
SCOTTISH RE GROUP LIMITED

FINANCIAL STATEMENTS

AS AT MARCH 31, 2010

(Issued on June 7, 2010)

(These financial statements are unaudited.)

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Summary of Results

Scottish Re Group Limited (“SRGL”, the “Company”, “we”, “our” and “us”) is a holding company incorporated under the laws of the Cayman Islands with our principal executive office in Bermuda.

For the three months ended March 31, 2010, SRGL reported net income attributable to ordinary shareholders of \$99.5 million, or \$0.46 per diluted ordinary share.

The \$99.5 million of net income attributable to ordinary shareholders for the three months ended March 31, 2010 was primarily driven by the following significant items:

Net Realized and Unrealized Gains

The market value of the Company’s invested assets, which primarily consist of fixed income securities, further benefited from recoveries in the global credit markets during the quarter. The total net realized and unrealized gains for the quarter were \$83.0 million.

Income tax benefit

For the three months ended March 31, 2010, the Company recorded an income tax benefit of \$36.4 million. This was principally a result of a reconsideration of an uncertain tax provision following a recent U.S. court tax ruling relating to an unaffiliated third party.

Excluding the significant items highlighted above, net income attributable to ordinary shareholders would have resulted in a net loss.

As of March 31, 2010, SRGL and Scottish Annuity & Life Insurance Company (Cayman) Ltd. (“SALIC”) had a combined \$136.4 million of unrestricted assets, compared to \$138.8 million at December 31, 2009. The unrestricted assets of SRGL and SALIC represent assets which are not held in trust accounts. These assets were available at March 31, 2010 to meet the obligations of SRGL and SALIC. There can be no assurances that the amount of unrestricted assets held by SRGL and SALIC will not further decrease from period to period.

SCOTTISH RE GROUP LIMITED
CONSOLIDATED BALANCE SHEETS
(Expressed in Thousands of United States Dollars, except share data)

	March 31, 2010 (Unaudited)	December 31, 2009
ASSETS		
Fixed maturity investments, trading at fair value	\$ 3,054,089	\$ 2,988,164
Preferred stock, trading at fair value	78,493	77,410
Cash and cash equivalents	397,499	390,025
Other investments	21,147	21,482
Funds withheld at interest	601,416	608,500
Total investments ¹	4,152,644	4,085,581
Accrued interest receivable ²	25,133	24,422
Reinsurance balances and risk fees receivable	139,075	161,977
Deferred acquisition costs	292,792	296,822
Amount recoverable from reinsurers	599,878	606,347
Present value of in-force business	38,412	38,316
Other assets ³	67,604	67,185
Embedded derivative assets at fair value	553	-
Current income tax receivable	12,769	12,762
Deferred tax assets	3,922	3,922
Total assets	<u>\$ 5,332,782</u>	<u>\$ 5,297,334</u>
LIABILITIES		
Reserves for future policy benefits	\$ 1,538,526	\$ 1,542,639
Interest sensitive contract liabilities	1,493,164	1,518,365
Collateral finance facilities ⁴	1,300,000	1,300,000
Accounts payable and other liabilities	44,818	68,921
Embedded derivative liabilities at fair value	38,557	35,732
Reinsurance balances payable	137,985	137,597
Deferred tax liabilities	48,756	50,143
Long term debt at fair value	42,147	55,068
Long term debt	129,500	129,500
Total liabilities	<u>4,773,453</u>	<u>4,837,965</u>
MEZZANINE EQUITY		
Convertible cumulative participating preferred shares, (liquidation preference, \$727.1 million)	555,857	555,857
Commitments and contingencies (Note 15)		
EQUITY (DEFICIT)		
Scottish Re Group Limited shareholders' deficit		
Ordinary shares, par value \$0.01:		
Issued 68,383,370 shares (2009 – 68,383,370)	684	684
Non-cumulative perpetual preferred shares, par value \$0.01:		
Issued: 5,000,000 shares (2009 – 5,000,000)	125,000	125,000
Additional paid-in capital	1,217,706	1,217,535
Retained deficit	(1,347,826)	(1,447,375)
Total Scottish Re Group Limited shareholders' deficit	(4,436)	(104,156)
Noncontrolling interest	7,908	7,668
Total equity (deficit)	<u>3,472</u>	<u>(96,488)</u>
Total liabilities, mezzanine equity and total equity (deficit)	<u>\$ 5,332,782</u>	<u>\$ 5,297,334</u>
¹ Includes total investments of consolidated variable interest entities ("VIE")	\$ 1,049,579	
² Includes accrued interest receivable of consolidated VIE	\$ 1,469	
³ Includes interest rate swap of consolidated VIE	\$ 30,224	
⁴ Reflects collateral finance facilities of consolidated VIE	\$ 1,300,000	

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

(Expressed in Thousands of United States Dollars, except share data)

	Three months ended	
	March 31, 2010	March 31, 2009 (Restated)
Revenues		
Premiums earned, net	\$ 102,523	\$ 99,386
Fee and other income	1,299	2,350
Investment income, net	43,997	44,190
Net realized and unrealized gains (losses)	82,977	(111,261)
Gain on de-consolidation of collateral finance facility	-	1,150,114
Change in value of long term debt at fair value	2,787	-
Gain on extinguishment of debt	-	53,545
Change in value of embedded derivatives, net	(2,272)	280,285
Total revenues	<u>231,311</u>	<u>1,518,609</u>
Benefits and expenses		
Claims and other policy benefits	109,325	(290,246)
Interest credited to interest sensitive contract liabilities	13,130	17,270
Acquisition costs and other insurance expenses, net...	18,367	38,836
Operating expenses	17,677	26,495
Collateral finance facilities expense	8,123	12,051
Interest expense	1,294	1,938
Total benefits and expenses	<u>167,916</u>	<u>(193,656)</u>
Income before income taxes	63,395	1,712,265
Income tax benefit (expense)	36,394	(50,942)
Consolidated income	99,789	1,661,323
Net (income) loss attributable to noncontrolling interest	(240)	259
Net income attributable to ordinary shareholders.	<u>\$ 99,549</u>	<u>\$ 1,661,582</u>
Basic income per ordinary share	<u>\$ 1.43</u>	<u>\$ 23.95</u>
Diluted income per ordinary share	<u>\$ 0.46</u>	<u>\$ 7.61</u>

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (DEFICIT)
(UNAUDITED)

(Expressed in Thousands of United States dollars, except share data)

	Three months ended	
	March 31, 2010	March 31, 2009 (Restated)
Share capital:		
Ordinary shares:		
Beginning and end of period.....	\$ 684	\$ 684
Non cumulative perpetual preferred shares:		
Beginning and end of period.....	125,000	125,000
Additional paid-in capital:		
Beginning of period	1,217,535	1,216,878
Option expense	171	5
End of period	1,217,706	1,216,883
Retained deficit:		
Beginning of period	(1,447,375)	(3,752,716)
Net income.....	99,549	1,661,582
End of period	(1,347,826)	(2,091,134)
Total Scottish Re Group Limited shareholders' deficit	\$ (4,436)	\$ (748,567)
Noncontrolling interest:		
Beginning of period	7,668	6,966
Net income (loss).....	240	(259)
End of period	7,908	6,707
Total shareholders' equity (deficit).....	\$ 3,472	\$ (741,860)

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(Expressed in Thousands of United States dollars)

	Three months ended	
	March 31, 2010	March 31, 2009 (Restated)
Operating activities		
Consolidated income	\$ 99,789	\$ 1,661,323
Adjustments to reconcile net income to net cash used in operating activities:		
Net realized and unrealized (gains) losses	(82,977)	111,262
Gain on de-consolidation of collateral finance facility	-	(1,150,114)
Change in value of long term debt at fair value	(2,787)	-
Gain on extinguishment of debt	-	(53,545)
Changes in value of embedded derivatives, net	2,272	(280,285)
Amortization of deferred acquisition costs	7,458	5,683
Amortization and write down of present value of in-force business	(96)	380
Write-off of fixed assets associated with the sale of the Acquired Business	-	6,289
Amortization of deferred transaction costs	617	768
Depreciation of fixed assets	138	386
Option expense	172	5
Changes in assets and liabilities:		
Accrued interest receivable	(711)	10,427
Reinsurance balances and risk fees receivable	23,290	142,398
Deferred acquisition costs	(3,427)	24,338
Deferred tax assets and liabilities	(1,387)	49,838
Other assets	6,177	(261,872)
Embedded derivative assets at fair value	553	-
Current income tax receivable and payable	(7)	139
Reserves for future policy benefits, net of amounts recoverable from reinsurers	2,356	(2,001,019)
Funds withheld at interest	7,083	1,176,795
Interest sensitive contract liabilities	27,713	(1,530)
Accounts payable and other liabilities	(21,281)	(234,457)
Embedded derivative liabilities at fair value	(2,825)	280,285
Net cash provided by (used in) operating activities	<u>62,120</u>	<u>(512,506)</u>
Investing activities		
Purchase of fixed maturity investments	(223,557)	(304,152)
Proceeds from sales and maturity of fixed maturity investments	220,423	585,431
Proceeds from sale and maturity of preferred stock	1,217	1,550
Purchase of and proceeds from other investments	299	(310)
Net cash (used in) provided by investing activities	<u>(1,618)</u>	<u>282,519</u>
Financing activities		
Withdrawals from interest sensitive contract liabilities	(53,028)	(90,387)
Net cash used in financing activities	<u>(53,028)</u>	<u>(90,387)</u>
Net change in cash and cash equivalents	\$ 7,474	\$ (320,374)
Cash and cash equivalents, beginning of period	390,025	824,613
Cash and cash equivalents, end of period	<u>\$ 397,499</u>	<u>\$ 504,239</u>

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

1. Organization and Business

Organization

Scottish Re Group Limited (“SRGL”, the “Company”, “we”, “our” and “us”) is a holding company incorporated under the laws of the Cayman Islands with our principal executive office in Bermuda. Through our operating subsidiaries, we are principally engaged in the reinsurance of life insurance, annuities and annuity-type products. We have principal operating companies in Bermuda, the Cayman Islands, Ireland, and the United States.

Run Off Strategy

In 2008, we ceased writing new business and notified our existing clients that we would not be accepting any new reinsurance risks under existing reinsurance treaties, thereby placing our remaining treaties into run-off. We expect to continue to pursue a run-off strategy for the remaining business, whereby we continue to receive premiums, pay claims and perform key activities under our remaining reinsurance treaties. Through prudent management of investments, reinsurance cash flows and operating expenses, our goal is to continue to satisfy our reinsurance and other obligations and to maintain a risk based capital ratio above the company action level prescribed by Delaware law and above any risk based capital-based recapture thresholds in our reinsurance agreements with ceding companies. No assurances can be given that we will be successful in implementing this strategy.

While pursuing our run-off strategy, we may from time to time, if opportunities arise, purchase in privately negotiated transactions, open market purchases or by means of general solicitations, tender offers or otherwise, additional amounts of our outstanding debt, non-voting preferred securities, and other liabilities. Any such purchases will depend on a variety of factors including, but not limited to, available corporate liquidity, capital requirements and indicative pricing levels. The amounts involved in any such transactions, individually or in the aggregate, may be material. For further discussion on our outstanding securities, see Note 7, “Debt Obligations and Other Funding Arrangements” and Note 16, “Subsequent Events”.

Regulatory Considerations

We currently operate with certain regulatory considerations in respect of Scottish Re (U.S.), Inc. (“SRUS”), our primary U.S. reinsurance subsidiary. In connection with the receipt by SRUS in late 2008 of a permitted statutory accounting practice related to the reduction from liability for reinsurance ceded to an unauthorized assuming insurer (the “Permitted Practice”), SRUS consented to the issuance by the Delaware Department of Insurance (the “Department”) on January 5, 2009, of an Order of Supervision against SRUS (the “Order of Supervision”), in accordance with 18 Del. C. §5942. The Order of Supervision required, among other things, the Department’s consent to any transaction by SRUS outside the ordinary course of business and any transaction with or any distribution or payment to its affiliates. The original Order of Supervision subsequently was amended and replaced with an Extended and Amended Order of Supervision, dated April 3, 2009 (the “Amended Order”), which amends and clarifies certain matters contained within the original Order of Supervision. See Note 12, “Regulatory and Rating Agencies”.

