overall fair value measurement were observable.

The Company does not believe that it has any securities that meet the definition of Level III, a valuation based on inputs that are unobservable and significant to the overall fair value measurement.

Contractual maturities of the Company's trading fixed maturities as of December 31, 2007 are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

December 31, 2007	Amortized cost			
or cost	Fair value	Fixed maturities:	Due in one year or less	\$ 173,155 \$ 173,213 Due after one year

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through five years	202,244	205,951	Due after five years	through 10 years	39,132	39,857	Due after 10
years	13,018	13,193	Total fixed maturities	\$ 427,549	\$ 432,214	Mortgage and asset-backed securities	
217,656	216,170	Total	\$ 645,205	\$ 648,384			

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Unaudited credit ratings of the Company's fixed maturities as of December 31, 2007 and 2006 are shown below.

December 31, 2007	December 31, 2006	Ratings *	Fair value	Percentage	Fair value	Percentage	AAA	\$					
571,370	88.1 %	\$ 730,271	86.2 %	AA	19,341	3.0 %	29,379	3.5 %	A	56,926	8.8 %		
76,543	9.0 %	BBB	747	0.1 %	7,950	0.9 %	Below BBB	—	— %	3,031	0.4 %	Total	\$
648,384	100.0 %	\$ 847,175	100.0 %										

* – ratings

as assigned by Standard & Poor's Corporation

The effects of the adoption of SFAS 159 on the Company's investments at January 1, 2007 are as follows:

Available
for sale

securities	Trading	Total Balance before adoption of SFAS 159	\$ 809,902	\$ 37,273	\$ 847,175	Cumulative effect adjustment of adoption of SFAS 159	(809,902)	809,902	—	Balance after adoption of SFAS 159	\$ —
\$ 847,175	\$ 847,175										

There was no effect on the Company's net deferred tax assets and liabilities at January 1, 2007 as a result of the adoption of SFAS 159.

The components of net investment income for the years ended December 31, 2007, 2006 and 2005 were derived from the following sources:

2007	2006	2005	Fixed maturities	\$ 27,253	\$ 35,669	\$ 26,879	Cash, cash equivalents and short-term investments	10,710	5,201	1,909	Gross investment income	37,963	40,870	28,788	Net amortization of discount/premium	5,460	6,705	(157)	Investment expenses	(1,523)	(1,641)
(1,450)			Net investment income	\$ 41,900	\$ 45,934	\$ 27,181															

Net gains (losses) on investment within the consolidated statement of operations for the year ended December 31, 2007, 2006 and 2005 consisted of the following:

2007	2006	2005	Net realized gains (losses) on investments	2,794	\$ (15,945)	\$ (13,020)	Net change in

fair market value of trading investments 3,024 — — Net gains (losses) on investments \$ 5,818 \$ (15,945)
\$ (13,020)

Gross realized pre tax investment gains and losses for the year ended December 31, 2007 were approximately \$3.2 million and \$0.4 million. Gross realized pre tax investment gains and losses for the year ended December 31, 2006 were approximately \$0.4 million and \$16.3 million. Gross realized pre

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tax investment gains and losses for the year ended December 31, 2005 were approximately \$4.4 million and \$17.4 million. For the year ended December 31, 2007 all gains and losses were realized from the sale of fixed maturity investments. For the years ended December 31, 2006 and 2005, all gains and losses were realized from the sale of fixed maturity investments, except for \$16.9 million and \$10.2 million of realized losses relating to other than temporary impairment charges and \$0.6 million and \$1.5 million of realized gains recognized on derivative investments.

7. Funds at Lloyd's

On December 9, 2004, Quanta 4000 Holding Company Ltd., on behalf of Quanta 4000, deposited with Lloyd's cash and investments having on the date of deposit a market value of £57.5 million, or \$107.9 million, to support the underwriting activities of Syndicate 4000. Between December 9, 2004 and March 1, 2007, Quanta 4000 was the sole member of Syndicate 4000 and committed 100% of its capital requirements. On March 1, 2007, Chaucer became a contributing member of Syndicate 4000 by committing to provide 10% of Syndicate 4000's capital requirements for the 2007 underwriting year and, subsequently, 20% of the capital requirements for the 2008 underwriting year. Quanta 4000 had committed to provide 90% and 80% of Syndicate 4000's capital requirement for the 2007 and 2008 underwriting years and maintained funds at Lloyd's for every underwriting year in which it has business through Syndicate 4000 at Lloyd's. The cash and investments were held by Lloyd's in its capacity as trustee of a Lloyd's Deposit Trust Deed (Third Party Deposit) dated December 23, 2004 and made between Quanta 4000 Holding Company Ltd., Quanta 4000, and Lloyd's, as security for the underwriting obligations of Syndicate 4000 (including certain obligations arising under Lloyd's byelaws and other rules). At the request of Quanta 4000 Holding Company Ltd. and Quanta 4000, Lloyd's had appointed a custodian to hold the cash and investments on its behalf and an investment manager to manage the cash and investments in accordance within certain investment objectives and restrictions agreed between Quanta 4000 Holding Company Ltd., Quanta 4000 and Lloyd's and in accordance with investment criteria and within restrictions specified by Lloyd's. The cash and investments held by Lloyd's are included within Notes 6 and 13(c). The return of this capital in February 2008, in conjunction with the sale of Quanta 4000, is discussed further in Notes 1 and 21.

The premium trust fund at Lloyd's holds the premiums written and received by Syndicate 4000. The amounts in the premium trust fund are used first to cover the expenses and future investments that may be necessary to support Syndicate 4000 obligations, then for the discharge of certain permitted trust outgoings and, thereafter, to the contributing members of Syndicate 4000 as a release of underwriting year profits as each underwriting year is closed which, in general, is after a three year period following the end of the underwriting year. Since the sale of the Company's interests in Syndicate 4000, more fully described in Note 21 below, the Company is no longer entitled to any profits of Syndicate 4000.

As of December 31, 2007, cash and investments with a market value of \$241.0 million were held by Lloyd's as trustee representing approximately \$105.2 million of premium trust funds and \$117.7 million of capital funds at Lloyd's. No additional cash and investments were required to be deposited with Lloyd's to support the syndicate's 2008 underwriting year. As of December 31, 2006, cash and investments with a market value of \$116.3 million were held by Lloyd's as trustee. No additional cash and investments were required to be deposited with Lloyd's to support the syndicate's 2007 underwriting year.

At December 31, 2007, in addition to its premium trust funds and capital funds at Lloyd's, the Company pledged a further \$18.1 million held on deposit pursuant to regulatory requirements. At December 31, 2006, in addition to its Funds at Lloyd's, the Company had cash and investments of \$64.9 million that were held in the premium trust funds for payments and discharge of certain trust outgoings, and a further \$8.4 million held on deposit pursuant to regulatory requirements.

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See also Note 21 in relation to subsequent events for Syndicate 4000.

8. Derivative instruments

The Company was exposed to potential loss on its derivative activities from various market risks, and managed these market risks based on guidelines established by management. Derivative instruments were carried at fair value with the resulting realized and unrealized gains and losses recognized in the consolidated statement of operations in the period in which they occurred. The change in fair value was included in other income in the consolidated statement of operations.

The following table summarizes these instruments and the effect on net loss and comprehensive loss for the years ended December 31, 2007, 2006 and 2005:

	2007	2006	2005	Net	
change in unrealized losses Net realized gains (losses) Net change in unrealized losses Net realized gains (losses) Net change in unrealized gains Net realized gains Investment derivatives				\$ —	\$ —
derivatives	—	—	(752)	216	42
Net realized and unrealized gains (losses) on derivatives	\$ (88)	\$ (608)	\$ 324	\$ 1,534	\$ —
a) Investment Derivatives					\$ 108
					\$ 1,492
					Mortality linked embedded

The Company had previously used foreign currency forward contracts to manage its exposure to the effects of fluctuating foreign currencies on the value of certain of its foreign currency denominated fixed maturity investments. These forward currency contracts were not designated as specific hedges for financial reporting purposes and, therefore, realized and unrealized gains and losses on these contracts were recorded in the consolidated statement of

operations in the period in which they occurred. These contracts generally had maturities of three months or less. As of December 31, 2007, 2006 and 2005, the net notional amount of foreign currency forward contracts, the net fair market value and the net unrealized losses were zero. For the year ended December 31, 2007, we had no net realized gains on settled foreign currency forward contracts. For the years ended December 31, 2006 and 2005, net realized gains on settled foreign currency forward contracts totaled approximately \$0.1 million and \$1.4 million.

During the years ended December 31, 2006 and 2005, the Company utilized other derivative instruments such as swaps and options to manage total investment returns in accordance with its investment guidelines and recognized net realized gains on these instruments of \$0.1 million and \$0.1 million. As of December 31, 2007, 2006 and 2005, the fair market value of other derivative instruments and net unrealized gains of other derivative instruments were zero.

b) Mortality linked embedded derivative

During the year ended December 31, 2005, the Company sold a mortality-risk-linked security that it had held since the fourth quarter of 2003. Simultaneously, it entered into a derivative total return swap agreement with an unrelated third party financial institution with reference to the same asset. The Company also entered into another derivative total return swap agreement with the same financial institution with reference to a similar mortality-risk-linked security. As a result, the Company retained all the risks and rewards of these two securities without having ownership of them. Income

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received from the total return swaps and any fair value adjustments was included in other income in the consolidated statement of operations. The Company recorded total return swaps at fair value, based on quoted market prices. Where such valuations were not available, the Company used internal valuation models to estimate fair value. The derivative total return swap agreement was subsequently terminated in April 2006. During the year ended December 31, 2005, the Company recorded \$0.1 million in unrealized losses associated with the change in fair value of these derivatives.

9.

Reinsurance

Syndicate 4000 utilized reinsurance principally to limit net exposures to losses. Syndicate 4000's reinsurance agreements provide for the recovery of a portion of losses and loss expenses from reinsurers. In addition, the Company remains party to reinsurance and retrocessional agreements on the business that is in run-off and those agreements also provide for the recovery of a portion of losses and loss expenses from reinsurers.

Reinsurance assets due from reinsurers include losses and loss adjustment expenses recoverable and deferred reinsurance premiums. The Company is subject to credit risk with respect to reinsurance ceded because the ceding of risk does not relieve the Company from its primary obligations to its policyholders. Failure of the Company's reinsurers to honor their obligations could result in credit losses. As at December 31, 2005 the Company recorded a provision for credit losses relating to losses and loss adjustment expenses recoverable of \$0.6 million which was increased during the year ended December 31, 2006 resulting in a provision as at December 31, 2006 of \$2.0 million. This was decreased during the year ended December 31, 2007 resulting in a provision as at December 31, 2007 of \$1.3 million, as described in Note 2(e). No amounts were written off during the years ended December 31, 2007, 2006 or 2005.

The following table lists the largest reinsurers measured by the amount of losses and loss adjustment expenses recoverable at December 31, 2007 and the reinsurers' financial strength rating assigned by A.M. Best:

Losses and Loss

Adjustment

Expenses

Recoverable A.M. Best

Rating	(\$ in millions)	Reinsurer	Everest Reinsurance Ltd.	\$ 51.4	A+	Arch Reinsurance	
Ltd.	14.3	A	Aspen Insurance Ltd.	11.3	A-	The Toa Reinsurance Company, Ltd. (Tokyo)	9.9
A			Various Lloyd's syndicates	9.3	A	General Fidelity	8.3
			Odyssey America Reinsurance Corporation	5.1	A	Glacier Reinsurance AG	4.3
			Reinsurance Ltd.	4.1	A-	Transatlantic Reinsurance Company	3.9
			Versicherungs AG	1.7	A-	XL Capital Ltd.	1.7
			All Other Reinsurers	5.1		Various	Total
							\$ 148.4

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The effect of reinsurance activity on premiums written, premiums earned and losses and loss expenses incurred for the years ended December 31, 2007, 2006 and 2005 is shown below.