Business

We have written reinsurance business that is wholly or partially retained in one or more of our reinsurance subsidiaries. With the sale of our Wealth Management business and Life Reinsurance International Segment in 2008, and the subsequent sale of a block of individual life reinsurance business in our Life Reinsurance North America Segment (as more fully defined in Note 13, the “Acquired Business”) in the first quarter of 2009, operating decisions and performance assessments of the Company are now performed without reference to any separate segments. Accordingly, we do not present information about distinct operating segments for periods after January 1, 2009. For further discussion on the sale of a block of individual life reinsurance business in our Life Reinsurance North America Segment, see Note 13, “Sale of a Block of Life Reinsurance North America Business”.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

1. Organization and Business (continued)

We have assumed risks associated with primary life insurance, annuities and annuity-type policies. We reinsure mortality, investment, persistency and expense risks of United States life insurance and reinsurance companies. Most of the reinsurance assumed is through automatic treaties, but in 2006 we also began assuming risks on a facultative basis. We suspended bidding for new business on March 3, 2008, and at that time, we began issuing notices cancelling the acceptance of new reinsurance risks for all open reinsurance treaties. The business we historically have written falls into two categories: Traditional Solutions and Financial Solutions, as detailed below.

Traditional Solutions: We reinsure the mortality risk on life insurance policies written by primary insurers. The business often is referred to as traditional life reinsurance. We wrote our Traditional Solutions business predominantly on an automatic basis. This means that we automatically reinsured all policies written by a ceding company that met the underwriting criteria specified in the treaty with the ceding company. As discussed herein, we completed in 2009 the sale to Hannover Re of the Acquired Business, which business generally was a part of our Traditional Solutions business.

Financial Solutions: Financial Solutions include contracts under which we assumed the investment and persistency risks of existing, as well as newly written, blocks of business that improve the financial position of our clients by increasing their capital availability and statutory surplus. The products reinsured include annuities and annuity-type products, cash value life insurance and, to a lesser extent, disability products that are in a pay-out phase. This line of business includes acquired solutions products in which we provided our clients with exit strategies for discontinued lines of business, closed blocks of business, or lines of business not providing a good fit for a client's growth strategies.

Life insurance products that we reinsure include yearly renewable term, term with multi-year guarantees, ordinary life and variable life. Retail annuity products that we reinsure include fixed deferred annuities and variable annuities.

For these products, we wrote reinsurance generally in the form of yearly renewable term, coinsurance or modified coinsurance. Under yearly renewable term, we share only in the mortality risk for which we receive a premium. In a coinsurance or modified coinsurance arrangement, we generally share proportionately in all material risks inherent in the underlying policies, including mortality, lapses and investments. Under such agreements, we agree to indemnify the primary insurer for all or a portion of the risks associated with the underlying insurance policy in exchange for a proportionate share of premiums. Coinsurance differs from modified coinsurance with respect to the ownership of the assets supporting the reserves. Under our coinsurance arrangements, ownership of these assets is transferred to us, whereas in modified coinsurance arrangements, the ceding company retains ownership of these assets, but we share in the investment income and risk associated with the assets.

As discussed above, however, we have ceased writing new reinsurance treaties and no longer are accepting any new reinsurance risks under existing treaties or contracts with ceding companies.

2. Basis of presentation

Basis of Presentation

Accounting Principles - Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). These unaudited consolidated financial statements should be read in conjunction with both the audited consolidated financial statements and notes thereto for the year ended December 31, 2009.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

2. Basis of Presentation (continued)

Restatement of Prior Financial Statements - During the fourth quarter of 2009, we identified an error in the tax accounting following the sale of the Acquired Business to Hannover Re of \$49.8 million, representing deferred tax liabilities that reverse following the expiration of net operating losses in applicable jurisdictions. This error caused us to understate income tax expense as of March 31, 2009. We restated the income statement and earnings per share amounts in the first quarter of 2009 to reflect the increase in income tax expense of \$49.8 million. The restatement of the prior financial statements as a result of the error in tax accounting increased our shareholders deficit as of March 31, 2009 from \$698.7 million to \$748.5 million, and decreased our basic and diluted earnings per share attributable to ordinary shareholders from \$24.67 per share and \$7.84 per share, respectively, to \$23.95 per share and \$7.61 per share, respectively. There was no impact to our year ended December 31, 2009 net income or shareholders' deficit because the error was properly recorded in the annual consolidated financial statements.

Comprehensive Income – There are no items of other comprehensive income included in the consolidated statements of income and, therefore, net income attributable to ordinary shareholders is the same as comprehensive income attributable to ordinary shareholders.

Going Concern - These consolidated financial statements have been prepared using accounting principles applicable to a going concern, which contemplates the realization of assets and the satisfaction of liabilities and commitments in the normal course of business. Our ability to continue as a going concern is dependent upon our ability to successfully meet our obligations in a manner that addresses ongoing regulatory requirements and capital, liquidity and collateral needs. There can be no assurance that any of the actions we have taken or plan to take will be successful in supplying funds in amounts and at times necessary to meet our liquidity requirements in future periods. These consolidated financial statements do not give effect to any adjustments to recorded amounts and their classification which would be necessary if we were unable to continue as a going concern. We have a shareholders' deficit attributable to SRGL of \$4.4 million as of March 31, 2010.

In the event that for any reason we fail to comply with the Department's Amended Order, or in the event the financial condition of SRUS materially was to deteriorate, the Department may take action to seize control of SRUS under applicable insurance law. Such a seizure would place control of all management decisions of SRUS with the Department, including with respect to controlling cash flows, settling claims and paying obligations. The primary objective of the Department would be to protect the interests of the ceding insurers (and additionally their policyholders) with whom SRUS has contracted and would not be to protect the interests of SRGL, SALIC, the shareholders or any other stakeholders of the Company. A seizure of SRUS would have numerous consequences, including potentially triggering ceding company recapture rights on reinsurance agreements with us. Such seizure also may lead to the need for SALIC and SRGL to seek bankruptcy protection.

Consolidation - The consolidated financial statements include the assets, liabilities and results of operations of SRGL and its subsidiaries and all variable interest entities for which we are the primary beneficiary as defined in FASB ASC 810-10. All significant inter-company transactions and balances have been eliminated on consolidation. We consolidate two non-recourse securitizations: Orkney I and Orkney Re II. Effective January 1, 2009, we no longer consolidated Ballantyne Re. For further discussion on Orkney I, Orkney II and Ballantyne Re, see Note 14, "Collateral Finance Facilities". Effective October 8, 2009, we consolidated the Stingray Pass-Through Trust and the Stingray Investor Trust, see Note 7 "Debt Obligations and Other Funding Arrangements".

Estimates, Risks and Uncertainties - The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates and assumptions used by management. Our most significant assumptions are for:

- investment valuation;
- accounting for derivative instruments;

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

2. Basis of Presentation (continued)

- assessment of risk transfer for structured insurance and reinsurance contracts;
- estimates of premiums;
- valuation of present value of in-force business;
- establishment of reserves for future policy benefits;
- amortization of deferred acquisition costs;
- retrocession arrangements and amounts recoverable from reinsurers;
- interest sensitive contract liabilities;
- long term debt at fair value; and
- income taxes, deferred taxes and determination of the valuation allowance.

We review and revise these estimates as appropriate. Any adjustments made to these estimates are reflected in the period the estimates are revised.

All tabular amounts are reported in thousands of United States dollars, except share and per share data, or as otherwise noted.

3. Recent Accounting Pronouncements

FASB ASC Topic 820, Fair Value Measurements and Disclosure

In January 2010, the FASB issued an update to require a number of additional disclosures regarding fair value measurements. Specifically, the update requires a reporting entity to disclose the amounts of significant transfers between Level 1 and Level 2 of the three tier fair value hierarchy and the reasons for these transfers, as well as the reasons for any transfers in or out of Level 3, effective for annual and interim periods beginning after December 15, 2009. The update also requires information in the reconciliation of recurring Level 3 measurements about purchases, sales, issuances, and settlements on a gross basis, effective for annual and interim periods beginning after December 15, 2010. We adopted this update in its entirety, including early adoption of the additional Level 3 information, effective January 1, 2010. The adoption of this update had no effect on our financial position or results of operations.

FASB ASC Topic 810, Consolidation

In June 2009, the FASB issued an update to FASB ASC Topic 810. This update requires an enterprise to perform an analysis to determine whether the enterprise's variable interest or variable interests give it a controlling financial interest in a VIE. This update also requires ongoing reassessments of whether an enterprise is the primary beneficiary of a VIE and is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within the first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application was prohibited. We adopted this update effective January 1, 2010 and the additional disclosure requirements are reflected on the Consolidated Balance Sheets as at March 31, 2010. The adoption of this update had no effect on our financial position or results of operations.

4. Investments

Trading investments are recorded at fair market value. Unrealized holding gains and losses on trading investments are included in earnings. Interest is recorded based upon the stated coupon rate as a component of net investment income. Cash flows for trading securities are classified in Investing Activities on the Consolidated Statement of Cash Flows based on the nature and purpose for which the related securities were acquired.

The portion of net unrealized gains (losses) for the three months ended March 31, 2010 and 2009, that relates to trading securities still held at the reporting date is \$69.1 million and (\$123.6) million, respectively.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

5. Fair Value Measurements

FASB ASC 820 establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value, and enhances disclosure requirements for fair value measurements. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820 are described below:

Level 1 – Quoted prices for identical instruments in active markets.

Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.

Level 3 – Model derived valuations in which one or more significant inputs or significant value drivers are unobservable.

As required by FASB ASC 820, when the inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement in its entirety. Thus, a Level 3 fair value measurement may include inputs that are observable (Level 1 and 2) and unobservable (Level 3).

Level 1 primarily consists of financial instruments whose value is based on quoted market prices such as public equities and actively traded mutual fund investments.

Level 2 includes those financial instruments that are valued by independent pricing services or valued using models or other valuation methodologies. These models are primarily industry-standard models that consider various inputs, such as interest rate, credit spread and foreign exchange rates for the underlying financial instruments. All significant inputs are observable, or derived from observable, information in the marketplace or are supported by observable levels at which transactions are executed in the marketplace. Financial instruments in this category primarily include: certain public and private corporate fixed maturity and equity securities; government or agency securities; certain mortgage and asset-backed securities; securities held as collateral; and segregated assets.

Level 3 is comprised of financial instruments whose fair value is estimated based on non-binding broker prices or internally developed models or methodologies utilizing significant inputs not based on, or corroborated by, readily available market information. This category primarily consists of certain less liquid fixed maturity and equity securities where we cannot corroborate the significant valuation inputs with market observable data. Additionally, the Company's embedded derivatives, all of which are associated with reinsurance treaties, are classified in Level 3 since their values include significant unobservable inputs associated with actuarial assumptions regarding policyholder behavior.

At each reporting period, all assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability, such as the relative impact on the fair value as a result of including a particular input.

The majority of our fixed maturity securities use Level 2 inputs for the determination of fair value. These fair values are obtained primarily from independent pricing services, when available, utilizing Level 2 inputs. Where pricing services do not provide fair values, the pricing services utilize proprietary pricing models to produce estimates of fair value primarily utilizing Level 2 inputs along with certain Level 3 inputs.

The proprietary pricing models include matrix pricing where we discount expected cash flows utilizing market interest rates obtained from third-party sources based on the credit quality and duration of the instrument to

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

5. Fair Value Measurements (continued)

fair value. For securities that may not be reliably priced using internally developed pricing models, broker quotes are obtained. These broker quotes represent an exit price but the assumptions used to establish the fair value may not be observable and represent Level 3 inputs.

Long term debt at fair value has been valued using Level 2 input for the determination of fair value. The fair value was derived with reference to traded prices for identical liabilities and observable market inputs for similar liabilities.

The interest rate swap derivative has been valued using Level 2 inputs including forward interest rates derived from observable information in the market place.

The embedded derivatives in funds withheld at interest include the embedded derivatives resulting from assumed modified coinsurance (“modco”) or coinsurance funds withheld reinsurance arrangements. These values are based upon the difference between the fair value of the underlying assets backing the modco or funds withheld receivable and the fair value of the underlying liabilities.

The fair value of the asset generally is based upon observable market data using valuation methods similar to those used for assets held directly by us. The fair value of the liabilities is determined by using market observable swap rates as well as some unobservable inputs such as actuarial assumptions regarding policyholder behavior. These assumptions require significant management judgment.

The following tables set forth our assets and liabilities that are measured at fair value on a recurring basis as of the date indicated:

	March 31, 2010			
(U.S. dollars in millions)	Total	Level 1	Level 2	Level 3
Investments				
Government securities.....	\$ 92.4	\$ -	\$ 92.2	\$ 0.2
Corporate securities.....	1,189.9		1,053.1	136.8
Municipal bonds.....	54.8		44.9	9.9
Mortgage and asset backed securities.....	1,717.0		1,231.5	485.5
Preferred stock.....	78.5	-	22.5	56.0
Equity.....	3.7	3.7	-	-
Derivatives – interest rate swap.....	30.2	-	30.2	-
Funds withheld at interest – embedded derivatives	0.6	-	-	0.6
Total assets at fair value.....	\$ 3,167.1	\$ 3.7	\$ 2,474.4	\$ 689.0
Funds withheld at interest – embedded derivatives.....	(38.6)	-	-	(38.6)
Long term debt at fair value.....	(42.1)		(42.1)	-
Total liabilities at fair value.....	\$ (80.7)	\$ -	\$ (42.1)	\$ (38.6)

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

5. Fair Value Measurements (continued)

(U.S. dollars in millions)	December 31, 2009			
	Total	Level 1	Level 2	Level 3
Investments				
Government securities.....	\$ 104.6	\$ -	\$ 104.4	\$ 0.2
Corporate securities.....	1,166.3	-	1,033.0	133.3
Municipal bonds.....	43.8	-	43.8	-
Mortgage and asset backed securities.....	1,673.5	-	1,200.7	472.8
Preferred stock	77.4	-	24.0	53.4
Equity	3.7	3.7	-	-
Derivatives – interest rate swap.....	25.9	-	25.9	-
Total assets at fair value	<u>\$ 3,095.2</u>	<u>\$ 3.7</u>	<u>\$ 2,431.8</u>	<u>\$ 659.7</u>
Embedded derivatives	(35.7)	-	-	(35.7)
Long term debt at fair value	(55.1)	-	(55.1)	-
Total liabilities at fair value.....	<u>\$ (90.8)</u>	<u>\$ -</u>	<u>\$ (55.1)</u>	<u>\$ (35.7)</u>

The following tables present additional information about assets measured at fair value on a recurring basis and for which we have utilized significant unobservable (Level 3) inputs to determine fair value:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) for the three month period ended March 31, 2010

(U.S. dollars in millions)	Funds			Total
	Fixed Maturities & Preferred Stock	Withheld at Interest – Embedded Derivatives, Net		
Beginning balance at January 1, 2010.....	\$ 659.7	\$ (35.7)		\$ 624.0
Total realized and unrealized gains (losses)				
included in net income	34.7	(2.3)		32.4
Purchases, issuances and settlements.....	(7.9)	-		(7.9)
Transfers in and/or out of Level 3.....	1.9	-		1.9
Ending balance at March 31, 2010.....	<u>\$ 688.4</u>	<u>\$ (38.0)</u>		<u>\$ 650.4</u>

Reclassifications impacting Level 3 financial instruments are reported as transfers in (out) of the Level 3 category as of the beginning of the quarter in which the transfer occurs. Therefore gains and losses in income only reflect activity for the period in which the transfer occurs.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

5. Fair Value Measurements (continued)

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) for the year ended December 31, 2009

(U.S. dollars in millions)	Fixed Maturities & Preferred Stock	Other Liabilities at Fair Value – Embedded Derivatives	Total
Beginning balance at January 1, 2009	\$ 921.6	\$ (347.5)	\$ 574.1
Transfers attributable to deconsolidation of			
Ballantyne Re.....	(108.6)	-	(108.6)
Total realized and unrealized gains (losses)			
included in net income	(16.9)	311.8	294.9
Purchases, issuances and settlements.....	(43.8)	-	(43.8)
Transfers in and/or out of Level 3.....	(92.6)	-	(92.6)
Ending balance at December 31, 2009.....	\$ 659.7	\$ (35.7)	\$ 624.0

The portion of net unrealized gains for the three months ended March 31, 2010 that relates to trading securities still held at the reporting date is \$29.8 million for Level 3.

We review the fair value hierarchy classifications quarterly. Changes in the observability of the valuation attributes may result in a reclassification of certain financial assets or liabilities.

6. Fair Value of Financial Instruments

As discussed above, fair value of financial assets and liabilities is estimated under FASB ASC 820 using the following methods and assumptions:

(i) Fixed maturity investments and preferred stock are carried at fair value. See Note 5, “Fair Value Measurements” for a description of the methodologies and assumptions used to determine the fair value of financial instruments carried at fair value.

(ii) Other investments carrying value approximates fair value.

(iii) Funds withheld at interest represent fixed maturity investments held by ceding companies and the fair values are consistent with the methodologies and assumptions used to determine the fair value of fixed maturities carried at fair value.

(iv) Fair values for collateral finance facilities prioritize the utilization of market observable inputs. For any notes issued by the collateral finance facilities that are wrapped by guarantors, we defined the unit of value as the combination of the issued note and guarantee. As a result, the fair value of the collateral finance facilities incorporates the value of the guarantee, including consideration of the non-performance risk of the guarantors.

(v) Fair value of the interest rate swap derivative has been calculated with reference to observable market inputs. See Note 5, “Fair Value Measurements” for a description of the methodologies and assumptions used to determine the fair value of financial instruments carried at fair value.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

6. Fair Value of Financial Instruments (continued)

(vi) Long term debt at fair value (i.e. outstanding Pass-Through Certificates held by third parties) have been derived with reference to traded prices for identical liabilities and observable market inputs for similar liabilities. See Note 5, "Fair Value Measurements" for a description of the methodologies and assumptions used to determine the fair value of financial instruments carried at fair value.

(vii) Fair values for our long term debt of trust preferred securities were determined with reference to similar quoted securities and settlements of other Company long term debt during 2010 and 2009.

(viii) Interest sensitive contract liabilities include amounts payable under funding agreements and investment contracts. The fair value for amounts payable under funding agreements was determined by a third party service provider. The fair value of investment contracts, which exclude significant mortality risk, is based on the cash surrender value of the liabilities as an approximation of the exit market.

(ix) Embedded derivative assets and liabilities are carried at fair value. See Note 5, "Fair Value Measurements" for a description of the methodologies and assumptions used to determine the fair value of financial instruments carried at fair value.

(U.S. dollars in thousands)	March 31, 2010		December 31, 2009	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Assets				
Fixed maturity investments.....	\$ 3,054,089	\$ 3,054,089	\$ 2,988,164	\$ 2,988,164
Preferred stock	78,493	78,493	77,410	77,410
Other investments	21,147	21,147	21,482	21,482
Funds withheld at interest (excluding cash).....	601,416	521,630	608,500	513,419
Derivatives – interest rate swap	30,224	30,224	25,924	25,924
Embedded derivative assets at fair value.....	553	553	-	-
Liabilities				
Collateral finance facilities	\$ 1,300,000	\$ 885,057	\$ 1,300,000	\$ 907,710
Long term debt at fair value	42,147	42,147	55,068	55,068
Long term debt.....	129,500	32,375	129,500	32,375
Investment contracts	1,493,164	1,460,835	1,518,365	1,485,554
Embedded derivative liabilities at fair value	38,557	38,557	35,732	35,732

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

7. Debt Obligations and Other Funding Arrangements

Long-term debt consists of:

(U.S. dollars in thousands)	March 31, 2010	December 31, 2009
Capital securities due 2032.....	\$ 17,500	\$ 17,500
Preferred trust securities due 2033	20,000	20,000
Trust preferred securities due 2033	10,000	10,000
Trust preferred securities due 2034	32,000	32,000
Trust preferred securities due 2034	50,000	50,000
Long term debt at par value.....	\$ 129,500	\$ 129,500
Outstanding Pass-Through Certificates	\$ 42,147	\$ 55,068
Long term debt at fair value	\$ 42,147	\$ 55,068

Capital Securities Due 2032

On December 4, 2002, Scottish Holdings Statutory Trust I, a Connecticut statutory business trust (“Capital Trust”) issued and sold in a private offering an aggregate of \$17.5 million Floating Rate Capital Securities (the “Capital Securities”). All of the common shares of the Capital Trust are owned by Scottish Holdings, Inc. (“SHI”), our wholly owned subsidiary.

The Capital Securities mature on December 4, 2032. They are redeemable in whole or in part at any time after December 4, 2007. Interest is payable quarterly at a rate equivalent to three-month LIBOR plus 4%. At March 31, 2010 and December 31, 2009, the interest rates were 4.29% and 4.25%, respectively. The Capital Trust may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than December 4, 2032. Any deferred payments would accrue interest quarterly on a compounded basis if SHI defers interest on the Debentures due December 4, 2032 (as described below).

The sole assets of the Capital Trust consist of \$18 million principal amount of Floating Rate Debentures (the “Debentures”) issued by SHI. The Debentures mature on December 4, 2032 and interest is payable quarterly at a rate equivalent to three-month LIBOR plus 4%. At March 31, 2010 and December 31, 2009, the interest rates were 4.29% and 4.25%, respectively. SHI may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than December 4, 2032. Any deferred payments would accrue interest quarterly on a compounded basis. SHI may redeem the Debentures at any time after December 4, 2007 and in the event of certain changes in tax or investment company law.

SALIC has guaranteed SHI’s obligations under the Debentures and distributions and other payments due on the Capital Securities.

Preferred Trust Securities Due 2033

On October 29, 2003, Scottish Holdings, Inc. Statutory Trust II, a Connecticut statutory business trust (“Capital Trust II”) issued and sold in a private offering an aggregate of \$20 million Preferred Trust Securities (the “Preferred Trust Securities”). All of the common shares of Capital Trust II are owned by SHI.

The Preferred Trust Securities mature on October 29, 2033. They are redeemable in whole or in part at any time after October 29, 2008. Interest is payable quarterly at a rate equivalent to three-month LIBOR plus 3.95%. At March 31, 2010 and December 31, 2009, the interest rates were 4.24% and 4.20%, respectively. Prior to October 29, 2008, interest cannot exceed 12.45%. Capital Trust II may defer payment of the interest for up to 20 consecutive

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

7. Debt Obligations and Other Funding Arrangements (continued)

quarterly periods, but no later than October 29, 2033. Any deferred payments would accrue interest quarterly on a compounded basis if SHI defers interest on the 2033 Floating Rate Debentures due October 29, 2033 (as described below).