		Year ended December 31,						
2007 Premiums								
Written Premiums								
Earned Losses and Loss								
Expenses Direct insurance	\$ 103,076	\$ 121,713	\$ 28,876	Reinsurance assumed	3,511	9,209	(6,997)	
) Gross	106,587	130,922	21,879	Ceded reinsurance	(28,645)	(43,675)	9,198 Net \$ 77,942	
\$ 87,247	\$ 31,077							

		Year ended December 31,						
2006 Premiums								
Written Premiums								
Earned Losses and Loss								
Expenses Direct insurance	\$ 139,671	\$ 273,694	\$ 156,471	Reinsurance assumed	19,058	108,197		
64,602 Gross	158,729	381,891	221,073	Ceded reinsurance	(78,175)	(156,592)	(64,952) Net	
\$ 80,554	\$ 225,299	\$ 156,121						

		Year ended December 31,						
2005 Premiums								
Written Premiums								
Earned Losses and Loss								
Expenses Direct insurance	\$ 367,890	\$ 246,955	\$ 226,712	Reinsurance assumed	241,045	270,537		
297,336 Gross	608,935	517,492	524,048	Ceded reinsurance	(218,894)	(153,417)	(199,799)	
Net	\$ 390,041	\$ 364,075	\$ 324,249					

Gross premiums written include \$24.9 million and \$97.8 million of returned gross premium associated with cancelled policies during the years ended December 31, 2007 and 2006. For the year ended December 31, 2005, there were no returned gross premiums written associated with cancelled policies.

10. Goodwill and other intangible assets

As a result of the Company's decision to cease underwriting and place most of its specialty insurance and reinsurance lines into orderly run-off, the Company determined that its U.S. insurance licenses had an indefinite useful life in accordance with Statement of Financial Accounting Standards No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets". The Company began amortizing these licenses to their estimated net realizable value over their estimated useful life during the year ended December 31, 2006, when, in connection with the preparation of a run-off

business plan, the Company determined that it was appropriate to evaluate the license asset for impairment, the results of which indicated that the license asset was impaired. Accordingly, the Company wrote down the asset to its estimated net realizable value of approximately \$7.4 million as of December 31, 2006 and ceased amortizing its U.S. insurance licenses. During the year ending December 31, 2007 the Company recorded a further charge for impairment of \$0.2 million resulting in

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an estimated net realizable value of approximately \$7.2 million as of December 31, 2007. The carrying amount of these intangible assets, which were not subject to amortization as of December 31, 2005, was \$9.1 million.

The carrying amount of goodwill, which primarily related to the Company's technical services segment, was \$12.6 million as of December 31, 2005. Included in this balance is a \$5.0 million earn-out payment that was contingent upon ESC achieving specified earnings targets during the two year period ended December 31, 2005 which was paid during 2006. During 2006, the Company determined that its goodwill asset of \$12.6 million related to its acquisition of ESC was impaired. The impairment was the result of the uncertain future outlook of ESC and a decline in expected technical services revenues in future periods given the Company's exit from its environmental insurance line of business. The impairment charge of \$12.6 million was recorded in the Company's results for the year ended December 31, 2006 and was charged to the technical services segment. Following the disposal of ESC, as described in Note 3, the impairment charge was reclassified in the consolidated statements of operations to (loss) income from discontinued operations.

11. Reserve for losses and loss adjustment expenses

The following table represents the activity in the reserve for losses and loss adjustment expenses for the years ended December 31, 2007, 2006 and 2005:

2007	2006	2005	Reserve for losses and loss adjustment expenses at beginning of period	\$ 623,618	\$ 533,983
	\$ 159,794		Losses and loss adjustment expenses recoverable (Net of paid recoveries of 2007: \$39,958, 2006: \$5,943 and 2005: \$0)	(181,270)	(184,410)
				(13,519)	
			Net reserve for losses and loss adjustment expenses at beginning of period	442,348	349,573
			Net losses and loss adjustment expenses incurred related to losses occurring in:		
			Current year	75,317	162,411
			Prior years	320,227	(44,240)
				(4,022)	(6,290)
			Total net incurred losses and loss adjustment expenses	31,077	156,121
			Net losses and loss adjustment expenses paid related to losses occurring in:		
			Current year	(4,709)	(13,678)
			Prior years	(84,634)	(53,910)
				(53,310)	
			Total net paid losses and loss adjustment expenses	(89,343)	(67,588)
			Foreign exchange (gain) loss	5,794	4,242
				(1,007)	
			Net reserve for losses and loss adjustment expenses at end of period	389,876	442,348
			Losses and loss adjustment expenses recoverable (Net of paid recoveries of 2007: \$13,228, 2006: \$39,958 and 2005: \$5,943)	135,212	181,270
			Reserve for losses and loss adjustment expenses at end of period	\$ 525,088	\$ 623,618
					\$ 533,983

During 2007, the Company refined its expected ultimate loss ratios for certain lines of business. The Company recorded a reduction of prior year loss reserves of \$44.2 million, including net favorable loss development of \$39.1 million. Of this amount, \$14.9 million in several product lines related to

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mature accident periods in which actual loss experience was better than expected, \$9.0 million related to the commutations of a number of our reinsurance policies, \$8.0 million in our Lloyd's segment, \$6.7 million related to the 2005 and 2004 hurricanes and \$0.5 million on tornadoes that occurred in the first quarter of 2006. The remaining \$5.1 million relates to a reduction in reserves primarily on our HBW program due to the cancellation of policies in the year.

Approximately \$14.9 million of net favorable loss development has been recorded in several of the Company's product lines, including professional, environmental, the property component of the Company's HBW program, fidelity, property and casualty and surety product lines. The Company's HBW program consists of one third party agent that sources the residential builders' and contractors' program that provides new home contractors throughout the U.S. with general liability, builders' risk and excess liability insurance coverages as well as reinsurance for warranty coverage ('HBW'). Actual loss experience in these product lines was better than expected in mature accident periods.

The Company recognized net gains on commutation of reinsurance contracts of approximately \$9.7 million which consisted of net favorable loss development of approximately \$9.0 million and other income of \$1.9 million. This amount was partially offset by returned earned premium of approximately \$1.3 million. The commutations net payments resulted in a reduction in net loss and loss expenses reserves of approximately \$47.1 million and a reduction in premium receivables of approximately \$15.6 million.

During the year ended December 31, 2007, the Company has experience net favorable loss development of \$8.0 million in relation to its Lloyd's segment. This is due to net favorable loss development in the 2005 underwriting year of account and, to a lesser extent, the 2006 underwriting year of account.

During the year ended December 31, 2007, the Company's estimated ultimate net losses and loss adjustment expenses experienced favorable development of \$5.8 million related to Hurricanes Katrina, Rita and Wilma ('2005 Hurricanes'), which represents the Company's best estimate of losses based upon information currently available. The Company's estimate of ultimate losses from these events is primarily based on claims received to date, industry loss estimates, a review of affected contracts and discussion with cedants and brokers. While the Company believes that its reserves for the 2005 Hurricanes are adequate, the exact losses will be unknown for some time given the uncertainty around the industry loss estimates, the size and complexity of the 2005 Hurricanes, limited claims data and potential legal and regulatory developments related to potential losses. As a result, the Company's losses may vary significantly from the recorded estimates.

The net losses incurred for the year ended December 31, 2007 amounted to \$75.3 million and include approximately \$9.8 million of net loss and loss expenses recorded in our Lloyd's segment related to our estimate of claims associated with Syndicate 4000's professional liability exposure to the subprime mortgage developments in the United States. The policies on which these losses were incurred are claims made policies. In relation to the subprime exposure, multiple methods were used to derive an estimate of the ultimate cost of losses. These included using the industry estimate of ultimate losses and calculating the Company's ultimate cost of losses based on Syndicates 4000's share of the market premium. Also, the Company used an internal loss exposure analysis commissioned by Syndicate 4000 based on the risk characteristics of the Syndicate 4000 Portfolio of policies written. Furthermore, the Company has recorded a premium deficiency reserve amounting to approximately \$8.0 million. This reserve relates to the write-off of deferred

acquisition costs that are deemed irrecoverable from the future earning of unearned premium reserves because the Company expects that potential future subprime reported losses may exceed those unearned premium reserves. This adjustment has been reflected in the consolidated statement of operations through acquisition costs. While the Company believes that its reserves for its exposure to the subprime mortgage developments are adequate, the exact losses will be unknown for some time given the uncertainty around the

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industry loss estimates, the complexity of the subprime mortgage developments, limited claims data and potential legal and regulatory developments related to potential losses. As a result, the Company's losses may vary significantly from the recorded estimates.

During the year ended December 31, 2006, the Company recorded net favorable development on prior year loss reserves of \$6.3 million. Included in this net favorable development was approximately \$13.9 million of favorable developments in several of its product lines, including fidelity, the property component of HBW, environmental, professional and surety product lines. Actual loss experience in these product lines was better than expected in maturing accident periods. This was offset by \$5.0 million of adverse development on the 2005 Hurricanes and \$2.6 million of adverse development related to an environmental oil pipeline claim that occurred in 2005.

During the year ended December 31, 2005, the Company recorded net adverse development on prior year loss reserves of \$4.0 million, including \$5.9 million of adverse development on the 2004 Hurricanes in the property reinsurance and marine, technical risk and aviation product lines and was partially offset by favorable development on other product lines.

Management believes that the assumptions used represent a realistic and appropriate basis for estimating the reserve for losses and loss adjustment expense as of December 31, 2007, 2006 and 2005. However, these assumptions are subject to change and the Company continually reviews and adjusts its reserve estimates and reserving methodologies taking into account all currently known information and updated assumptions related to unknown information. While management believes it has made a reasonable estimate of loss expenses occurring up to the consolidated balance sheet date, the ultimate costs of claims incurred could exceed the Company's reserves and have a materially adverse effect on its future results of operations and financial condition.

12. Junior subordinated debentures

On December 21, 2004, the Company participated in a private placement of \$40.0 million of floating rate capital securities (the "2004 Trust Preferred Securities") issued by Quanta Trust, which have since been repurchased, as discussed below. The 2004 Trust Preferred Securities were due to mature on March 15, 2035, were redeemable at the Company's option at par beginning March 15, 2010, and required quarterly distributions of interest by Quanta Trust to the holder of the 2004 Trust Preferred Securities. Distributions would have been payable at a variable per annum rate of interest, reset quarterly, equal to the London Interbank Offered Rate ("LIBOR") plus 385 basis points, which equated to an interest rate of 6.37% at December 31, 2004. Quanta Trust simultaneously issued 1,238 of its common securities to the Company for a purchase price of \$1.2 million, which constituted all of the issued and outstanding common securities of Quanta Trust. The Company's investment of \$1.2 million in the common shares of Quanta Trust was recorded in other assets in the consolidated balance sheet.

Quanta Trust used the proceeds from the sale of the 2004 Trust Preferred Securities and the issuance of its common securities to purchase \$41.2 million junior subordinated debt securities, due March 15, 2035, in the principal amount of \$41.2 million issued by the Company (the "2004 Debentures"). The net proceeds of the transaction were \$38.8 million, after the deduction of approximately \$1.2 million of commissions paid to the placement agents in the transaction and approximately \$1.2 million representing the Company's investment in Quanta Trust.

On February 24, 2005, the Company participated in a private placement of \$20.0 million of floating rate capital securities (the “2005 Trust Preferred Securities” and, together with the 2004 Trust Preferred Securities, the “Trust Preferred Securities”)) issued by Quanta Trust II, which have since been repurchased, as described below. The 2005 Trust Preferred Securities were due to mature on June 15, 2035, were redeemable at the Company’s option at par beginning June 15, 2010, and required

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quarterly distributions of interest by Quanta Trust II to the holder of the 2005 Trust Preferred Securities. Distributions would have been payable at a variable per annum rate of interest, reset quarterly, equal to the LIBOR plus 350 basis points. Quanta Trust II simultaneously issued 619 of its common securities to the Company for a purchase price of \$0.6 million, which constituted all of the issued and outstanding common securities of Quanta Trust II. The Company's investment of \$0.6 million in the common shares of Quanta Trust II was recorded in other assets in the consolidated balance sheet.