The sole assets of Capital Trust II consist of \$20.6 million principal amount of Floating Rate Debentures (the "2033 Floating Rate Debentures") issued by SHI. The 2033 Floating Rate Debentures mature on October 29, 2033 and interest is payable quarterly at three-month LIBOR plus 3.95%. At March 31, 2010 and December 31, 2009, the interest rates were 4.24% and 4.20%, respectively. SHI may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than October 29, 2033. Any deferred payments would accrue interest quarterly on a compounded basis. SHI may redeem the 2033 Floating Rate Debentures at any time after October 29, 2008 and in the event of certain changes in tax or investment company law.

SALIC has guaranteed SHI's obligations under the 2033 Floating Rate Debentures and distributions and other payments due on the Preferred Trust Securities.

Trust Preferred Securities Due 2033

On November 14, 2003, GPIC Holdings Inc. Statutory Trust, a Delaware statutory business trust ("GPIC Trust") issued and sold in a private offering an aggregate of \$10 million Trust Preferred Securities (the "2033 Trust Preferred Securities"). All of the common shares of GPIC Trust are owned by SHI.

The 2033 Trust Preferred Securities mature on September 30, 2033. They are redeemable in whole or in part at any time after September 30, 2008. Interest is payable quarterly at a rate equivalent to three-month LIBOR plus 3.90%. At March 31, 2010 and December 31, 2009, the interest rates were 4.19% and 4.15%, respectively. GPIC Trust may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than September 30, 2033. Any deferred payments would accrue interest quarterly on a compounded basis if SHI defers interest on the Junior Subordinated Notes due September 30, 2033 (as described below).

The sole assets of GPIC Trust consist of \$10.3 million principal amount of Junior Subordinated Notes (the "Junior Subordinated Notes") issued by SHI. The Junior Subordinated Notes mature on September 30, 2033 and interest is payable quarterly at three-month LIBOR plus 3.90%. At March 31, 2010 and December 31, 2009, the interest rates were 4.19% and 4.15%, respectively. SHI may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than September 30, 2033. Any deferred payments would accrue interest quarterly on a compounded basis. SHI may redeem the Junior Subordinated Notes at any time after September 30, 2008 and in the event of certain changes in tax or investment company law.

SALIC has guaranteed SHI's obligations under the Junior Subordinated Notes and distributions and other payments due on the trust preferred securities.

Trust Preferred Securities Due 2034

On May 12, 2004, Scottish Holdings, Inc. Statutory Trust III, a Connecticut statutory business trust ("Capital Trust III") issued and sold in a private offering an aggregate of \$32 million Trust Preferred Securities (the "2034 Trust Preferred Securities"). All of the common shares of Capital Trust III are owned by SHI.

The 2034 Trust Preferred Securities mature on June 17, 2034. They are redeemable in whole or in part at any time after June 17, 2009. Interest is payable quarterly at a rate equivalent to three-month LIBOR plus 3.80%. At March 31, 2010 and December 31, 2009, the interest rate was 4.09% and 4.05%, respectively. Prior to June 17, 2009, interest could not exceed 12.50%. Capital Trust III may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than June 17, 2034. Any deferred payments would accrue interest quarterly on a

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

7. Debt Obligations and Other Funding Arrangements (continued)

compounded basis if SHI defers interest on the 2034 Floating Rate Debentures due June 17, 2034 (as described below).

The sole assets of Capital Trust III consist of \$33 million principal amount of Floating Rate Debentures (the “2034 Floating Rate Debentures”) issued by SHI. The 2034 Floating Rate Debentures mature on June 17, 2034 and interest is payable quarterly at three-month LIBOR plus 3.80%. At March 31, 2010 and December 31, 2009, the interest rate was 4.09% and 4.05%, respectively. Prior to June 17, 2009, interest could not exceed 12.50%. SHI may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than June 17, 2034. Any deferred payments would accrue interest quarterly on a compounded basis. SHI may redeem the 2034 Floating Rate Debentures at any time after June 17, 2009 and in the event of certain changes in tax or investment company law.

SALIC has guaranteed SHI’s obligations under the 2034 Floating Rate Debentures and distributions and other payments due on the 2034 Trust Preferred Securities.

Trust Preferred Securities Due 2034

On December 18, 2004, SFL Statutory Trust I, a Delaware statutory business trust (“SFL Trust I”) issued and sold in a private offering an aggregate of \$50 million Trust Preferred Securities (the “December 2034 Trust Preferred Securities”) and, together with the 2034 Trust Preferred Securities, the 2033 Trust Preferred Securities, the Preferred Trust Securities and the Capital Securities, the “Capital and Trust Preferred Securities”). All of the common shares of SFL Trust I are owned by Scottish Financial (Luxembourg) S.a.r.l (“SFL”).

The December 2034 Trust Preferred Securities mature on December 15, 2034. They are redeemable in whole or in part at any time after December 15, 2009. Interest is payable quarterly at a rate equivalent to three-month LIBOR plus 3.50%. At March 31, 2010 and December 31, 2009, the interest rate was 3.79% and 3.75%, respectively. Prior to December 15, 2009, interest could not exceed 12.50%. SFL Trust I may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than December 15, 2034. Any deferred payments would accrue interest quarterly on a compounded basis if SFL defers interest on the 2034 Floating Rate Debentures due December 15, 2034 (as described below).

The sole assets of SFL Trust I consist of \$51.5 million principal amount of Floating Rate Debentures (the “December 2034 Floating Rate Debentures”) issued by SFL. The December 2034 Floating Rate Debentures mature on December 15, 2034 and interest is payable quarterly at three-month LIBOR plus 3.50%. At March 31, 2010 and December 31, 2009, the interest rate was 3.79% and 3.75%, respectively. Prior to December 15, 2009, interest could not exceed 12.50%. SFL may defer payment of the interest for up to 20 consecutive quarterly periods, but no later than December 15, 2034. Any deferred payments would accrue interest quarterly on a compounded basis. SFL may redeem the December 2034 Floating Rate Debentures at any time after December 15, 2009 and in the event of certain changes in tax or investment company law.

SALIC has guaranteed SFL’s obligations under the December 2034 Floating Rate Debentures and distributions and other payments due on the December 2034 Trust Preferred Securities.

Stingray Investor Trust and Stingray Pass-Through Trust (together “Stingray”)

On January 12, 2005, SALIC entered into a put agreement with the Stingray Investor Trust for an aggregate value of \$325 million, which put agreement relates to \$325 million aggregate stated amount of 5.902% Pass-Through Certificates (the “Pass-Through Certificates”) issued by the Stingray Pass-Through Trust (together with the Stingray Investor Trust, “Stingray”). Under the terms of the put agreement, we acquired an irrevocable put option to issue funding agreements to the Stingray Investor Trust in return for the assets in a portfolio of 30-day commercial paper.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

7. Debt Obligations and Other Funding Arrangements (continued)

Since April 14, 2008, this facility has been fully utilized and \$325 million of funding agreements have been issued to the Stingray Investor Trust and remain outstanding as of March 31, 2010.

Throughout 2009, we acquired Pass-Through Certificates in privately negotiated purchases which represented reconsideration events under FASB ASC 810-10. We used a quantitative analysis in determining that the holder of the majority of the Pass-Through Certificates would absorb the majority of the expected gains or losses of Stingray. As a result of these acquisitions, by October 8, 2009, we had acquired Pass-Through Certificates with a stated amount of \$169.4 million. This holding represented the majority of the Pass-Through Certificates; therefore at that time we determined we were the primary beneficiary of Stingray and we were required to consolidate Stingray in our consolidated financial statements. The consolidation of Stingray has been recorded in accordance with ASC 810-10, which requires us to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in Stingray at the acquisition date, measured at their fair values as of that date. We are also required to eliminate any inter-company balances and transactions. The Stingray structure includes an interest rate swap as a mechanism for charging interest to SALIC on the funding agreements at a variable interest rate and paying interest to the Pass-Through Certificate holders at a fixed rate. The interest rate swap is included in Other Assets at a fair value of \$30.2 million and \$25.9 million on our Consolidated Balance Sheets as at March 31, 2010 and December 31, 2009, respectively. Movements in the fair value of the interest rate swap are included in net realized and unrealized income (losses) in the Consolidated Statements of Income.

On December 15, 2009, pursuant to a cash tender offer that had been launched on November 16, 2009, we acquired \$57.3 million in aggregate stated amount of Pass-Through Certificates. As a result, as of December 31, 2009, we had repurchased \$226.7 million in aggregate stated amount of the Pass-Through Certificates, leaving \$98.3 million outstanding with non-affiliated investors.

In January 2010, we acquired in a privately negotiated transaction an additional \$18.1 million of aggregate stated amount of Pass-Through Certificates, leaving \$80.2 million in aggregate stated amount of the Pass-Through Certificates outstanding with non-affiliated investors as of March 31, 2010.

We have elected the fair value option under FASB ASC 825 in respect of the Pass-Through Certificates held by non-affiliated investors. We elected this option as we believe it will reflect more appropriately the value of the liability at subsequent reporting periods. The fair value as at March 31, 2010 and December 31, 2009 of the outstanding Pass-Through Certificates held by non-affiliated investors is \$42.1 million and \$55.1 million, respectively, and is included in long term debt at fair value in our Consolidated Balance Sheets. Changes in fair value will be reflected through earnings. The change in fair value, for the three months ended March 31, 2010, of the Pass-Through Certificates held by non-affiliated investors resulted in a gain of \$2.8 million. See Note 5, "Fair Value Measurements".

Premium Asset Trust Series 2004-4

On March 12, 2004, SALIC entered into an unsecured funding agreement with the Premium Asset Trust for an aggregate of \$100 million (the "PATS"). The funding agreement had a stated maturity of March 12, 2009 (the "PATS Maturity Date") and accrued interest at a rate of three-month LIBOR plus 0.922%, payable on a quarterly basis. The amount due under this funding agreement was included under interest sensitive contract liabilities on the Consolidated Balance Sheets.

During the first quarter of 2009, we extinguished, primarily through negotiated repurchases, SALIC's unsecured funding agreement payment obligation in respect of the PATS. The extinguishment of PATS securities acquired through negotiated repurchases and the settlement of the remaining funding obligation in respect of all PATS securities not repurchased prior to the Maturity Date were completed for a total consideration of \$46.5 million compared to the \$100 million par value of the PATS. Consequently, in accordance with FASB ASC Topic 860, Transfers and Servicing, we recorded a gain on the extinguishment of the PATS debt of \$53.5 million in the first

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

7. Debt Obligations and Other Funding Arrangements (continued)

quarter of 2009. The funding agreements were included in interest sensitive contract liabilities in the accompanying Consolidated Balance Sheets at December 31, 2008.

Deferral of Interest Payments on Floating Rate Capital Securities and Trust Preferred Securities

In order to preserve liquidity, we began deferring interest payments as of March 4, 2009 on our floating rate capital securities and trust preferred securities issued and sold through certain statutory trusts established by us. These deferrals are permitted by the terms of the indentures governing the securities and have been made at the discretion of our Board to preserve liquidity. We intend to continue to defer such interest payments for the duration of the permitted 20 consecutive quarterly periods to maximize liquidity. As of March 31, 2010, we have accrued and deferred payment of \$7.4 million of interest. SHI and SALIC are restricted in their ability to make dividend payments in any period where interest payment obligations on these securities are not current.

For further discussion on the accrued and deferred payment on our floating rate capital securities and trust preferred securities subsequent to March 31, 2010, see Note 16, "Subsequent Events".

8. Mezzanine Equity

Convertible Cumulative Participating Preferred Shares

On May 7, 2007, we completed the equity investment transaction by MassMutual Capital Partners LLC ("MassMutual Capital"), a member of the MassMutual Financial Group, and SRGL Acquisition, LDC, an affiliate of Cerberus Capital Management, L.P. ("Cerberus"), announced by us on November 27, 2006 (the "2007 New Capital Transaction"). Pursuant to the 2007 New Capital Transaction, MassMutual Capital and Cerberus invested an aggregate \$600 million in us in exchange for 1,000,000 in the aggregate newly issued Convertible Cumulative Participating Preferred Shares. The gross proceeds were \$600 million less \$44.1 million in closing costs, which resulted in aggregate net proceeds of \$555.9 million. Each Convertible Cumulative Participating Preferred Share has a par value of \$0.01 per share with a liquidation preference of \$600 per share, as adjusted for dividends or distributions as described further below.

As of March 31, 2010, MassMutual Capital and Cerberus hold in the aggregate approximately 68.7% of our equity voting power, along with the right to designate two-thirds of the members of our Board.

The Convertible Cumulative Participating Preferred Shares are convertible at the option of the holder, at any time, into an aggregate of 150,000,000 ordinary shares of SRGL. On the ninth anniversary of issue, the Convertible Cumulative Participating Preferred Shares automatically will convert into an aggregate of 150,000,000 ordinary shares if not previously converted. We are not required at any time to redeem the Convertible Cumulative Participating Preferred Shares for cash, except in the event of a liquidation or a change-in-control event.

We have accounted for the Convertible Cumulative Participating Preferred Shares in accordance with FASB ASC Subtopic 470-20, Debt – Debt with Conversion and Other Options ("FASB 470-20"), which incorporates EITF D-98: "Classification and Measurement of Redeemable Securities". Dividends on the Convertible Cumulative Participating Preferred Shares are cumulative and accrete daily on a non-compounding basis at a rate of 7.25% per annum on the stated value of \$600 million. Dividends only will be paid in a liquidation preference scenario upon our liquidation or change-in-control prior to the ninth anniversary. There have been no dividends accrued in the period as this scenario is not deemed probable at this time. As of March 31, 2010, the amount of dividends not accrued pursuant to the terms of the Convertible Cumulative Participating Preferred Shares is \$127.1 million in the aggregate, or \$127 per share.

To the extent that the Convertible Cumulative Participating Preferred Shares participate on an as-converted basis in dividends paid on ordinary shares, a corresponding reduction will be made to the liquidation preference for

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

8. Mezzanine Equity (continued)

the Convertible Cumulative Participating Preferred Shares. The Convertible Cumulative Participating Preferred Shares have a liquidation preference equal to their stated value, as adjusted for (x) the accretion of dividends and (y) any cash payment or payment in property of dividends or distributions. The holders of Convertible Cumulative Participating Preferred Shares may, among other things, require us to redeem the Convertible Cumulative Participating Preferred Shares upon a change-in-control.

Upon a change-in-control, the redemption price of the Convertible Cumulative Participating Preferred Shares is an amount equal to the greater of (i) the stated value of the outstanding Convertible Cumulative Participating Preferred Shares, plus an amount equal to the sum of all accrued dividends through the earlier of (A) the date of payment of the consideration payable upon a change-in-control, or (B) the fifth anniversary of the issue date of the Convertible Cumulative Participating Preferred Shares, or (ii) the amount that the holder of the Convertible Cumulative Participating Preferred Shares would have been entitled to receive with respect to such change-in-control if it had exercised its right to convert all or such portion of its Convertible Cumulative Participating Preferred Shares for ordinary shares immediately prior to the date of such change-in-control.

The liquidation preference of the Convertible Cumulative Participating Preferred Shares is not applicable once the Convertible Cumulative Participating Preferred Shares have been converted into ordinary shares, as described above.

The Convertible Cumulative Participating Preferred Shares rank, with respect to payment of dividends and distribution of assets upon voluntary or involuntary liquidation, dissolution or winding-up (a "Liquidation Event"): (a) senior to our ordinary shares and to each other class or series of our shares established by the Board, the terms of which do not expressly provide that such class or series ranks senior to or pari passu with the Convertible Cumulative Participating Preferred Shares as to payment of dividends and distribution of assets upon a Liquidation Event; (b) pari passu with each class or series of our shares, the terms of which expressly provide that such class or series ranks pari passu with the Convertible Cumulative Participating Preferred Shares as to payment of dividends and distribution of assets upon a Liquidation Event; and (c) junior to each other class or series of our securities outstanding as of the date of the completion of the 2007 New Capital Transaction that ranks senior to our ordinary shares, and to each class or series of our shares, the terms of which expressly provide that such class or series ranks senior to the Convertible Cumulative Participating Preferred Shares as to payment of dividends and distribution of assets upon a Liquidation Event and all classes of our preferred shares outstanding as of the completion of the 2007 New Capital Transaction.

The Convertible Cumulative Participating Preferred Shares conversion price (\$4.00 per ordinary share) was lower than the trading value of \$4.66 of our ordinary shares on the date of issue. This discount has been accounted for as an embedded beneficial conversion feature in accordance with FASB ASC 470-20 which incorporates EITF 98-5, "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios", and EITF 00-27, "Application of Issue No. 98-5 to Certain Convertible Instruments". Accordingly, the Company recognized a \$120.8 million embedded beneficial conversion feature, which reduced the Convertible Cumulative Participating Preferred Share issue amount shown in Mezzanine Equity and increased the amount of additional paid in capital. Under the accounting guidance above, we had the choice to accrete the full intrinsic value of the embedded beneficial conversion feature out of retained earnings over the nine year term of the shares or immediately due to the ability of the holders to convert at their option at any time. Given the ability of the holders to convert at any time, we elected to accrete the full intrinsic value of the embedded beneficial conversion feature on the date of issue. As we did not have any retained earnings on the date of issue, the \$120.8 million beneficial conversion feature was accreted out of additional paid in capital into Mezzanine Equity.

Pursuant to our Securities Purchase Agreement, dated November 26, 2006 (the "Agreement"), with MassMutual Capital and Cerberus, certain representations and warranties were provided relating to our statutory accounting records. As discussed in Note 15 "Commitments and Contingencies", certain statutory accounting errors were

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

8. Mezzanine Equity (continued)

discovered in 2006 which have resulted in an indemnification claim against us, by MassMutual and Cerberus. Resolution of this claim could result in a change in the conversion formula on these securities.

9. Non-cumulative Perpetual Preferred Shares (“Perpetual Preferred Shares”)

Perpetual Preferred Shares

We are authorized to issue 50,000,000 preferred shares of par value \$0.01 each.

On June 28, 2005, we priced our offering of 5,000,000 non-cumulative Perpetual Preferred Shares (the “Perpetual Preferred Shares”) and entered into a purchase agreement relating to the shares pursuant to which the underwriters of the offering agreed to purchase the shares. Gross proceeds were \$125 million and related expenses were \$4.6 million. Settlement of the net proceeds occurred on July 6, 2005.

Dividends on the Perpetual Preferred Shares are payable on a non-cumulative basis at a rate per annum of 7.25% until the dividend payment date in July 2010. Thereafter, the dividend rate may be at a fixed rate determined through remarketing of the Perpetual Preferred Shares for specific periods of varying length not less than six months or may be at a floating rate reset quarterly based on a predefined set of interest rate benchmarks. During any dividend period, unless the full dividends for the current dividend period on all outstanding Perpetual Preferred Shares have been declared or paid, no dividend shall be paid or declared on our ordinary shares and no ordinary shares or other junior shares shall be purchased, redeemed or otherwise acquired for consideration. Declaration of dividends on the Perpetual Preferred Shares is prohibited if we fail to meet specified capital adequacy, net income or shareholders’ equity levels.

The Perpetual Preferred Shares do not have a maturity date and we are not required to redeem the shares. The Perpetual Preferred Shares are not redeemable prior to July 2010. Subsequent to July 2010, the Perpetual Preferred Shares will be redeemable at our option, in whole or in part, at a redemption price equal to \$25.00 per share, plus any declared and unpaid dividends at the redemption date, without accumulation of any undeclared dividends. The Perpetual Preferred Shares are unsecured and subordinated to all indebtedness that does not by its terms rank *pari passu* or junior to the Perpetual Preferred Shares. The holders of the Perpetual Preferred Shares have no voting rights except with respect to certain fundamental changes in the terms of the Perpetual Preferred Shares and in the case of certain dividend non-payments.

The Perpetual Preferred Shares ratings were withdrawn by Standard & Poor’s, Moody’s, Fitch Ratings and A.M. Best Company in 2009 following our notification to each of the rating agencies that we would no longer be compensating the agencies for their maintenance of such ratings. See Note 12, “Regulatory and Rating Agencies”.

For further discussion on the Perpetual Preferred Shares, see Note 16, “Subsequent Events”.

Dividends on Perpetual Preferred Shares

On April 14, 2008, we announced that, given our current financial condition, our Board in its discretion had decided not to declare a dividend on our Perpetual Preferred Shares for the April 15, 2008 dividend payment date. In addition, we announced that pursuant to the Certificate of Designations for our Perpetual Preferred Shares we may be precluded from declaring and paying dividends on the October 15, 2008 dividend payment date in the event we did not meet certain financial tests under the terms of the Perpetual Preferred Shares required for us to pay such dividends, which tests we subsequently did not meet for such dividend payment date. On July 3, 2008, the Board determined that in light of our financial condition and in accordance with the terms of the then outstanding forbearance agreements with the relevant counterparties to the HSBC II and Clearwater Re collateral finance facilities, we would suspend the cash dividend for the July 15, 2008 payment date. In addition, as previously indicated we were precluded from declaring and paying dividends on the October 15, 2008 dividend payment date

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

9. Non-cumulative Perpetual Preferred Shares (“Perpetual Preferred Shares”) (continued)

as we did not meet the relevant financial tests under the terms of the Perpetual Preferred Shares. In accordance with the relevant financial tests under the terms of the Perpetual Preferred Shares, we were precluded from declaring and paying dividends on the January 15, 2009, April 15, 2009, July 15, 2009, October 15, 2009 and January 15, 2010 dividend payment dates and did not declare and pay a dividend on such dates. Nonpayment of dividends on July 15, 2009 marked the sixth dividend period for which dividends had not been declared and paid. Pursuant to the terms of, and subject to the procedures set forth in, the Certificate of Designations related to the Perpetual Preferred Shares, the holders of the Perpetual Preferred Shares are entitled to elect two directors to our Board in the event dividends on the Perpetual Preferred Shares have not been declared and paid for six or more dividend periods. For further discussion on the non-declaration of Perpetual Preferred Shares dividends, see Note 16, “Subsequent Events”.

In accordance with the Certificate of Designations, future dividends on the Perpetual Preferred Shares generally may be funded only to the extent they are payable out of our distributable profits, and/or the proceeds of a new issue of shares, and/or out of the Share Premium Account (as defined in the Certificate of Designations) related to the Perpetual Preferred Shares. At March 31, 2010, we had a shareholders’ deficit of \$4.4 million and therefore lacked sufficient distributable profits to permit the funding of a dividend.

10. Income Taxes

Income tax benefit for the three months ended March 31, 2010 was \$36.4 million compared to an income tax expense of \$50.9 million for the three months ended March 31, 2009. The income tax benefit for the three months ended March 31, 2010, is principally due to a release of \$35.9 million of accrued tax liabilities. The release was as a result of the reconsideration of our position in respect of an uncertain tax position following a U.S. tax court ruling relating to an unaffiliated third party (Container Corporation v. Commissioner, 134 T.C. 5 (2010)). The net income of our Bermuda and Cayman entities are not subject to income tax. The net income of our U.S. and Irish entities did not generate a current tax expense, other than interest and penalties on accrued tax liabilities, due to the availability of tax losses from prior tax years. The utilization of tax losses results in a reduction in deferred tax assets and a corresponding reduction in the valuation allowance established against those deferred tax assets.

At March 31, 2010, we had total unrecognized tax benefits (excluding interest and penalties) of \$114.6 million, the recognition of which would result in a \$2.9 million benefit at the effective tax rate. At December 31, 2009, we had total unrecognized tax benefits (excluding interest and penalties) of \$132.2 million, the recognition of which would result in a \$20.6 million benefit at the effective tax rate.