Quanta Trust II used the proceeds from the sale of the 2005 Trust Preferred Securities and the issuance of its common securities to purchase \$20.6 million junior subordinated debt securities, due June 15, 2035, in the principal amount of \$20.6 million issued by the Company (the "2005 Debentures" and, together with the 2004 Debentures, the "Debentures"). The net proceeds of the transaction were \$19.6 million from the sale of the debentures to Quanta Trust II, after the deduction of approximately \$0.4 million of commissions paid to the placement agents in the transaction and approximately \$0.6 million representing the Company's investment in Quanta Trust II.

The Debentures were issued pursuant to Indentures (the "Indentures"), dated December 21, 2004 in respect of Quanta Trust and dated February 24, 2005 in respect of Quanta Trust II, by and between the Company and HSBC Bank USA, National Association, as successor trustee to JPMorgan Chase Bank, N.A., as trustee. The terms of the Debentures were substantially the same as the terms of the Trust Preferred Securities. The interest payments on the Debentures paid by the Company were used by Quanta Trust and Quanta Trust II to pay the quarterly distributions to the holders of the Trust Preferred Securities. The Indentures permitted the Company to redeem the Debentures (and thus a like amount of the Trust Preferred Securities) on or after March 15, 2010 in respect of Quanta Trust and June 10, 2010 in respect of Quanta Trust II. If the Company redeemed any amount of the Debentures, Quanta Trust and Quanta Trust II would have been obligated to redeem a like amount of the Trust Preferred Securities.

Pursuant to Guarantee Agreements (the "Guarantee Agreements"), dated December 21, 2004 in respect of Quanta Trust and dated February 24, 2005 in respect of Quanta Trust II, by and between the Company and HSBC Bank USA, National Association, as successor trustee to JPMorgan Chase Bank, N.A., as trustee, the Company agreed to guarantee the payment of distributions and payments on liquidation or redemption of the Trust Preferred Securities, but only in each case to the extent of funds held by Quanta Trust and Quanta Trust II. The obligations of the Company under the Guarantee Agreements and the Trust Preferred Securities were subordinated to all of the Company's debt.

The issuance costs incurred related to Quanta Trust and Quanta Trust II were capitalized and were included in other assets in the consolidated balance sheet. Issuance costs are being amortized over the term of the Debentures as a component of interest expense.

Quanta Trust and Quanta Trust II were determined to be Variable Interest Entities ("VIE") under FASB Interpretation No. 46(R) "Consolidation of Variable Interest Entities ("FIN46(R)"). The Company was not determined to be the primary beneficiary of Quanta Trust and Quanta Trust II and in accordance with FIN46(R) has not consolidated Quanta Trust and Quanta Trust II in the consolidated financial statements. The earnings of Quanta Trust and Quanta Trust II were included in the consolidated statement of operations and comprehensive (loss) income.

On November 29, 2006, the Company exercised its right under the Indentures described above and provided notice that it had elected to defer payments of interest on its Junior Subordinated Debt Securities due March 15, 2035 and June 15, 2035 under the related Indentures dated December 21, 2004 and February 24, 2005, respectively, until March 15, 2007. As a consequence of this deferral, the Company was precluded from paying dividends or distributions, redeeming,

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purchasing, acquiring or making liquidation payments on its 10.25% Series A Preferred Shares and its common stock until after it had paid all interest presently deferred and any interest deferred in the future. At December 31, 2006 the Company had accrued interest of \$1.6 million. At December 31, 2005 the Company did not have accrued interest.

On August 22, 2007, the Company repurchased all of the Trust Preferred Securities from the Trusts for an aggregate purchase price of \$54.5 million resulting in a gain on repurchase of \$4.4 million, net of repurchase costs of \$0.5 million and the write off of original deferred issuance costs of \$1.7 million.

The effect of the repurchase on the basic and diluted income per common share amounted to \$0.06 per common share for the year ended December 31, 2007.

There was no tax effect for the Company in relation to the repurchase of the Trust Preferred Securities of the Company for the year ended December 31, 2007.

Following the repurchase of the Trust Preferred Securities, the Company cancelled the Trust Preferred Securities, dissolved the Trusts and terminated the Declarations, the Guarantees, the Debentures and the Indentures.

13. Concentrations, commitments and contingencies

a) Concentrations of credit risk

As of December 31, 2007 substantially all of the Company's cash and cash equivalents, and investments were held by two custodians. As of December 31, 2006 and 2005, substantially all of the Company's cash and cash equivalents, and investments were held by three custodians. Management believes these custodians to be of high credit quality. The Company's investment portfolio is managed by external investment advisors in accordance with the Company's investment guidelines. The Company's investment guidelines require that the average credit quality of the investment portfolio is typically Aa3/AA- and that no more than 5% of the investment portfolio's market value shall be invested in securities rated below Baa3/BBB-. The Company also limits its exposure to any single issuer to 5% or less of the total portfolio's market value at the time of purchase, with the exception of U.S. government and agency securities. As of December 31, 2007, 2006 and 2005, the largest single non-U.S. government and government agencies issuer accounted for less than 2% of the aggregate market value of the externally managed portfolios.

At December 31, 2007 and 2006 the Company had a provision for uncollectible premiums receivable of \$0.4 million and \$0.9 million. The Company did not record any provision for uncollectible premiums receivable for the year ended December 31, 2005. No balances were written off during the years ended December 31, 2007, 2006 and 2005.

Concentrations related to reinsurance assets due from reinsurers are discussed further in Note 9.

b) Concentrations of premium production

During the years ended December 31, 2007, 2006 and 2005, Syndicate 4000 accounted for approximately \$124.0 million, or 116.3%, \$91.8 million, or 57.8%, and \$80.7 million, or 13.3%, of the gross written premiums. For

the year ended December 31, 2007, the gross written premiums generated by Syndicate 4000 exceeded 100% of the total gross written premiums generated by the Company primarily relating to cancellations and terminations of insurance and reinsurance policies.

Syndicate 4000 generates its business primarily through brokers and to a much lesser extent direct relationships with insurance companies. During the year ended December 31, 2007, two brokers

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accounted for approximately 19% and 17% of the gross premiums written. No other brokers accounted for more than 10% of the underwriting segment's gross written premium for the year ended December 31, 2007. During the year ended December 31, 2006, two brokers accounted for approximately 21% and 14% of the Lloyd's segment's gross premiums written. No other brokers accounted for more than 10% of the underwriting segment's gross written premium for the year ended December 31, 2006.

During the years ended December 31, 2006 and 2005, the HBW program accounted for \$61.9 million, or 39.0%, and \$165.9 million, or 27.2%, of the Company's gross written premiums for those years. During the year ended December 31, 2007, the HBW program returned gross written premiums amounting to \$12.8 million.

c) Restricted assets

The Company is required to maintain assets on deposit with various regulatory authorities to support its insurance and reinsurance operations. These requirements are generally promulgated by the regulations of the individual locations within which the Company operates. These funds on deposit are available to settle insurance and reinsurance liabilities.

Until February 2008, the Company participated in the Lloyd's of London market through Syndicate 4000 and has dedicated a significant amount of its capital to the Lloyd's business. The regulations of the Council of Lloyd's determine the amount of premium that may be written, also known as stamp capacity, based on the Company's funds at Lloyd's. Funds at Lloyd's are discussed further in Note 7.

The Company has also issued letters of credit ("LOC") under its Credit Agreement described in Note 18, for which cash and cash equivalents and investments are pledged as security and in favor of certain ceding companies to collateralize its obligations under contracts of insurance and reinsurance. As of December 31, 2007 the Company had \$91.6 million of face amount of fully secured letters of credit issued and outstanding under its Credit Agreement

The Company also utilizes trust funds in certain large transactions where the trust funds are set up for the benefit of the ceding companies, and generally take the place of letter of credit requirements. In addition, the Company holds cash and cash equivalents and investments in trust to fund the Company's obligations associated with the assumption of environmental remediation liability.

The fair values of these restricted assets by category at December 31, 2007 and 2006 are as follows:

2007	2006	Cash and cash equivalents	Investments	Cash and cash equivalents	Deposits with U.S. regulatory authorities	Funds deposited with Lloyd's(1)	Trust funds	LOC pledged assets	Amounts held in trust funds
111,154	129,819	52,838	136,788	9,602	17,213	979	28,888	211	
111,889	2,520	271,129	10,046	143,740	9,331	191,463			

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related to deposit liabilities — 39,195 2,475 36,840 Total \$ 131,013 \$ 441,856 \$ 68,143 \$ 665,108

(1) The above includes funds held by Syndicate 4000 as well as those held by Quanta 4000 Holdings. See Note 21 for subsequent events in relation to Syndicate 4000.

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d) Lease commitments

The Company leases office space and furniture and equipment under operating lease agreements. Certain office space leases include an escalation clause that calls for annual increases to the base rental payments. Rent expenses are being recognized on a straight-line basis over the respective lease terms. Future annual minimum payments under non-cancelable operating leases, are as follows:

						Year ending December 31, 2008
\$ 1,150	2009	1,155	2010	1,052	2011	603 2012 and thereafter
						560 Total
						\$ 4,520

Total rent expense under operating leases for the years ended December 31, 2007, 2006 and 2005, was approximately \$1.4 million, \$5.4 million and \$5.3 million.

Effective January 2007, the Company entered into a new lease for offices of the Company's U.S. subsidiaries' operations in downtown New York. Also effective January 2007, the Company entered into a lease assignment transaction which relieves the Company of all obligations under a lease of office space used by the Company's U.S. subsidiaries through mid-February 2007. Effective September 15, 2007, the Company entered into a new lease for offices for the Company's Bermuda operations. The future minimum lease payments above have been adjusted to reflect these leasing transactions.

e) Taxation

Quanta Holdings is a Bermuda corporation and, except as described in Note 14 below, neither it nor its non-U.S. subsidiaries have paid or provided for U.S. income taxes on the basis that they are not engaged in a U.S. trade or business or otherwise subject to taxation in the U.S. However, because definitive identification of activities which constitute being engaged in a trade or business in the U.S. is not provided by the Internal Revenue Code of 1986, regulations or court decisions, there can be no assurance that the Internal Revenue Service will not contend that the Company or its non-U.S. subsidiaries are engaged in a U.S. trade or business or otherwise subject to taxation. If the Company or its non-U.S. subsidiaries were considered to be engaged in a trade or business in the U.S., the Company or such subsidiaries could be subject to U.S. tax at regular corporate tax rates on its taxable income, if any, that is effectively connected with such U.S. trade or business plus an additional 30% "branch profits" tax on such income remaining, if any, after the regular corporate taxes, in which case there could be a significant adverse effect on the Company's results of operations and its financial condition.

f) Employment agreements

The Company has entered into employment agreements with certain officers and key employees that provide for severance payments and executive benefits under certain circumstances.

g) Litigation

On February 5, 2007, plaintiff Harold Zirkin filed a complaint against the Company in the U.S. District Court for the Southern District of New York, Zirkin v. Quanta Capital Holdings, Ltd. et al., U.S. District Court, Southern District of New York, Case No. 07 CV 851. On February 26, 2007,

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plaintiff Jorge Coronel filed a complaint against the Company in the same Court, *Coronel v. Quanta Capital Holdings, Ltd. et al.*, U.S. District Court, Southern District of New York, Case No. 07 CV 1405. Both complaints alleged that the Company violated the federal securities laws as a result of false or misleading statements in disclosures to the investing public.

Both of these cases are now pending before U.S. District Judge Robert P. Patterson, Jr. On May 7, 2007, Judge Patterson appointed Zirkin-Cutler Investments, Inc. (“Zirkin”) as lead plaintiff for a putative class of investors who purchased our preferred shares, and appointed Washington State Plumbing and Pipefitting Pension Trust (“Washington”) as lead plaintiff for a putative class of investors who purchased our common shares. Judge Patterson directed Zirkin and Washington to file amended pleadings that would supersede the complaints previously filed by Mr. Zirkin and Mr. Coronel.

On July 16, 2007, Zirkin filed an amended complaint (the “Zirkin Complaint”). Zirkin purports to sue on behalf of itself and a class of investors who purchased preferred shares of the Company between December 14, 2005 and March 2, 2006. The Zirkin Complaint alleges that the Company made false statements concerning reserves for hurricane-related losses in a registration statement and prospectus that were circulated to investors in connection with a securities offering the Company completed in December 2005. The Complaint alleges that the Company is liable under Sections 11 and 12(a)(2) of the Securities Act of 1933.

Zirkin has named as defendants, in addition to the Company, two firms that served as underwriters for this offering (Friedman, Billings, Ramsey & Co., Inc. (“FBR”) and BB&T Capital Markets (“BBT”)), and six individuals who served as officers or directors of the company at the time of the offering (James Ritchie, Jonathan Dodd, Robert Lippincott III, Michael Murphy, Nigel Morris, and W. Russell Ramsey).

Washington filed a separate amended complaint (the “Washington Complaint”) on July 16, 2007. Washington purports to sue on behalf of itself and a class of investors who purchased our common shares between October 4, 2005 and April 3, 2006. The Washington Complaint alleges that during that period, the Company made false and misleading statements, and omitted to state material information, in various disclosures. The disclosures and alleged omissions at issue in the case relate to reserves for hurricane-related losses, reserves related to an oil pipeline leak, and the quality of the Company’s internal controls over financial reporting. The Washington Complaint alleges claims against the Company under Sections 11 and 12(a)(2) of the Securities Act of 1933, based on statements made in connection with the above-referenced securities offering and under Section 10(b) of the Securities Act of 1934 and Rule 10b-5 promulgated thereunder, based on statements made at various times and contexts.

The Company, FBR, BBT, and the six individuals named as individual defendants in the Zirkin Complaint (Messrs. Ritchie, Dodd, Lippincott, Murphy, Morris, and Ramsey) are all named as defendants in the Washington Complaint as well. In addition, the Washington Complaint also names as a defendant Tobey Russ (former Chairman of the Company’s Board of Directors and former Chief Executive Officer).

In September 2007, the Company filed motions challenging the legal sufficiency of the claims asserted in both cases, and asked the Court to dismiss both cases. The briefing on these motions was completed in January 2008, but the Court has not yet addressed the motions. In accordance with the Private Securities Litigation Reform Act, discovery in

these cases has been stayed pending a ruling by the Court on the motions.

The court has not yet made any rulings addressing the merits of these cases, nor has the court decided whether it will certify any case against the Company to proceed as a class action. The Company intends to continue to defend these actions vigorously.

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In the normal course of business, we are involved in various claims and legal proceedings, including litigation and arbitration. Management does not believe that the eventual outcome of any such pending ordinary course of business litigation or arbitration is likely to have a material effect on our financial condition. Many of our insurance and reinsurance arrangements require disputes thereunder to be finally settled by binding arbitration. Assets and liabilities which are or may be the subject of arbitration are reflected in the financial statements based on management's estimates of the ultimate amount to be realized as paid.

h) Non-traditional statutory surplus relief contract

During the year ended December 31, 2004, the Company wrote a non-traditional statutory surplus relief life reinsurance contract that was deemed not to meet the risk transfer criteria promulgated by FASB Statement No. 113, "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts" ("SFAS 113") and was therefore accounted for as a deposit under SFAS 113. Under this contract, the Company provided reinsurance on certain underlying life insurance contracts written by its client, a U.S. life insurance company. The client is subject to insurance regulation in the United States and, therefore, is required to maintain a certain amount of statutory capital. The client was entitled to reduce its statutory capital requirements as a result of entering into a reinsurance contract with the Company. The reinsurance transaction was done partially on a funds withheld basis under which some funds are held by the life insurance company. The Company receives fees for this transaction. Other than receipt of the fees, there were no net cash flows at inception of this contract, nor were there expected to be net cash flows other than fees through the life of the contract. The Company monitors this transaction on a quarterly basis to, among other things, ensure that the performance of the underlying life insurance policies is in line with the representations made by the client to the Company. During the Company's monitoring process in 2007, it became apparent that this transaction was not performing as anticipated. The Company continues to obtain facts to evaluate and to analyze the performance of the life insurance policies that are underlying this transaction. The Company continues to evaluate the validity of data received from the client and the validity of risks ceded to it by its client as provided for by the terms of the reinsurance contract. On February 27, 2008, the Company exercised its right to cancel the contract ab initio as it believes there have been material breaches of the contract as defined within the contract. As a result of this rescission notice, and in accordance with the cancellation provisions in the contract, the Company at December 31, 2007 has recorded the return of all fee income, net of commissions, in the amount of \$3.7 million reflecting net fee income earned since inception of the contract. Included in contingencies on the consolidated balance sheet is an amount of \$2.5 million of fees due to be returned upon the rescission of this contract. In addition the Company has recorded an estimated \$1.0 million in legal costs that may be incurred in pursuing cancellation and any other legal remedies. The Company has provided approximately \$29.6 million of letter of credit and trust collateral in support of the amount of statutory surplus relief that the U.S. life insurance company has obtained. While the final outcome cannot be ascertained at this time, based on current facts and circumstances, knowledge of the data that has been received and the Company's understanding of the original contract, the Company believes that the outcome could have a further material adverse effect on its financial position and results of operations in the future. The Company will continue to pursue any legal remedies against the insurance company that it believes are available and warranted under the circumstances.

14.

Taxation

Under current Bermuda law, the Company and its Bermuda subsidiaries are not required to pay any taxes in Bermuda on its income or realized capital gains. The Company has received an undertaking from the Minister of Finance of Bermuda that, in the event of any taxes being imposed, the Company will be exempt from taxation in Bermuda until March 2016.

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Quanta U.S. Holdings Inc. (“Quanta U.S. Holdings”) and its operating subsidiaries are subject to income taxes imposed by U.S. authorities. The Company’s operating units in the United Kingdom and Ireland are subject to the relevant income taxes imposed by those jurisdictions.

Effective August 15, 2003, Quanta Reinsurance U.S. Ltd. (“Quanta Re U.S.”) made an election under Section 953(d) of the Internal Revenue Code of 1986 (“IRC”), as amended, to be treated as a domestic corporation for United States federal income tax purposes. As a result of the “domestic election”, Quanta Re U.S. is subject to U.S. taxation on its worldwide income as if it were a U.S. corporation.

Quanta U.S. Holdings together with its operating subsidiaries have elected to file a consolidated U.S. tax return. Under IRC Section 953(d), net operating losses generated by Quanta Re U.S. may only be carried back two years and forward twenty years and offset past or future U.S. federal taxable income that is generated by Quanta Re U.S.

The Company is not subject to taxation other than as stated above. There can be no assurance that there will not be changes in applicable laws, regulations or treaties, which might require the Company to become subject to additional taxation (see Note 13(e)).

The consolidated income tax provisions for the years ended December 31, 2007, 2006 and 2005 are as follows:

Continuing operations:

2007	2006	2005	Current tax expense	\$ —	\$ —	\$ —	U.S. Federal	—	—	—	U.S. State	12	14	232
	Non-U.S.	5,277	—	—	Total current expense	5,289	14	232	Deferred tax expense (benefit)					
	U.S. Federal	(2,042)	(19,178)	(10,034)	U.S. State	—	—	—	Non-U.S.	(6,784)	(5,173)			
	(1,413)	Change in valuation allowance	3,549	24,351	11,447	Total deferred benefit	(5,277)	—	—					
	Total income tax expense	\$ 12	\$ 14	\$ 232										

As described above, on September 15, 2006 ESC was sold. ESC was a single member Limited Liability Company that had been disregarded for tax purposes and thus did not incur any stand alone tax liability. Its sale was treated as a sale of assets by its member.

No current U.S. Federal or foreign income taxes were paid or payable during the years ended December 31, 2007, 2006 and 2005. For the year ended December 31, 2007, current non-U.S. taxes payable were \$5.3 million. No non-U.S. taxes were payable for the years ended December 31, 2006 and 2005.

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Income tax benefit attributable to income for the years ended December 31, 2007, 2006 and 2005 differed from amounts computed by applying the U.S. federal income tax rate of 35% to income before taxation as a result of the following:

Continuing operations:

2007	2006	2005	Computed	expected	tax expense (benefit)	\$ 7,018	\$ (22,687)	\$ (37,083)	Foreign	
(income)/loss	not subject to U.S. tax	(10,300)	(632)	24,637	Loss from controlled foreign corporation					
34	455	—	Income subject to tax at foreign rates	922	1,670	653	Loss on sale of ESC	—	(5,028)	
—	State taxes	12	14	232	Reversal of deferred taxes	(1,246)	4,018	—	Effect of valuation allowance	
3,549	24,351	11,447	Other	23	(2,147)	346	Actual income tax expense	\$ 12	\$ 14	\$ 232

Deferred income taxes reflect the tax impact of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and those for income tax purposes. The significant components of the net deferred tax assets and liabilities as of December 31, 2007 and 2006 are as follows:

										2007																			
2006	Deferred tax assets:	Bonus provisions	\$ 1,108	\$ 1,890	Reserves for losses and loss adjustment expenses	3,751	3,512	Unearned premiums	705	1,278	Deferred income	—	87	Net unrealized investment losses	935	1,422	Net operating loss carry forwards	42,400	33,783	Write down of goodwill	664	603	Capital loss from sale of ESC	4,701	4,418	Other than temporary impairments	2,701	2,211	
		Depreciation of property and equipment	346	225	Deferred acquisition costs	—	149	Net unrealized currency losses	529	427	Other	335	169	Total deferred tax assets	58,175	50,174	Valuation allowance	(50,942)	(49,141)	Total deferred tax assets net of valuation allowance	7,233	1,033	Deferred tax liabilities:	Deferred acquisition costs	(207)	—	Amortization of intangible assets	(838)	(686)
) Investments	(911)	(347)	Total deferred tax liabilities	(1,956)	(1,033)	Net deferred tax asset	\$ 5,277	\$ —																			

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As of December 31, 2007, the Company has a net deferred tax asset relating to net operating loss carry forwards (“NOL”) of approximately \$42.4 million (of which \$28.3 million relates to the NOL in the United States (“U.S. NOL”), \$11.7 million relates to the NOL in the United Kingdom (“U.K. NOL”) and \$2.4 million relates to the NOL in Ireland (“Irish NOL”). As of December 31, 2007 and 2006, approximately \$26.0 million and \$22.4 million of the net operating loss carry forwards are dual consolidation losses generated by Quanta Re U.S. and can only be used to offset future taxable income earned by Quanta Re U.S.

As of December 31, 2006, the Company had a net deferred tax asset relating to NOL carryforwards of approximately \$33.8 million (of which \$27.1 million relates to U.S. NOL, \$5.9 million relates to U.K. NOL and \$0.8 million relates to Irish NOL), which are available to offset future taxable income.

The U.S. NOL expires in 2027 while the U.K. NOL and Irish NOL currently do not have an expiry date.

As of December 31, 2007, the Company had a deferred tax asset related to capital losses of approximately \$4.7 million, which is available to offset future U.S. federal taxable income through 2012.

The realization of deferred tax assets is dependent on future taxable income and future reversals of existing taxable temporary differences. Based upon management’s assessment of historical data and future earnings, it is their belief that it is more likely than not that the \$5.3 million net deferred tax asset established for the U.K. NOL carryforwards will be realized in future periods by Quanta 4000. The Company will continue to periodically assess the realizability of its net deferred tax asset and adjust the valuation allowance accordingly.