Our deferred tax assets are principally supported by the reversal of deferred tax liabilities. We have maintained a full valuation allowance against any remaining net deferred tax assets, given our inability to rely on future taxable income tax projections.

At March 31, 2010, our deferred tax liabilities include \$48.5 million of deferred tax liabilities that reverse after the expiration of net operating losses in applicable jurisdictions and therefore cannot support deferred tax assets. At December 31, 2009, the corresponding amount of deferred tax liabilities was \$49.8 million.

We file our tax returns as prescribed by the tax laws of the jurisdictions in which we operate. As of March 31, 2010, we remained subject to examination in the following major tax jurisdictions for the years indicated below:

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

10. Income Taxes (continued)

<u>Major Tax Jurisdictions</u>	<u>Open Years</u>
U.S.	
Life Group	2006 through 2010
Non-Life Group	2006 through 2010
Ireland	2005 through 2010

11. Earnings per Ordinary Share

Basic earnings per share is computed based on the weighted average number of ordinary shares outstanding and assumes an allocation of net income to Convertible Cumulative Participating Preferred Shares for the period or portion of the period that this security is outstanding. Losses are not allocated to Convertible Cumulative Participating Preferred Shares. Under the provisions of FASB ASC Topic 260, Earnings per Share (“FASB ASC 260”), formerly SFAS No. 128, basic earnings per share are computed by dividing the net loss attributable to ordinary shareholders by the weighted average number of shares of our ordinary shares outstanding for the period. Diluted earnings per share is calculated based on the weighted average number of ordinary shares outstanding plus the diluted effect of potential ordinary shares in accordance with the if-converted method. In accordance with FASB ASC 260, the exercise of options and warrants or conversion of convertible securities is not assumed unless it would reduce earnings per share or increase loss per share.

The following table sets forth the computation of basic and diluted earnings per ordinary share under the two-class method and the if-converted method, respectively, as required under FASB ASC 260 which incorporates EITF No. 03-06, “Participating Securities and the Two-Class Method under FASB Statement No. 128”.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

11. Earnings per Ordinary Share (continued)

(U.S. dollars in thousands, except share data)	Three months ended	
	March 31, 2010	March 31, 2009 (Restated)
Basic income attributable to ordinary shareholders		
Numerator:		
Net income attributable to ordinary shareholders.....	\$ 99,549	\$ 1,661,582
Amounts allocable to convertible cumulative participating preferred shares	(1,435)	(23,948)
Numerator for basic income per ordinary share ..	\$ 98,114	\$ 1,637,634
Denominator:		
Denominator for basic income per ordinary share - weighted average number of ordinary shares	68,383,370	68,383,370
Basic income from continuing operations attributable to ordinary shareholders	\$ 1.43	\$ 23.95
Diluted income attributable to ordinary shareholders		
Numerator:		
Net income attributable to ordinary shareholders.....	\$ 99,549	\$ 1,661,582
Denominator:		
Denominator for basic income per ordinary share - weighted average number of ordinary shares	68,383,370	68,383,370
Effect of dilutive securities*.....	150,000,000	150,000,000
Denominator for diluted income per ordinary share	218,383,370	218,383,370
Diluted income from continuing operations attributable to ordinary shareholders	\$ 0.46	\$ 7.61

* In accordance with FASB ASC 260, exercise of options and warrants or conversion of convertible securities is not assumed if the result would be anti-dilutive, such as when a loss from continuing operations is reported. Due to the anti-dilutive effect on earnings per share ("EPS"), our stock options (which are convertible into 4,481,592 ordinary shares) potentially could dilute EPS in the future.

12. Regulatory and Rating Agencies

Order of Supervision

In connection with its receipt of the Permitted Practice described above in Note 1, SRUS consented to the issuance by the Department on January 5, 2009 of an Order of Supervision, in accordance with 18 Del. C. §5942. The Order of Supervision subsequently was extended and amended on April 3, 2009 with the issuance of the Amended Order. Pursuant to the Amended Order, SRUS generally must receive prior written consent from the Department in order to engage in any transaction outside of the ordinary course of business; make certain payments

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

12. Regulatory and Rating Agencies (continued)

or incur certain debts, obligations or liabilities in any transaction of \$1 million or greater (provided that this limitation does not apply to the payment of claims, premiums and other third party reinsurance settlements, in each case of less than \$10 million per payment); engage in new business; lend any of its funds; invest any of its funds in a manner that deviates from the plan filed with the Department; commute, novate, amend or otherwise change any existing reinsurance contract or treaty; or engage in any transaction with any related party.

Delaware Emergency Regulations

On February 17, 2009, citing, among other things, then current economic conditions and the uncertainty of the conditions that lay ahead, the Commissioner issued an emergency order amending Delaware Insurance Regulation §1215 relating to Recognition of Preferred Mortality Tables for use in Determining Minimum Reserve Liabilities (the “Preferred Mortality Table Emergency Regulation”) and an emergency order amending Delaware Insurance Regulation §1212 relating to Valuation of Life Insurance Policies (the “X-Factor Emergency Regulation”, and together with the Preferred Mortality Table Regulation, the “Emergency Regulations”). Generally, the Preferred Mortality Table Emergency Regulation allows, upon receipt of the Commissioner’s approval, use of the 2001 CSO Preferred Class Structure Mortality Table as the minimum valuation standard for policies issued after January 1, 2004. In connection with the Preferred Mortality Table Emergency Regulation, the Company sought and, on February 26, 2009, obtained the Department’s approval for use of the 2001 CSO Preferred Class Structure Mortality Table in accordance with such Emergency Regulation. The X-Factor Emergency Regulation relaxes existing constraints related to the X-factor assumptions used in the calculation of statutory reserves.

The Emergency Regulations by their terms became effective for valuations on and after December 31, 2008. The Emergency Regulations were adopted into law pursuant to the Delaware Administrative Procedures Act on September 1, 2009. Similar regulations were adopted by the NAIC during the 2009 Fall National Meeting and as such, the Emergency Regulations no longer are considered a prescribed practice.

Ratings

Our financial strength ratings and the financial strength ratings of our subsidiaries have been lowered on several occasions since 2007. Ratings at such levels also previously triggered the vesting of contractual recapture rights in respect of certain of our reinsurance business and resulted in the increase to a maximum “stepped up” rate of certain guarantor fees in respect of the securitization structures used to finance the Regulation XXX statutory reserve requirements associated with business ceded by SRUS to each of Orkney Re and Orkney Re II. In light of the foregoing and our pursuit of a run-off strategy for our remaining business, among other factors, we determined that we no longer intended to utilize capital for the payment of ratings fees to maintain the financial strength and other ratings for us and our operating subsidiaries at such levels. Accordingly, we notified each of the rating agencies in June 2009 that we no longer would compensate the agencies for their maintenance of such ratings.

Following this communication, on June 4, 2009, Standard & Poor’s Corporation (“S&P”), affirmed and then subsequently withdrew the “CC” counterparty credit rating of SRGL, the “C” rating of SRGL’s Perpetual Preferred Shares, and the “CCC-” counterparty credit and financial strength ratings of SALIC. At the same time, S&P affirmed and then withdrew the “R” counterparty credit and financial strength ratings of SRUS, the “CCC” counterparty credit and financial strength ratings of Scottish Re Life Corporation and the “CCC-” senior secured rating of the Pass-Through Certificates.

On June 12, 2009, A.M. Best Company Inc. (“A.M. Best”) affirmed and then withdrew the financial strength ratings and issuer credit ratings of SALIC, Scottish Re Life Corporation and Orkney Re. At the same time, A.M. Best affirmed and then withdrew our issuer credit rating and the rating of our Perpetual Preferred Shares, as well as our indicative ratings of senior unsecured debt, subordinated debt and preferred stock. SRUS’ financial strength rating of “E” (Under Regulatory Supervision) and issuer credit rating of “rs” was unchanged.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

12. Regulatory and Rating Agencies (continued)

On June 22, 2009, Fitch Ratings (“Fitch”) downgraded the issuer default rating of SRGL to “CC” from “CCC” and then withdrew its rating of SRGL. At the same time, Fitch affirmed and then withdrew the insurer financial strength rating of SRUS. Fitch also has withdrawn the insurer financial strength rating of SALIC and the rating of the Pass-Through Certificates and the Perpetual Preferred Shares. As such, Fitch has withdrawn all of our ratings and no longer will provide analytical coverage in respect of us and our affiliates.

On August 18, 2009, Moody’s downgraded the insurance financial strength ratings of SALIC to “Ca” from “C” and SRUS to “Ba3” from “Ba1”, before withdrawing both ratings. At the same time, Moody’s downgraded to “Ca” from “C” and then withdrew the senior secured rating of the Pass-Through Certificates and our preferred stock rating.

13. Sale of a Block of Life Reinsurance North America Business

We engaged in 2008 in a process to sell our entire Life Reinsurance North America Segment. In October 2008, the process led to exclusive negotiations with a prospective buyer; however, a satisfactory transaction for the sale of the entire Life Reinsurance North America Segment could not be reached, primarily as a result of the historic disruption in the financial markets. Thereafter, in an effort to find ways to address our capital, liquidity and collateral needs and the concerns of regulators, we pursued the sale of a specific block of individual life reinsurance in our North American business. These efforts culminated in the announcement on February 20, 2009 that we had closed the transactions contemplated by the Master Asset Purchase Agreement (the “Purchase Agreement”), by and among the Company, SHI, SRUS, Scottish Re Life (Bermuda) Limited (“SRLB”) and Scottish Re (Dublin) Limited (“SRD”) (collectively, the “Sellers”) with Hannover Re to sell a block of individual life reinsurance business acquired in 2004 from the ING Companies, which block consisted primarily of term life reinsurance universal life with secondary guarantees, and yearly renewable term business (the “Acquired Business”).

Pursuant to the Purchase Agreement, Hannover Re purchased the Acquired Business, which was acquired in 2004 by us from the ING Companies. The Acquired Business consists primarily of term life reinsurance, universal life with secondary guarantees, and yearly renewable term business. When we originally purchased the Acquired Business in 2004, the ING Companies reinsured their individual life reinsurance business to us on a 100% indemnity reinsurance basis. A large portion of such business included guaranteed level premium term life insurance that was subject to the Regulation XXX reserve requirements and universal life policies with secondary guarantees subject to the “Regulation AXXX” reserve requirements. Under our 2004 agreement with the ING Companies, the ING Companies were obligated to maintain collateral for the Regulation XXX and AXXX reserve requirements of the Acquired Business for the duration of such requirements, and financial incentives were provided to encourage us to replace this financing with alternative third party financing. The Acquired Business does not include business ceded by SRUS to Ballantyne Re as the reinsurance transaction with this special purpose reinsurance vehicle was novated and assigned from SRUS to SLD effective October 1, 2008. However, the Acquired Business does include the business recaptured from Ballantyne Re in connection with a series of recaptures during 2008 in which SRUS recaptured business from Ballantyne Re, which business then was recaptured by SLD which in turn ceded the recaptured business to SLDI who ceded it to SRLB (the foregoing recaptures, collectively, the “Ballantyne Recaptures”), nor does it include the business recaptured in connection with the unwind of our HSBC II collateral finance facility (together with the Ballantyne Recaptures, the “ING Financings”). In connection with each of the ING Financings, SLD ceded the applicable recaptured business to SLDI, which ceded the recaptured business to SRLB. SLDI agreed to provide, or cause the provision of, one or more LOCs in order to provide SLD with statutory financial statement credit for the excess reserves associated with the recaptured business in respect of the ING Financings. As partial consideration for each of the ING Financings, the Company agreed to bear the costs of the LOCs by paying SLD a facility fee based on the face amount of such LOCs outstanding. The cost of these LOCs was consistent with the pricing schedules from our 2004 acquisition agreement with ING Companies, as such schedule was amended on May 7, 2007. Upon closing the transactions contemplated by the Purchase Agreement, Hannover Re assumed the business related to the ING Financings as part of the Acquired Business, as well as the obligation to pay the existing and any future increases in the related LOC fees.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

13. Sale of a Block of Life Reinsurance North America Business (continued)

In connection with the Purchase Agreement, the ING Companies and certain of the Sellers entered into recapture agreements (and, in specific instances, novations to Hannover Re of certain existing reinsurance agreements) with respect to the Acquired Business, and the ING Companies and Hannover Re subsequently entered into new reinsurance agreements with respect to the Acquired Business immediately thereafter. These recapture and reinsurance transactions and the novations had an effective date of January 1, 2009. SRUS and SRLB remain responsible for liabilities and obligations to SLD and SLDI under their reinsurance agreements with these parties to the extent attributable to periods prior to January 1, 2009.