In relation to the U.S. NOL and Irish NOL, due to prior and existing operating losses, the Company believes that it is more likely than not that the deferred tax asset will not be recognized. Accordingly, the Company has recorded a full valuation allowance against these net deferred tax assets as of December 31, 2007 and 2006.

The Company adopted the provisions of FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109” (“FIN 48”) on January 1, 2007. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

At the adoption date and as of December 31, 2007, the Company had no material unrecognized tax benefits and no adjustments to liabilities or operations were required.

At December 31, 2007, there are no income tax positions for which it is reasonably possible that the total amount of unrecognized tax benefits may significantly decrease or increase within the next twelve months.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. At December 31, 2007, the Company did not have interest and penalties related to uncertain tax positions.

Tax years 2003 through 2006 are subject to examination by the federal and state authorities.

15. Shareholders' equity

The authorized common share capital of the Company consists of 200,000,000 common shares of par value \$0.01 each. The following table is a summary of common shares issued and outstanding for

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the years ended December 31, 2007 and 2006:

2007	2006	Issued and outstanding common shares, beginning of period	70,008,185	69,946,861	Shares issued
125,314	61,324	Issued and outstanding common shares, end of period	70,133,499	70,008,185	

The common shares issued during the years ended December 31, 2007 and 2006 all related to director compensation in lieu of cash compensation.

On September 3, 2003, in connection with the closing of the sale of common shares, the Company granted certain founders of the Company's 2,542,813 warrants to purchase common shares. These warrants are exercisable at \$10.00 per share and have a ten year term.

16. Mandatorily redeemable preferred shares

The authorized preference share capital of the Company consists of 25,000,000 preferred shares of a par value of \$0.01 each.

On December 20, 2005 and January 11, 2006, the Company issued and sold 3,000,000 and 130,525 10.25% Series A Preferred Shares at \$25 per share, par value \$0.01 per share (the "Series A Preferred Shares") in an underwritten public offering. The Series A Preferred Shares had certain dividend, redemption, liquidation and voting rights. The Series A Preferred Shares had no stated maturity, were not be subject to any sinking fund and were not convertible into any of the Company's other securities or property.

During the third quarter of 2007 the Company repurchased all of its Series A Preferred Shares at a price of \$22.50 per share. The aggregate consideration paid for the preferred shares purchased amounted to \$70.4 million which resulted in a gain of \$2.4 million, net of repurchase costs of \$2.2 million and the write off of original deferred issuance costs of \$3.3 million.

There was no tax effect in relation to the repurchase of the Series A Preferred Shares of the Company for the year ended December 31, 2007.

17. Employee benefit plans

a) Pension plans

The Company provides pension benefits to eligible employees through various defined contribution plans, including 401(k) plans, sponsored by the Company. Under these plans, employee contributions may be supplemented by the Company matching contributions based on the level of employee contribution up to certain maximum amounts. Expenses incurred relating to these plans during the years ended December 31, 2007, 2006 and 2005, totaled \$0.1 million, \$0.5 million and \$1.3 million.

b) Options and stock based compensation

In July 2003, the shareholders of the Company approved the 2003 long-term incentive plan (the ‘‘Incentive Plan’’). The Incentive Plan provides for the grant to eligible employees, directors and consultants of stock options, stock appreciation rights, restricted shares, restricted share units, performance awards, dividend equivalents and other share-based awards. The Incentive Plan is administered by the Compensation Committee of the Board of Directors. The Compensation Committee determines the dates, amounts, exercise prices, vesting periods and other relevant terms of

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the awards. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the date of grant; those option awards generally vest based on four years of continuous service and have seven or ten-year contractual terms. Recipients of awards may exercise at any time after they vest and before they expire, except that no awards may be exercised after seven or ten years from the date of grant, as the case may be.

Performance share units were also awarded to various employees pursuant to the Incentive Plan. The number of shares of common stock to be received under these awards following December 31, 2007 (the end of the performance period) depended on whether the Company's GAAP average return on shareholders' equity over a three year period preceding December 31, 2007 was 12% or higher. If this performance target had been met, the grantees would have received shares of common stock in an amount ranging from zero to 300% percent of the share award (as such amount is defined in the grant).

Since unvested performance share units are contingent upon satisfying performance objectives, those unvested shares are considered to be contingently issuable shares and are not included in the computation of diluted earnings per share until all conditions for issuance are met. Performance share units are included in basic shares outstanding when issued.

As of December 31, 2007 and 2006, the maximum number of shares available for award and issuance under the Incentive Plan was 9,350,000 and 9,350,000.

The Company continually reviews and adjusts its provisions for the 2007 LTIP awards and other bonus awards by taking into account known information and updated assumptions related to unknown information. Award provisions are an estimate and amounts established in prior periods are adjusted in current operations as new information becomes available. Any adjustments to previously established provisions or the establishment of new provisions may significantly impact current period results and net income. The Company expenses the cost of the 2007 LTIP plan using the fair value recognition provisions of FASB Statement No. 123(R), "Share-Based Payment" ("SFAS 123(R)"). In order to do this the Company utilizes the Black-Scholes valuation model which uses various assumptions and then expenses the vested portion. The following assumptions were used in the Black-Scholes valuation model:

	Year ended			
December 31,				
2007 Expected volatility	32.2 %	Dividend yield	0.0 %	Risk-free interest rate
years) 2				3.1 %
				Expected term (in

For the year ended December 31, 2007, the amount expensed in relation to the 2007 LTIP was \$0.6 million.

i) Options and warrants

In accordance with SFAS 123 and SFAS 123(R), the fair value of each option award is estimated on the date of grant using a Black-Scholes option-pricing formula that uses the assumptions noted in the following table, which represent the weighted average assumptions used for grants in the periods presented. Expected volatilities are based on implied volatilities from traded options on the Company's stock, historical volatility of the Company's stock, and other factors.

The Company uses historical data to estimate future employee terminations. The expected term of options granted is calculated using the Staff Accounting Bulletin No. 107 simplified method. It is the mid-point between the vesting date and the expiration date and represents the period of time that options granted are

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expected to be outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The dividend yield is based on forward looking data.

	Year ended			
December 31, 2007	Year ended			
December 31, 2006	Expected volatility	46.1 %	48.9 %	Dividend yield
	4.5 %			0.0 %
	Expected term (in years)	4	4	0.0 %
				Risk-free interest rate
				4.87 %

The following is a summary of the Company's stock options and warrants and related activity during the year ended December 31, 2007 and 2006:

Year ended December 31, 2007	Year ended December 31, 2006	Number of options and warrants	Weighted Average exercise price	Number of options and warrants	Weighted Average exercise price	Granted	2.18
Outstanding – beginning of period	3,343,879	\$ 9.41	5,306,979	\$ 9.72	121,000	2.18	
220,000	2.87	Exercised	—	—	—	Forfeited (349,062)	(8.15)
						(2,183,100)	(9.50)
Outstanding – end of period	3,115,817	\$ 9.27	3,343,879	\$ 9.41			

The weighted-average grant date fair value of options granted during the years ended December 31, 2007 and 2006 was \$0.92 and \$1.23.

The compensation cost that was expensed in the Statement of Operations during the years ended December 31, 2007 and 2006 was \$0.3 million and \$0.4 million.

The Company did not incur any compensation expense under APB 25 relating to the grant of option awards during the year ended December 31, 2005 because all options granted had an exercise price that equaled the fair market value of the underlying common stock of the Company on the date of the grant.

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The following is a summary of the Company's outstanding options and warrants and exercisable options and warrants as of December 31, 2007.

Options and warrants outstanding				Options and warrants exercisable			
Range of exercise prices		Number of options and warrants		Range of exercise prices		Number of options and warrants	
Average exercise price		Average contractual life		Average exercise price		Average contractual life	
\$1.88	100,000	\$ 1.88	5.71 years	\$ 1.88	25,000	\$ 2.08-\$2.09	50,000
\$ —	75,000	\$ 2.26	7.14 years	\$ 2.30	6,250	\$ 4.59-\$4.69	66,666
\$ 4.67	20,833	\$ 7.85	5,901	\$ 7.85	2,951	\$ 8.92	143,437
\$ 8.92	71,719	\$ 10.00-\$10.20	2,639,813	\$ 10.00	2,638,563	\$ 11.60-\$12.50	35,000
\$ 11.99	26,250	\$ 11.99	6.20 years	\$ 11.99	26,250		

The intrinsic value of unvested stock options and warrants as of December 31, 2007 was \$0.1 million. As of December 31, 2006, the unvested stock options and warrants had no intrinsic value.

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As of December 31, 2007, there was \$0.5 million of total unrecognized compensation cost related to non vested share-based compensation arrangements with respect to stock options granted under the Incentive Plan. This cost is expected to be recognized over a weighted-average period of 1.8 years.

ii) Performance Share Units and Restricted Shares

The fair value of performance share units and restricted shares awarded under the Incentive Plan is determined based on the closing trading price of the Company's shares on the grant date. The following is a summary of the Company's non vested performance share units and restricted shares and related activity during the year ended December 31, 2007 and 2006:

Year ended December 31, 2007	Year ended December 31, 2006	Number	Weighted-average share price	Number	Weighted-average share price	Non vested – beginning of period	Granted	Non vested – end of period	Forfeited
143,990	148,335	2.57	3.79	(102,548)	7.39	184,938	68,085	109,882	(40,593)
(81,127)	(26,260)	(7.93)	(4.59)	(3.11)	(4.52)	\$ 3.79	\$ 7.39	\$ 3.17	\$ 3.79

Included in the December 31, 2007 and December 31, 2006 non-vested shares are 14,419 and 27,219 of performance share units.

The intrinsic value of unvested performance share units and restricted shares as of December 31, 2007 and December 31, 2006 was \$0.2 million and \$0.4 million.

18. Credit agreement

On October 27, 2006, the Company entered into a Credit Agreement with a syndicate of lenders and ING Bank N.V., London Branch, as the Mandated Lead Arranger, providing for a secured bank letter of credit facility (the "ING Credit Facility"). The ING Credit Facility provided for an aggregate commitment of up to \$240 million for a period of three years terminating on October 27, 2009, pursuant to which the lenders will issue from time to time, for the account of the designated subsidiary borrowers, one or more back-to-back letters of credit naming JPMorgan Chase Bank, N.A. as beneficiary in the face amount equal to the face amount of the outstanding letters of credit under the JPM Credit Agreement, and other letters of credit in an aggregate face amount up to the aggregate commitment. The JPM Credit agreement was terminated prior to December 31, 2007. The total amount of letters of credit issued under the JPM Credit Agreement at December 31, 2006 was \$110.0 million. Since January 1, 2007, the Company has reduced the aggregate commitment under the ING Credit Facility from \$240 million to \$110 million at December 31, 2007. Effective February 11, 2008, the ING Credit Facility commitment was reduced by a further \$15 million to \$95 million. The facility is secured by specified investments of the borrowers. Availability for issuances of letters of credit on account of any borrower is based on the amount of eligible investments pledged by the applicable

borrower(s) and no material adverse change provisions. Regulatory restrictions will also limit the amount of investments that may be pledged by certain U.S. insurance borrowers and, consequently, the amount available for letters of credit under the facility on account of those borrowers. The Company unconditionally and irrevocably guaranteed all of the obligations of its subsidiaries to the lenders under the ING Credit Facility.

The ING Credit Facility includes customary representations and warranties, affirmative and negative covenants, and events of default. Upon the occurrence, and during the continuance, of an

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event of default, including but not limited to nonpayment of principal when due, failure to perform or observe certain terms, covenants or agreements under the ING Credit Facility, and certain defaults of other indebtedness, the Administrative Agent may terminate the obligation of the lenders to make advances and issue letters of credit and declare any outstanding obligations immediately due and payable.