The Purchase Agreement also related to the purchase and sale of certain assets used by the Sellers in connection with their administration of the Acquired Business (the "Transferred Assets") and the transfer of certain employees from the Sellers to Hannover Re in connection therewith. Pursuant to the Purchase Agreement, the remaining lease on SRUS' Denver office location was assigned to Hannover Re as was a portion of SRUS' Charlotte office location. In addition, Hannover Re entered into an administrative services agreement with SRUS pursuant to which Hannover Re administers the accepted and ceded mortality business retained by SRUS and its affiliates. Similarly, Hannover Re entered into an administrative services agreement with the ING Companies pursuant to which Hannover Re administers the Acquired Business and provides certain other administrative services to the ING Companies.

In accordance with the Purchase Agreement, payments were made as follows: (i) the Sellers made recapture payments to the ING Companies in an aggregate amount equal to \$1,325 million (adjusted for interim period earnings from January 1, 2009 to the date of closing), (ii) the ING Companies made corresponding initial premium payments to Hannover Re, and (iii) Hannover Re made a payment to the Sellers in respect of the Transferred Assets in an amount equal to \$18 million.

Following the transfer of assets with respect to the recapture payments noted above, we were released of all associated policyholder liabilities on the sale of the Acquired Business as of the effective date of January 1, 2009. The release of such liabilities resulted in a pre-tax gain of \$703.6 million, after transaction expenses and related costs. This gain was also subject to certain contingencies, which were all satisfied as at December 31, 2009. Of the \$703.6 million gain, \$642.4 million, \$59.8 million, \$1.0 million, and \$0.4 million were recognized in the first, second, third and fourth quarters of 2009, respectively. This total gain is summarized as follows:

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

13. Sale of a Block of Life Reinsurance North America Business (continued)

(U.S. dollars in millions)	<u>Balance Sheet</u>	<u>Consolidated Statement of Income</u>
Transfer of investments	\$ (1,468.7)	
Release of reserve for future policy benefits	1,902.9	
Decrease in accounts payable and other liabilities.....	1.7	
Decrease in reinsurance balances and risk fees receivable	(6.3)	
Decrease in reinsurance balances payable	4.7	
Increase in other assets	18.7	
Decrease in claims and other policy benefits	\$ 453.0	\$ 453.0
Decrease in accounts payable and other liabilities.....	275.5	
Change in value of embedded derivatives.....	\$ 275.5	275.5
Release in deferred acquisition costs	(24.9)	
Acquisition costs and other insurance expenses, net.....	\$ (24.9)	(24.9)
Total pre-tax gain as at December 31, 2009.....		\$ 703.6

In connection with the Purchase Agreement, the Company, Hannover Re and the ING Companies agreed to use commercially reasonable efforts to transfer to Hannover Re certain retrocession agreements under which we and/or the ING Companies ceded to third parties certain risks related to the Acquired Business. If a certain amount of such third party retrocessionaires did not consent to such transfers prior to April 30, 2009, we were required under the Purchase Agreement to deposit into escrow with Hannover Re by May 14, 2009, a pro-rata amount related to such retrocession agreements for which consent had not been obtained as of that date. Pursuant to the Purchase Agreement, in the event none of the retrocessionaires consented to transfer their agreements, the maximum potential escrow funding amount was \$136.3 million. In the event one or more retrocessionaire consents had not been obtained by December 31, 2009, the related escrow funds would be released to Hannover Re. As of the escrow funding requirement date of May 14, 2009, the balance was \$1.9 million. The required escrow balance was reduced to \$0 million and all of the funds were released back to us by the end of 2009.

This transaction resulted in a \$49.8 million income tax expense in the first quarter of 2009, due to an increase in our valuation allowance. The increased valuation allowance was because the remaining deferred tax liabilities did not support the full recoverability of our deferred tax assets, as discussed earlier in Note 2, "Basis of Presentation-Restatement of Prior Financial Statements".

14. Collateral Finance Facilities

Ballantyne Re

De-consolidation of Ballantyne Re

Ballantyne Re is a special purpose reinsurance vehicle incorporated under the laws of Ireland. In May 2006, Ballantyne Re issued in a private offering \$1.74 billion of debt to third party investors, \$178 million of Class C Notes and \$181.2 million in preference shares to SALIC and \$500,000 in Class D Notes to SRGL.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

Initially, in accordance with FASB ASC 810-10, Ballantyne Re was considered to be a variable interest entity and we were considered to hold the primary beneficial interest following a quantitative analysis whereby it was determined that we would absorb a majority of the expected losses. As a result, Ballantyne Re was consolidated in our financial statements through December 31, 2008.

Effective January 1, 2009, Ballantyne Re no longer is consolidated within the financial statements of SRGL. Pursuant to the Purchase Agreement (as defined herein) for the disposal of the Acquired Business, Hannover Re explicitly agreed to assume the mortality risk for all recaptures of business from Ballantyne Re. Our disposal of the variable interest to absorb mortality risk recaptured from Ballantyne Re under the reinsurance agreement constituted a reconsideration event related to the consolidation of Ballantyne Re under FASB ASC 810-10, Consolidation - Overall ("FASB ASC 810-10"). We subsequently completed a primary beneficiary analysis and concluded that we no longer are the primary beneficiary of Ballantyne Re as defined within FASB ASC 810-10 and, as a result, no longer are consolidating Ballantyne Re into the financial statements of SRGL. The de-consolidation of Ballantyne Re reduced our consolidated total assets and liabilities by approximately \$885 million and \$2,035 million, respectively, resulting in a one-time non-cash de-consolidation gain of \$1,150 million which we recognized in the first quarter of 2009. This gain had no impact on our liquidity position.

As of March 31, 2010, we had no remaining direct loss exposure related to Ballantyne Re since our interests in the Ballantyne Re Class D Notes and Preferred Shares are valued at \$0 and are classified as trading securities on the Consolidated Balance Sheet. The Class C Notes were contractually written-off during the fourth quarter of 2008.

SRUS remains liable for breaches of its representations, warranties, covenants and other obligations that relate to periods before the assignment and novation to SLD of the reinsurance agreement with Ballantyne Re. In addition, the Company and SRUS remain responsible for certain ongoing covenants and indemnities made for the benefit of Ballantyne Re and the financial guarantors of certain of the notes issued by Ballantyne Re.

Orkney I

On February 11, 2005, Orkney Holdings, LLC, a Delaware limited liability company ("Orkney I"), issued and sold in a private offering an aggregate of \$850 million Series A Floating Rate Insured Notes due February 11, 2035 (the "Orkney Notes"). Orkney I was organized for the limited purpose of issuing the Orkney Notes and holding the stock of Orkney Re, Inc., originally a South Carolina special purpose financial captive insurance company, now a Delaware special purpose captive insurance company ("Orkney Re"). SRUS holds all of the limited liability company interest in Orkney I, and has contributed capital to Orkney I in the amount of \$268.5 million. Proceeds from this offering were used to fund the Valuation of Life Insurance Policies Model Regulation ("Regulation XXX") reserve requirements for a defined block of level premium term life insurance policies issued by direct ceding companies between January 1, 2000 and December 31, 2003, and reinsured by SRUS to Orkney Re. Proceeds from the Orkney Notes have been deposited into a series of accounts that collateralize the notes and the reserve obligations of SRUS.

The holders of the Orkney Notes have no recourse against us or any of our subsidiaries, other than Orkney I. The timely payment of interest and ultimate payment of principal for the Orkney Notes are guaranteed by MBIA Insurance Corporation ("MBIA"). We are not required to provide any additional financial support to Orkney I.

Interest on the principal amount of the Orkney Notes is payable quarterly at a rate equivalent to three-month LIBOR plus 0.53%. At March 31, 2010, the interest rate was 0.78% (compared to 0.80% at December 31, 2009). Any payment of principal, including by redemption, or interest on the Orkney Notes is sourced from dividends from Orkney Re, and the balances available in a series of trust accounts generally excluding amounts on deposit in a reinsurance trust account supporting the associated reserve requirements of SRUS. Dividends only may be made after filing with the Commissioner in accordance with the terms of Orkney Re's licensing order and in accordance with applicable law. The Orkney Notes also contain a customary limitation on lien provisions and customary events

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

of default provisions, which, if breached, could result in the accelerated maturity of the Orkney Notes. Orkney I has the option to redeem all or a portion of the Orkney Notes prior to and on or after February 11, 2010, subject to certain call premiums.

In accordance with FASB ASC 810-10, Orkney I is considered to be a variable interest entity and we are considered to hold the primary beneficial interest as we cede all the business assumed by Orkney I and following an analysis whereby it was determined that we would absorb a majority of the expected losses. As a result, Orkney I is consolidated in our financial statements. The assets of Orkney I have been recorded as fixed maturity investments and cash and cash equivalents. Our Consolidated Statements of Income shows the investment return of Orkney I as investment income and the cost of the facility is reflected in collateral finance facilities expense. Funds in the securitization structure are used for the sole purpose of the securitization structure and hence are not available for general corporate purposes.

To the extent we experience fair value declines in our investment portfolio, we may need to recapture a pro-rata portion of the underlying business in Orkney I and find alternative collateral support for the recaptured business. No assurances can be given that we would be successful in securing alternative collateral support.

Related Party Acquisition of Orkney Notes

We have been informed by Cerberus that an affiliate of Cerberus acquired from one or more unaffiliated third parties \$700 million in aggregate principal amount of the Orkney Notes in 2009. None of the Company, Orkney I, Orkney Re or any of our other subsidiaries were a party to this purchase. No terms of the Orkney Notes or any of the underlying transaction documents were changed as a result of this purchase.

Orkney Re, Inc. Notices of Default

On February 9, 2009, MBIA served Orkney Re, Orkney I and SRUS with notices of default under each of the Orkney I indenture and the insurance and indemnity agreement (the "Orkney Insurance Agreement"), alleging failure by the parties to provide certain required financial statements and improper withdrawals by the parties from Orkney I tax accounts. SRUS cured such alleged defaults within the cure periods set forth in the indenture and the Orkney Insurance Agreement.

On September 21, 2009, MBIA served Orkney Re, Orkney I and SRUS with a notice of default under the restructuring agreement executed at the time of Orkney Re's redomestication from South Carolina to Delaware, alleging failure by the parties to provide MBIA with an actuarial review in accordance with the requirements set forth in the restructuring agreement. SRUS, Orkney I and Orkney Re disagree with such contention. However, in the event such alleged failure to provide an actuarial review ultimately is determined to be a default, and because it was not cured within five (5) business days of the September 21, 2009 notice, then such default would constitute an event of default under the Orkney Insurance Agreement, which in turn would provide certain enhanced contractual rights to MBIA under the Orkney Insurance Agreement, including the right to recover from Orkney I any actual losses, costs and expenses incurred by MBIA in connection with the event of default and the receipt of certain penalty fees. Pursuant to the terms of a letter agreement put in place between SRUS and MBIA at the time of the Orkney I transaction, SRUS would also be obligated to pay on behalf of Orkney I certain of the foregoing fees and expenses to the extent due from Orkney I. As of the date hereof, MBIA, Orkney Re, Orkney I and SRUS are engaged in negotiations related to such actuarial review and alleged default.