The ING Credit Facility has a financial covenant requiring the Company to maintain a minimum consolidated tangible net worth, as well as covenants restricting the activities of the Company and its subsidiaries, such as the incurrence of additional indebtedness and liens, the sale of assets, and the payment of dividends and other restricted payments. At December 31, 2007 and 2006 the amount of letters of credit issued under the facility was \$91.6 million and \$235.4 million. At December 31, 2007 the Company believes it was in compliance with the covenants under the ING Credit Facility.

19. Related party transactions

In the normal course of business, the Company enters into cost sharing and service level agreement transactions with certain other subsidiaries, which management believes to be conducted consistent with arms-length rates. Such transactions, individually and in the aggregate, are not material to the Company's financial condition, results of operations and cash flows.

a) Friedman Billings Ramsey, Inc. ("FBR")

Until December 11, 2006, W. Russell Ramsey was one of the Company's directors and he also served on the Board of Directors of FBR. Following Mr. Ramsey's resignation as a member of the Board of FBR on June 7, 2007 FBR is no longer a related party to the Company. The Company entered into an advisory agreement with FBR in December 2005. Under the advisory agreement, FBR from time to time provided financial advisory advice and assistance to the Company in connection with certain mergers and acquisitions. The agreement terminated during 2006. Under the terms of the agreement, FBR's compensation for services provided was agreed between the Company and FBR on an arms-length basis.

In connection with the Company's issuance of 13,136,841 common shares and 3,000,000 preferred shares during the year ended December 31, 2005, FBR received \$3.4 million and \$2.4 million for underwriting fees.

In connection with the issuance by Quanta Trust and Quanta Trust II of the Trust Preferred Securities, FBR indirectly received a portion of the \$1.2 million and \$0.4 million of issuance costs from the placement agents for providing financial advisory services.

In connection with the sale of ESC during 2006, FBR received advisory fees of \$0.6 million directly associated with the sale.

As at December 31, 2006 there were no amounts due between the Company and FBR.

20. Statutory financial information and dividend restrictions

The Company is subject to a 30% withholding tax on certain dividends and interest received from its U.S. subsidiaries.

The Company's insurance and reinsurance subsidiaries are subject to insurance laws and regulations in the jurisdictions in which they operate, which are Bermuda, the United States and Ireland. The regulations in Bermuda, the United States and Ireland include restrictions that limit the amount of dividends or other distributions available to shareholders without prior approval of the insurance regulatory authorities. Typically, these restrictions relate to minimum levels of solvency, capital and liquidity as defined by the relevant insurance laws and regulations.

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Estimated unaudited statutory capital and surplus for the principal operating subsidiaries of the Company in these jurisdictions as of December 31, 2007 and 2006 was:

	Bermuda	United States	Ireland	2007	2006	2007	2006	2007	2006	Required minimum
statutory capital and surplus		\$ 102,262	\$ 103,306	\$ 16,160	\$ 32,179	\$ 4,669	\$ 3,960	Actual		
statutory capital and surplus (unaudited)		375,339	463,769	84,493	88,472	7,361	19,394			

The differences between statutory financial statements and statements prepared in accordance with U.S. GAAP vary by jurisdiction. However, in general the primary differences are that statutory financial statements do not reflect certain non-admitted assets, which may include deferred acquisition costs, intangible assets, and the unrealized appreciation on investments.

The Company's U.S. operations required statutory capital and surplus is determined using various criteria, including risk based capital tests. If a company falls below certain levels of risk based capital, and dependent upon the degree to which the company falls below, the commissioner of insurance with jurisdiction of the Company is authorized to take certain regulatory actions to protect policyholders and creditors.

As at December 31, 2007, there are statutory restrictions on the payment of dividends from retained earnings or the return of capital from the Company's subsidiaries. Following the A.M. Best rating action and the Company's decision to run-off a substantial portion of its business, and effective on June 1, 2006, the Bermuda Monetary Authority (the "BMA") amended the license of Quanta Reinsurance Ltd. to require the approval of the BMA prior to making dividend payments and entering into certain large transactions. In the U.S. and Ireland, certain dividend payments from retained earnings or the return of capital require prior approval from the insurance regulatory authorities. The Company believes that its U.S. subsidiaries may not pay dividends as these companies currently have accumulated losses and that approval for the return of capital requires compliance with a number of requirements. Further, because Quanta Re U.S., a Bermuda company, is a subsidiary of Quanta Indemnity Co., any dividends it pays or any return of capital it makes to Quanta Indemnity Co. would also be subject to the above restrictions relating to U.S. subsidiaries. At December 31, 2007, the Company believes that the minimum levels of solvency and liquidity were met in all jurisdictions in which the Company operates.

21.

Subsequent Events

On February 13, 2008, the Company sold Quanta 4000 and its interest in Pembroke JV to Chaucer for an amount of approximately £1 each and received the return of \$117.2 million which had previously been pledged to Lloyd's as security for the business being written by Syndicate 4000.

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At December 31, 2007, the unaudited balance sheet of Quanta 4000 was as follows:

December 31,
2007 Assets Investments at fair value 18,590 Cash and cash equivalents 107,268 Premiums receivable 45,417 Losses and loss adjustment expenses recoverable 25,793 Deferred acquisition costs, net 902 Deferred reinsurance premiums 12,135 Net deferred tax asset 5,277 Other assets 3,236 Total assets \$ 218,618

Liabilities Reserve for losses and loss expenses \$ 160,302 Unearned premiums 58,524 Reinsurance balances payable and other liabilities 14,858 Income taxes payable 5,277 Total liabilities 238,961 Shareholders' equity Common shares — Additional paid-in capital 77 Accumulated deficit (18,944) Accumulated other comprehensive income (1,476) Total shareholders' equity (20,343) Total liabilities and shareholders' equity \$ 218,618

At December 31, 2007, the investment in Pembroke JV was carried at cost of approximately \$0.1 million.

The Company expects that, in the first quarter of 2008, it will recognize a gain on the sale of its interest in Quanta 4000. The amount of such gain will be determined based on recorded balances as of the date of sale. If the sale had occurred on December 31, 2007, based on balances recorded at that date, the pro forma amount of the gain would have been approximately \$17.9 million. This gain is net of transaction costs, the payment of bonuses to the management and employees of Pembroke and writing off of the cost of its investment in Pembroke JV. There can be no assurances that the gain the Company will record in the first quarter of 2008 will be substantially similar to the amount stated above or that there will be any gain at all. If the Company records a loss it could have a material adverse impact on its financial results and statement of operations.

On March 13, 2008, the Company announced that it declared a special dividend of \$1.75 per common share resulting in an aggregate dividend payment of approximately \$122.7 million. The dividend will be payable in cash on March 28, 2008 to shareholders of record as of the close of business on March 25, 2008.

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22. Unaudited quarterly financial information

The following is a summary of quarterly financial data for the years ended December 31, 2007 and 2006.

Quarter ended December 31, 2007	Quarter ended September 30, 2007	Quarter ended June 30, 2007	Quarter ended March 31, 2007	2006	2005	2004	2003	2002	2001	2000
Net premium earned	\$ 19,370	\$ 22,376	\$ 19,864	\$ 25,637	Technical service revenues	1	713			
501	492	Net investment income	8,065	11,306	10,724	11,805	Net gains (losses) on investments			
6,205	3,379	(5,652)	1,886	Net foreign exchange gains (losses)	47	(184)	723	264	Gain on	
repurchase of junior subordinated debentures	—	4,421	—	—	Other income	(3,693)	375	2,714		
1,051	Total revenues	29,995	42,386	28,874	41,135	Net loss and loss expenses incurred	465			
3,156	13,161	14,295	Acquisition costs	10,748	5,517	5,264	5,199	General and administrative		
expenses	13,171	14,772	16,955	14,968	Interest expense	—	797	1,442	1,393	Depreciation of
fixed assets and amortization and impairment of intangible assets	154	115	78	677	Total expenses					
24,539	24,357	36,900	36,532	Income (Loss) from continuing business before income taxes	5,456					
18,029	(8,026)	4,603	Income tax expense (benefit)	26	2	9	(25)	Net income (loss) from		
continuing operations	5,431	18,027	(8,035)	4,628	Gain on repurchase on Series A preferred shares	—				
2,364	—	—	Net income (loss) to common shareholders	\$ 5,431	\$ 20,391	\$ (8,035)	\$ 4,628			
Weighted average common share and common share equivalents					Basic	70,126,934				
70,106,237	70,059,993	70,008,185	Diluted	70,190,803	70,224,287	70,059,993	70,008,185			
Basic income (loss) from continuing operations per common share	\$ 0.08	\$ 0.26	\$ (0.11)	\$ 0.06	Basic					
gain on repurchase on Series A preferred shares per share	\$ —	\$ 0.03	\$ —	\$ —	Basic income (loss) per common					
share	\$ 0.08	\$ 0.29	\$ (0.11)	\$ 0.06	Diluted income (loss) from continuing operations per common share					
\$ 0.08	\$ 0.26	\$ (0.11)	\$ 0.06	Diluted gain on repurchase on Series A preferred shares per share	\$ —	\$				
0.03	\$ —	\$ —	Diluted income (loss) per common share	\$ 0.08	\$ 0.29	\$ (0.11)	\$ 0.06			

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Quarter ended	December 31, 2006	Quarter ended September 30, 2006	Quarter ended June 30, 2006	Quarter ended March 31, 2006	Net premium earned	\$ 36,124	\$ 49,202	\$ 60,405	\$ 79,568	Technical service revenues	384																															
	752	496	1,699	Net investment income	10,584	12,821	11,753	10,776	Net (losses) gains on investments	(1,803)	906	(6,728)	(8,320)	Net foreign exchange losses	(1,839)	(257)	(1,375)																									
	(319)	Other income	962	1,174	486	1,032	Total revenues	44,412	64,598	65,037	84,436	Net loss and loss expenses incurred	21,943	30,153	49,533	54,492	Acquisition costs	9,932																								
	8,415	10,260	13,933	General and administrative expenses	15,958	20,578	34,018	29,452	Interest expense	1,422	1,430	1,344	1,262	Depreciation of fixed assets and amortization and impairment of intangible assets	3,016	715	435	833	Total expenses	52,271	61,291	95,590	99,972																			
	(30,575)	(15,561)	Discontinued operations:	(Loss) income from operations of discontinued operations	—	(936)	(12,359)	342	Income on disposal of discontinued operations	—	704	—	—	Net (loss) income from discontinued operations	—	(232)	(12,359)	342	Net (loss) income	(7,826)	3,307	(30,553)	(15,536)	Income tax (benefit) expense	(33)	—	22	25	Net (loss) income from continuing operations	(7,826)	3,307	(30,553)	(15,536)									
	3,075	(42,934)	(15,219)	Dividends on preferred shares	—	—	—	(1,916)	Net (loss) income to common shareholders	\$ (7,826)	\$ 3,075	\$ (42,934)	\$ (17,135)	Weighted average common share and common share equivalents	Basic	69,971,646	69,981,925	69,956,211	69,946,861	Diluted	69,971,646	69,984,614	69,956,211	69,946,861	Basic (loss) income from continuing operations per share	\$ (0.11)	\$ 0.04	\$ (0.43)	\$ (0.24)	Basic (loss) income from discontinued operations per share	\$ —	\$ (0.01)	\$ (0.18)	\$ (0.00)	Basic income from disposal of discontinued operations per share	\$ —	\$ —	Basic (loss) income per share	\$ (0.11)	\$ 0.04	\$ (0.61)	\$ (0.24)
	0.01	\$ —	\$ —	Basic (loss) income per share	\$ (0.11)	\$ 0.04	\$ (0.43)	\$ (0.24)	Diluted (loss) income from continuing operations per share	\$ (0.11)	\$ 0.04	\$ (0.43)	\$ (0.24)	Diluted (loss) income from discontinued operations per share	\$ —	\$ (0.01)	\$ (0.18)	\$ (0.00)	Diluted income from disposal of discontinued operations per share	\$ —	\$ 0.01	\$ —	\$ —	Diluted loss per share	\$ (0.11)	\$ (0.04)	\$ (0.61)	\$ (0.24)														

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QUANTA CAPITAL HOLDINGS LTD.
Financial Statement Schedules
As of December 31, 2007

	I
Summary of Investments Other Than Investments in Related Parties II	Condensed Financial Information of Registrant III
Supplementary Insurance Information IV	Reinsurance V
Valuation and Qualifying Accounts VI	Supplementary Information Concerning Property/Casualty Insurance Operations
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QUANTA CAPITAL HOLDINGS LTD.

Schedule I

Summary of Investments Other Than Investments in Related Parties

As of December 31, 2007

(Expressed in thousands of U.S. dollars)

Amortized

Cost or Cost Fair

Value Amount

at which

shown in

Balance

Sheet Trading:	Fixed maturities:				U.S. government and government sponsored agencies	\$ 263,320	
\$ 267,488	\$ 267,488	Foreign governments	11,486	11,496	11,496	Tax-exempt municipal	1,036
1,038	1,038	Corporate	62,827	63,312	63,312	Asset-backed securities	51,724
							51,403
		Mortgage-backed securities	165,932	164,767	164,767	Total fixed maturities	\$ 556,325
							\$ 559,504
\$ 559,504		Short-term investments	\$ 88,880	\$ 88,880	\$ 88,880	Total trading investments	\$ 645,205
\$ 648,384	\$ 648,384	Total investments	\$ 645,205	\$ 648,384	\$ 648,384		\$

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QUANTA CAPITAL HOLDINGS LTD.
 Schedule II
 CONDENSED FINANCIAL INFORMATION OF REGISTRANT
 BALANCE SHEETS
 PARENT COMPANY ONLY

(Expressed in thousands of U.S. dollars except for share amounts)

December 31,		2007		December 31,		2006	
Assets	Investments in subsidiaries on equity basis	\$ 382,097	\$ 489,583	Investments at fair value			
(amortized cost: December 31, 2007: \$2,622; December 31, 2006: \$0)		2,622	—	Cash and cash equivalents			
4,070	10,108	Other accounts receivable	16	—	Property and equipment, net of accumulated depreciation of		
\$334 (December 31, 2006: \$261)	485	200	Due from subsidiaries	5,373	73,189	Other assets	3,052
5,895	Total assets	\$ 397,715	\$ 578,975	Liabilities	Accounts payable and accrued expenses	3,752	
5,756	Due to subsidiaries	43,301	108,028	Junior subordinated debentures	—	61,857	Total liabilities
47,053	\$ 175,641	Mandatorily redeemable preferred shares		(\$0.01 par value; 25,000,000 shares			\$
	authorized; 0 issued and			outstanding at December 31, 2007 and 3,130,525 issued and outstanding at December 31, 2006)	\$ —	\$ 74,998	
	Shareholders' equity	Common shares		(\$0.01 par value; 200,000,000 shares authorized; 70,133,499			
	issued and outstanding at December 31, 2007 and 70,008,185 issued and outstanding at December 31, 2006)			\$ 701			
	\$ 700	Additional paid-in capital	582,889	582,578	Accumulated deficit	(231,399)	(263,830)
	Accumulated other comprehensive (loss) income	(1,529)	8,888	Total shareholders' equity	\$ 350,662	\$	
	328,336	Total liabilities and shareholders' equity	\$ 397,715	\$ 578,975			

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QUANTA CAPITAL HOLDINGS LTD.
 Schedule II
 CONDENSED FINANCIAL INFORMATION OF REGISTRANT
 STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
 PARENT COMPANY ONLY

(Expressed in thousands of U.S. dollars)

For the year
 ended
 December 31,
 2007 For the year
 ended
 December 31,
 2006 For the year
 ended
 December 31,
 2005

Revenues				Net investment income	\$ 1,599	\$ 678	\$ 139	Net losses on investments	(169
)	—	—	Net foreign exchange gains (losses)	350	—	(8)	Equity in net income of subsidiaries	25,333	—
—	Gain on repurchase of junior subordinated debentures	4,421	—	—	Total revenues	31,534	678	131	
Expenses				Equity in net loss of subsidiaries	—	53,314	83,392	General and administrative	
expenses	11,407	10,102	22,471	Other expenses	(6)	41	22	Depreciation of fixed assets	82
125	198	Total expenses	11,483	63,582	106,083	Income (loss) before income taxes	20,051		
(62,904)	(105,952)	Income tax expense	—	—	—	Net income (loss)	20,051	(62,904)	(105,952)
Gain on repurchase of Series A preferred shares	2,364	—	—	Dividends on preferred shares	—	(1,916)	—		
Net income (loss) to common shareholders	22,415	(64,820)	(105,952)	Other comprehensive income (loss):					
	Net income (loss)	\$ 20,051	\$ (62,904)	\$ (105,952)	Other comprehensive income (loss)				
	Net unrealized investment losses arising during the period, net of income taxes	—	(6,222)						
(12,429)	Foreign currency translation adjustments	(401)	(1,381)	327	Reclassification of net realized				
losses (gains) on available for sale investments included in net loss, net of income taxes	—	15,945	13,020						
Other comprehensive (loss) income	(401)	8,342	918	Comprehensive income (loss)	\$ 19,650	\$			
(54,562)	\$ (105,034)								

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QUANTA CAPITAL HOLDINGS LTD.
 Schedule II
 CONDENSED FINANCIAL INFORMATION OF REGISTRANT
 STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
 PARENT COMPANY ONLY

(Expressed in thousands of U.S. dollars except for share and per share amounts)

For the year
 ended
 December 31,
 2007 For the year
 ended
 December 31,
 2006 For the year
 ended
 December 31,

2005 Share capital – common shares of par value \$0.01 each					Balance at beginning of period	\$ 700
\$ 699 \$ 568 Issued during period	1	1	131	Balance at end of period	701	700
699				Additional paid-in capital		
				Balance at beginning of period	582,578	581,929
				523,771		
issued during period	—	—	62,269	Net offering costs	—	—
				(4,183)		
311 649 72	Balance at end of period	582,889	582,578	581,929		
	Balance at beginning of period	(263,830)	(199,010)	(93,058)		
	from the adoption of SFAS 159	10,016	—	—		
	Net income (loss)	20,051	(62,904)	(105,952)		
	Gain on repurchase of Series A preferred shares	2,364	—	—		
	Dividends on preferred shares	—	(1,916)	—		
	Balance at end of period	(231,399)	(263,830)	(199,010)		
	Accumulated other comprehensive income (loss)					
	Balance at beginning of period	8,888	546	(372)		
	from the adoption of SFAS 159	(10,016)	—	—		
	Net change in unrealized losses on investments, net of income taxes	—	—	—		
	9,723 591	Foreign currency translation adjustments	(401)	(1,381)	327	
	Balance at end of period	(1,529)	8,888	546		
	Total shareholders' equity	\$ 350,662	\$ 328,336	\$ 384,164		

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QUANTA CAPITAL HOLDINGS LTD.
 Schedule II (continued)
 CONDENSED FINANCIAL INFORMATION OF REGISTRANT
 STATEMENTS OF CASH FLOWS
 PARENT COMPANY ONLY

(Expressed in thousands of U.S. dollars)

For the year ended December 31, 2007	For the year ended December 31, 2006						
2005							
Cash flows from operating activities		Net income (loss)	\$ 20,051	\$ (62,904)	\$ (105,952)		
Adjustments to reconcile net loss to net cash (used in) provided by operating activities						Depreciation of property and equipment	82 125 198
83,392		Equity in net (gain) loss of subsidiaries	(25,333)	52,761			
		Gain on foreign exchange translation	(401)	—	—	Non-cash stock compensation expense	312 649
		Gain on repurchases of junior subordinated debentures	(4,421)	—	—	Changes in assets and liabilities:	
		Other accounts receivable	(16)	—	2	Due from subsidiaries	67,816 (46,636) (20,741)
		Other assets	(653)	506	(627)	Accounts payable and accrued expenses	(1,443) (1,020) 4,999
		Due to subsidiaries	(64,727)	53,266	40,326	Net cash (used in) provided by operating activities	(8,733)
		(3,253)	1,669			Cash flows provided by (used in) investing activities	
		(investment in) subsidiaries	132,819	(2,500)	(136,658)	Return of capital from	
		investments	(85,202)	—	—	Purchases of fixed maturities and short-term	
		—				investments	82,580
		—				Proceeds from sale of fixed maturities and short-term investments	—
		—				Net (purchases) proceeds from sale of property and equipment	(367) 193 (262)
		(used in) investing activities	129,830	(2,307)	(136,920)	Net cash provided by	
		activities				(used in) investing activities	129,830 (2,307) (136,920)
						Cash flows (used in) provided by financing	
						activities	
						Proceeds from issuance of common shares, net of offering costs	— — 58,217
						Proceeds from issuance of preferred shares, net of offering costs	— 3,160 71,838
						Dividend on preferred shares	—
						(1,916) —	
						Repurchase of preferred shares	(72,634) — —
						Proceeds from junior subordinated debentures, net	
						of issuance costs	— — 19,591
						Repurchase of junior subordinated debentures	(54,501) — —
						Net cash	
						(used in) provided by financing activities	(127,135) 1,244 149,646
						(Decrease) Increase in cash and cash	
						equivalents	(6,038) (4,316) 14,395
						Cash and cash equivalents at beginning of period	10,108 14,424
						29	
						Cash and cash equivalents at end of period	\$ 4,070 \$ 10,108 \$ 14,424

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QUANTA CAPITAL HOLDINGS LTD.
Schedule III
Supplementary Insurance Information

(Expressed in thousands of U.S. dollars)

December 31, 2007

	Reporting segment (2) Net												
Deferred													
Acquisition													
Costs Reserve for													
Losses and													
Loss													
Expenses Unearned													
Premiums Net													
Premiums													
Earned Net													
Investment													
Income													
(1) Net Losses													
and Loss													
Expenses Amortization													
of Deferred													
Acquisition													
Costs Other													
Operating													
Expenses													
(3) Net													
Premiums													
Written Specialty Insurance run-off	\$ 4,087	\$ 262,128	\$ 37,067	\$ 6,127	\$ —	\$ (16,621)	\$ 441	\$					
7,369	\$ (17,417)	Specialty Reinsurance run-off	(1)	102,658	(5)	336	—	(6,147)	(1,100)				
1,357	(1,036)	Lloyds	902	160,302	58,524	80,784	—	53,845	27,387	13,784	96,395		
Technical Services (4)	—	—	—	—	—	2,317	—	Not allocated to individual segments			—	—	—
—	41,900	—	—	35,039	—	Total	\$ 4,988	\$ 525,088	\$ 95,586	\$ 87,247	\$ 41,900	\$ 31,077	
	\$ 26,728	\$ 59,866	\$ 77,942										

	Reporting segment (2) Net									
Deferred										
Acquisition										

Costs Reserve for Losses and Loss Expenses Unearned Premiums Net Premiums Earned Net Investment Income (1) Net Losses and Loss Expenses Amortization of Deferred Acquisition Costs Other Operating Expenses (3) Net Premiums	Written Specialty Insurance run-off	\$ 7,185	\$ 319,355	\$ 75,510	\$ 113,289	\$ —	\$ 65,706	\$ 18,029											
	\$ 18,440	\$ 25,981	Specialty Reinsurance run-off	160	204,624	1,985	46,487	—	40,033										
	12,468	6,420	(7,171)	Lloyds	4,779	99,639	41,702	65,523	—	50,382	12,043	12,886							
	61,744	Technical Services (4)	—	—	—	—	—	4,283	—	Not allocated to individual segments									—
	—	—	—	45,934	—	—	57,977	—	Total	\$ 12,124	\$ 623,618	\$ 119,197	\$ 225,299	\$					
	45,934	\$ 156,121	\$ 42,540	\$ 100,006	\$ 80,554														
	December 31, 2005																		

Reporting segment (2) Net

Deferred
Acquisition
Costs Reserve for
Losses and
Loss
Expenses Unearned
Premiums Net
Premiums
Earned Net
Investment
Income
(1) Net Losses
and Loss
Expenses Amortization
of Deferred
Acquisition
Costs Other
Operating
Expenses
(3) Net

Premiums

Written Specialty Insurance run-off	\$ 13,658	\$ 257,255	\$ 209,324	\$ 160,620	\$ —	\$ 120,710	\$	
21,836	\$ 21,750	\$ 194,917	Specialty Reinsurance run-off	15,572	244,404	90,615	166,944	—
178,887	42,714	9,847	133,478	Lloyds	3,887	32,324	36,611	36,511
8,716	61,646	Technical Services (4)	—	—	—	—	18,545	—
segments	—	—	—	27,181	—	—	50,749	—
364,075	\$ 27,181	\$ 324,249	\$ 69,624	\$ 109,607	\$ 390,041	Total	\$ 33,117	\$ 533,983
							\$ 336,550	\$

(1) Because the Company does not manage its assets by segment, net investment income is not allocated to the individual segments. (2) During the year ended December 31, 2006, following the decision of the Company's Board of Directors in May 2006 to place most of its business in run-off, the Company changed the composition of its reportable segments such that the Lloyd's operating segment, which was aggregated with the Company's specialty insurance reportable segment for the year ended December 31, 2005 has now become a reportable segment and the Company renamed its specialty insurance segment and specialty reinsurance segment to specialty insurance run-off segment and specialty reinsurance run-off segment. The December 31, 2005 balances have been restated and renamed to conform with the presentation for the year ended December 31, 2006 and December 31, 2007.

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Table of Contents (3) During the year ended December 31, 2006, the Company revised its accounting methodology for the allocation of corporate general and administrative expenses. Following its decision to place most of its business into run-off, the Company no longer allocates capital to its reportable segments and, accordingly, corporate general and administrative expenses are no longer allocated to each segment in proportion to each segment's amount of allocated capital. The December 31, 2005 balances have been restated to conform with the presentation for the year ended December 31, 2006 and December 31, 2007. (4) As a result of the disposal of ESC, the technical services segment now consists only of the two environmental liability assumption programs, but without the results of ESC. The results of the technical services segment for the year ended December 31, 2005 have been reclassified to conform with the presentation of ESC in discontinued operations for the year ended December 31, 2006 resulting in the results of ESC for the years ending December 31, 2006 and 2005 no longer forming part of the Technical Services reportable segments.

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QUANTA CAPITAL HOLDINGS LTD.
Schedule IV
Reinsurance

(Expressed in thousands of U.S. dollars)

December 31, 2007

Premiums Other Companies from Other Companies Amount of Amount Assumed	Gross Assumed Net Percentage	Ceded to Other Companies Net Percentage			
to Net Property and liability insurance December 31, 2006	\$ 103,076	\$ 28,645	\$ 3,511	\$ 77,942	5 %

Premiums Other Companies from Other Companies Amount of Amount Assumed	Gross Assumed Net Percentage	Ceded to Other Companies Net Percentage			
to Net Property and liability insurance December 31, 2005	\$ 139,671	\$ 78,175	\$ 19,058	\$ 80,554	24 %

Premiums Other Companies from Other Companies Amount of Amount Assumed	Gross Assumed Net Percentage	Ceded to Other Companies Net Percentage			

to Net Property and liability insurance \$ 367,890 \$ 218,894 \$ 241,045 \$ 390,041 62 %
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QUANTA CAPITAL HOLDINGS LTD.
 Schedule V
 Valuation and Qualifying Accounts
 (Expressed in thousands of U.S. dollars)

Balance at									
Beginning of									
Period	Additions								
Charged									
to Costs									
and									
Expenses	Deductions	Balance at							
End of									
Period	Deferred tax valuation allowance:			December 31, 2007	\$ 49,141	\$ 7,078	\$ (5,277)		
\$ 50,942	December 31, 2006	\$ 24,795	\$ 24,346	\$ —	\$ 49,141	December 31, 2005	\$ 13,348	\$	
11,447	\$ —	\$ 24,795	Allowance for doubtful accounts:			Year Ended December 31, 2007	\$		
870	\$ —	\$ (476)	\$ 394	Year Ended December 31, 2006	\$ —	\$ 870	\$ —	\$ 870	Year Ended
December 31, 2005	\$ —	\$ —	\$ —	\$ —	Allowance for losses and loss adjustment expenses recoverable:				
	Year Ended December 31, 2007	\$ 2,000	\$ —	\$ (747)	\$ 1,253	Year Ended December 31, 2006	\$		
639	\$ 1,361	\$ —	\$ 2,000	Year Ended December 31, 2005	\$ —	\$ 639	\$ —	\$ 639	
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QUANTA CAPITAL HOLDINGS LTD.

Schedule VI

Supplementary Information Concerning Property/Casualty Insurance Operations

(Expressed in thousands of U.S. dollars)

Deferred

Policy
Acquisition
Expenses
(net) Reserves
for Unpaid
Loss and
Loss
Adjustment
Expenses
(gross) Discount
deducted
from
Reserves
for Unpaid
Loss and
Loss
Adjustment
Expenses Unearned
Premiums
(gross) Earned
Premiums
(net) Net
Investment
Income

Net Loss and Loss
Adjustment Expenses
Incurred related to: Amortization
of Deferred
Policy
Acquisition
Costs
(net) Paid
Losses and
Loss
Adjustment
Expenses

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(net) (U.S. dollars in thousands) Current

Year Prior

Years	Consolidated entities	\$ 4,988	\$ 525,088	—	\$ 95,586	\$ 87,247	\$ 41,900	\$ 75,317	\$
(44,240)	\$ 26,728	\$ 89,343	Unconsolidated subsidiaries	—	—	—	—	—	—
Proportionate share of equity investees	—	—	—	—	—	—	—	—	—

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Exhibit Index

Number	Exhibit
Description 3 .1 Memorandum of Association of the Company (incorporated by reference from Exhibit 3.1 to the Company's Registration Statement on Form S-1 (No. 333-111535) filed on December 24, 2003)	3 .2
Amended and Restated Bye-Laws of the Company (incorporated by reference from Exhibit 4.2 to the Company's Quarterly Report on Form 10-Q filed on August 9, 2007)	4 .1
Memorandum of Association of the Company (included as Exhibit 3.1)	4 .2
Amended and Restated Bye-Laws of the Company (included as Exhibit 3.2)	4 .3
Form of Common Share Certificate (incorporated by reference from Exhibit 4.1 to the Company's Amendment No. 1 to Registration Statement on Form S-1/A (No. 333-111535) filed on February 13, 2004)	10 .1
† Quanta Capital Holdings Ltd. 2003 Long Term Incentive Plan, as amended on June 2, 2005 (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated June 8, 2005)	10 .2
† Form of Non-Qualified Stock Option Agreement for recipients of options under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10 .3
† Form of Performance-Based Share Unit Agreement for recipients of performance-based share units under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10 .4
† Employment Agreement of Jonathan J.R. Dodd dated December 22, 2004 (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated July 26, 2005)	10 .5
Technical Property Binder of Reinsurance dated November 18, 2005, between Quanta Indemnity Company, Quanta Specialty Lines Insurance Company and Quanta Reinsurance US Ltd. and Arch Reinsurance Ltd. (incorporated by reference from Exhibit 10.30 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10 .6
Treaty Property Reinsurance Binder dated November 18, 2005, between Quanta Reinsurance Ltd., Quanta Indemnity Company, Quanta Reinsurance US Ltd., and Quanta Specialty Lines Insurance Company and Arch Reinsurance Ltd. (incorporated by reference from Exhibit 10.31 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10 .7
Commutation and Mutual Release Agreement dated November 21, 2005, between Quanta Reinsurance Limited and Houston Casualty Company and certain of its subsidiaries (incorporated by reference from Exhibit 10.32 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	10 .8
† Separation Agreement and General Release, effective January 3, 2006, between Quanta Capital Holdings Ltd. and Tobey J. Russ (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated January 9, 2006)	

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Number	Exhibit
Description 10 .9 † Retention Agreement between Quanta Capital Holdings Ltd. and Jonathan J.R. Dodd, dated March 30, 2006 (incorporated by reference from Exhibit 10.35 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed on March 31, 2006)	
10 .10 † Form of Restricted Share Agreement for recipients of restricted shares under 2003 Long Term Incentive Plan (incorporated by reference from Exhibit 10.1 to the Company's Amendment No. 1 on Form 10-K/A for the year ended December 31, 2005 filed on March 31, 2006)	
10 .11 † Separation Agreement and General Release dated July 25, 2006 between the Company and Michael J. Murphy (incorporated by reference from Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 filed on August 9, 2006)	
10 .12 † Separation Agreement and General Release dated August 7, 2006 between the Company and Gary G. Wang (incorporated by reference from Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 filed on August 9, 2006)	
10 .13 † Letter Agreement dated September 14, 2006 between the Company and Peter Johnson (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated September 15, 2006)	
10 .14 † Employment Agreement dated September 14, 2006 between the Company and James J. Ritchie (incorporated by reference from Exhibit 10.2 to the Company's Current Report on Form 8-K dated September 15, 2006)	
10 .15 † Amendment to Employment Agreement dated March 1, 2007 between the Company and James J. Ritchie (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated March 5, 2007)	
10 .16 Credit Agreement dated as of July 13, 2004 and Amended and Restated as of July 11, 2005, between Quanta Capital Holdings Ltd., various designated subsidiary borrowers, the lenders party thereto, BNP Paribas, Calyon, New York Branch, Comerica Bank, and Deutsche Bank AG New York Branch, as Co-Documentation Agents, and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated July 15, 2005)	
10 .17 Fourth Consent and Amendment to Credit Agreement dated October 25, 2006, between Quanta Capital Holdings Ltd., various designated subsidiary borrowers, the lenders party thereto, BNP Paribas, Calyon, New York Branch, Comerica Bank, and Deutsche Bank AG New York Branch, as Co-Documentation Agents, and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference from Exhibit 10.2 to the Company's Current Report on Form 8-K dated October 27, 2006)	
10 .18 Credit Agreement dated October 27, 2006 among the Company, ING Bank N.V., London Branch, Barclays Private Clients International Limited, Comerica Bank, HSH Nordbank AG, London Branch, designated subsidiary borrowers, and other lenders party thereto (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated October 30, 2006)	
10 .19 Amended and Restated Retention Agreement dated December 13, 2007 between the Company and Jonathan J.R. Dodd (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated December 13, 2007)	

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Number	Exhibit
Description	
10 .20	Stock Purchase Agreement, dated as of February 7, 2008, among Quanta Capital Holdings Ltd., Chaucer Holdings Plc and Quanta 4000 Holding Company Ltd. (incorporated by reference from Exhibit 10.1 to the Company's Current Report on Form 8-K dated February 7, 2008)
10 .21	Letter Agreement dated March 11, 2008 between the Company and Peter Johnson.
12 *	Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Dividends
16	Letter from PricewaterhouseCoopers LLP dated August 15, 2006 (incorporated by reference from Exhibit 16.1 to the Company's Current Report on Form 8-K dated August 17, 2006)
21 *	List of subsidiaries of the Company
23 *	Consent of Johnson Lambert & Co. LLP
31 .1 *	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31 .2 *	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32 .1 *	Certification of Principal Executive Officer of Quanta Capital Holdings Ltd. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32 .2 *	Certification of Principal Financial Officer of Quanta Capital Holdings Ltd. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
* Filed herewith † Represents a management contract or compensatory plan arrangement	