On February 22, 2010, MBIA served Orkney Re, Orkney I and SRUS with notices of default under each of the Orkney I indenture and the Orkney Insurance Agreement, alleging failure by the parties to provide certain required financial statements and other documents required to be delivered under these transaction documents. SRUS

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

subsequently caused such documents to be delivered within the applicable cure periods and, as of the date hereof, there is no event of default resulting from such notices of default.

Orkney Re II

On December 21, 2005, Orkney Re II plc, a special purpose vehicle incorporated under the laws of Ireland (“Orkney Re II”), whose issued ordinary shares are held by a share trustee and its nominees in trust for charitable purposes, issued in a private offering \$450 million of debt to external investors. The debt consisted of \$382.5 million of Series A-1 Floating Rate Guaranteed Notes (the “Series A-1 Notes”), \$42.5 million of Series A-2 Floating Rate Notes (the “Series A-2 Notes”), and \$25 million of Series B Floating Rate Notes (the “Series B Notes”), all due December 31, 2035 (collectively, the “Orkney Re II Notes”). The Orkney Re II Notes are listed on the Irish Stock Exchange. Proceeds from this offering were used to fund the Regulation XXX reserve requirements for a defined block of level premium term life insurance policies issued between January 1, 2004 and December 31, 2004 reinsured by SRUS to Orkney Re II. Proceeds from the Orkney Re II Notes have been deposited into a series of accounts that collateralize the notes and the reserve obligations of SRUS.

The holders of the Orkney Re II Notes have no recourse against us or any of our subsidiaries. Assured Guaranty (UK) Ltd. (“Assured”) has guaranteed the timely payment of the scheduled interest payments and the principal on the maturity date of the Series A-1 Notes. We are not required to provide any additional financial support to Orkney Re II.

The debt issued to SALIC consisted of \$30 million of Series C Floating Rate Notes (“Series C Notes”) due December 21, 2036, and \$5 million of Series B Notes. These Series C Notes accrue interest only until the Orkney Re II Notes are fully repaid. SRGL owns \$0.5 million Series D Convertible Notes due December 21, 2036, and 76,190,000 Preference Shares of \$1.00 each in capital.

Interest on the principal amount of the Orkney Re II Notes is payable quarterly at a rate equivalent to three-month LIBOR plus 0.425% for the Series A-1 Notes, three-month LIBOR plus 0.73% for the Series A-2 Notes, and three-month LIBOR plus 3.0% for the Series B Notes. At March 31, 2010, the interest rate on the Series A-1 Notes was 0.68% (compared to 0.70% at December 31, 2009), Series A-2 Notes was 0.98% (compared to 1.00% at December 31, 2009), and Series B Notes was 3.25% (compared to 3.27% at December 31, 2009). The Orkney Re II Notes also contain customary limitation on lien provisions and customary events of default provisions, which, if breached, could result in the accelerated maturity of the Orkney Re II Notes. Orkney Re II has the option to redeem all or a portion of the Orkney Re II Notes, subject to certain call premiums and available (unencumbered) funds.

In accordance with FASB ASC 810-10, Orkney Re II is considered to be a variable interest entity and we are considered to hold the primary beneficial interest as we cede all the business assumed by Orkney Re II and following an analysis whereby it was determined that we would absorb a majority of the expected losses. As a result, Orkney Re II is consolidated in our financial statements. The assets of Orkney Re II have been recorded as fixed maturity investments and cash and cash equivalents. Our Consolidated Statements of Income shows the investment return of Orkney Re II as investment income and the cost of the securitization structure is reflected in collateral finance facilities expense. Funds in the securitizations are primarily used for the purpose of the securitizations and hence are not available for general corporate purposes.

To the extent we experience fair value declines in our investment portfolio, we may need to recapture a pro-rata portion of the underlying business in Orkney Re II and find alternative collateral support for the recaptured business. No assurances can be given that we would be successful in securing alternative collateral support.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

Orkney Re II Event of Default, Acceleration and Foreclosure

On the scheduled interest payment date on May 11, 2009, Orkney Re II was unable to make scheduled interest payments on the Series A-1 Notes. Failure to make such payments in full when due constitutes an event of default under the Orkney Re II indenture (“Orkney EOD”). Assured, in its capacity as financial guarantor of the Series A-1 Notes, made guarantee payments on the Series A-1 Notes in the amount of \$1.2 million. As a result of the Orkney EOD, Assured obtained, and will continue to have, certain enhanced contractual rights under the transaction documents and additional fees will be accrued for the guarantee coverage.

Among Assured’s enhanced contractual rights are (a) the right to instruct the trustee to declare the principal of and the interest on all the Notes to be due and payable immediately and (b) the right to foreclose upon the Collateral (as defined in the related indenture). On June 1, 2009, Assured instructed the trustee to accelerate the Notes and the trustee delivered a notice of acceleration to Orkney Re II on June 18, 2009. On June 19, 2009, Assured notified Orkney Re II and the trustee that it was electing to foreclose upon the Collateral.

Following these actions, on June 26, 2009, SRUS exercised its contractual right under its agreements with Orkney Re II to withdraw all assets from the reserve credit trust established by Orkney Re II for the benefit of SRUS. The withdrawn assets were deposited into SRUS segregated accounts pursuant to the terms of the reinsurance agreement between SRUS and Orkney Re II (the “Orkney Re II Reinsurance Agreement”) where they are held in order to provide reserve credit to SRUS for the reinsurance liabilities that continue to be ceded to Orkney Re II and for certain other permissible uses under the Orkney Re II Reinsurance Agreement. The transfer of assets had no impact on our consolidated financial statements.

On the scheduled interest payment dates of August 11, 2009, November 12, 2009, and February 11, 2010, Orkney Re II was unable to make scheduled interest payments on the Series A-1 Notes. Assured made guarantee payments on the Series A-1 Notes in the amount of \$1.4 million, \$0.9 million and \$0.7 million, for August 11, 2009 and November 12, 2009 and February 11, 2010, respectively.

For further discussion on the Orkney Re II scheduled interest payments on the Series A-1 Notes, see Note 16, “Subsequent Events”.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

Consolidated collateral finance facilities and securitization structures

The following table reflects the significant balances attributable to the collateral finance facilities and securitization structures providing collateral support to us as at and for the three months ended March 31, 2010:

(U.S. dollars in millions)	Orkney I	Orkney Re II	Total
Assets			
Fixed maturity investments	\$ 1,082.7	\$ -	\$ 1,082.7
Funds withheld at interest	-	311.6	311.6
Cash and cash equivalents	58.6	1.7	60.3
All other assets	100.5	60.3	160.8
Total assets	<u>\$ 1,241.8</u>	<u>\$ 373.6</u>	<u>\$ 1,615.4</u>
Liabilities			
Reserves for future policy benefits	\$ 310.4	\$ 120.3	\$ 430.7
Collateral finance facilities	850.0	450.0	1,300.0
All other liabilities	4.7	7.8	12.5
Total liabilities	<u>\$ 1,165.1</u>	<u>\$ 578.1</u>	<u>\$ 1,743.2</u>
Revenues			
Premiums earned, net	\$ 15.8	\$ 13.8	\$ 29.6
Investment income, net	5.9	5.1	11.0
Net realized and unrealized gains	24.7	0.1	24.8
Net embedded derivative adjustments.....	-	1.0	1.0
Total revenues	<u>\$ 46.4</u>	<u>\$ 20.0</u>	<u>\$ 66.4</u>
Expenses			
Claims and other policy benefits	\$ 14.9	\$ 10.1	\$ 25.0
Acquisition costs and other insurance expenses, net	3.2	3.3	6.5
Operating expenses ...	0.1	0.2	0.3
Collateral finance facilities expense	3.6	2.2	5.8
Total benefits and expenses	<u>\$ 21.8</u>	<u>\$ 15.8</u>	<u>\$ 37.6</u>

The assets listed in the foregoing table are subject to a variety of restrictions on their use, as set forth in, and governed by, the transaction documents for the applicable collateral finance facilities and securitization structures to which they relate. In addition, of the amounts set forth in total assets above, \$328.2 million and \$95.5 million, for Orkney I and Orkney Re II, respectively, have been excluded from the total investments of consolidated VIE amount on the Consolidated Balance Sheet of SRGL as at March, 31, 2010. Such excluded amounts represent the assets projected to support the expected reinsurance liabilities of \$310.4 million and \$120.3 million associated, with business ceded to Orkney I and Orkney Re II, respectively. No assurances can be given that the expected reinsurance liabilities will not increase in the event of adverse mortality experience in our reinsurance agreements. Under certain circumstances, such adverse mortality experience may in future periods increase the amount of assets excluded from the total investments of consolidated VIE on the Consolidated Balance Sheet of

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

14. Collateral Finance Facilities (continued)

SRGL. These reinsurance liabilities of Orkney I and Orkney Re II are eliminated from the Consolidated Balance Sheet because they represent inter-company transactions.

The following table reflects the significant balances attributable to the collateral finance facilities and securitization structures providing collateral support to us as at the year ended December 31, 2009:

(U.S. dollars in millions)	Orkney I	Orkney Re II	Total
Assets			
Fixed maturity investments	\$ 1,001.1	\$ -	\$ 1,001.1
Funds withheld at interest	-	303.1	303.1
Cash and cash equivalents	113.1	1.9	115.0
All other assets	106.4	60.1	166.5
Total assets	<u>\$ 1,220.6</u>	<u>\$ 365.1</u>	<u>\$ 1,585.7</u>
Liabilities			
Reserves for future policy benefits	\$ 313.0	\$ 118.0	\$ 431.0
Collateral finance facilities	850.0	450.0	1,300.0
All other liabilities	5.8	10.8	16.6
Total liabilities	<u>\$ 1,168.8</u>	<u>\$ 578.8</u>	<u>\$ 1,747.6</u>

The following table reflects the significant income statement balances attributable to the collateral finance facilities and securitization structures providing collateral support to us for the three months ended March 31, 2009:

(U.S. dollars in millions)	Orkney I	Orkney Re II	Total
Revenues			
Premiums earned, net	\$ 16.8	\$ 14.9	\$ 31.7
Investment income, net	6.5	2.9	9.4
Net realized and unrealized gains (losses)	(30.7)	(27.9)	(58.6)
Total revenues	<u>\$ (7.4)</u>	<u>\$ (10.1)</u>	<u>\$ (17.5)</u>
Expenses			
Claims and other policy benefits	\$ 17.1	\$ 7.9	\$ 25.0
Acquisition costs and other insurance expenses, net	3.4	3.4	6.8
Operating expenses ...	0.3	0.2	0.5
Collateral finance facilities expense	6.6	3.7	10.3
Total benefits and expenses	<u>\$ 27.4</u>	<u>\$ 15.2</u>	<u>\$ 42.6</u>

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

15. Commitments and Contingencies

Indemnification

In connection with an examination of the statutory accounting books of certain of our operating insurance subsidiaries, and specifically, the purchase accounting entries made in connection with the 2004 acquisition of the ING business, we determined that certain intercompany receivables and intercompany claims were not reflected in the statutory financial statements of SRUS and SRD in accordance with applicable statutory accounting practices. Management determined that as a result of these errors the statutory surplus for SRD was overstated on a cumulative basis at year end 2004, 2005 and 2006, resulting in a restated statutory surplus at year end 2006 of approximately \$285 million after giving effect to these corrections.

In addition, management determined that the statutory surplus for SRUS was understated on a cumulative basis at year end 2005 and 2006, resulting in a restated statutory surplus at year end 2006 of approximately \$344 million after giving effect to these corrections.

The restated statutory surplus of each of SRUS and SRD met the applicable minimum statutory surplus requirements at December 31, 2006. None of these corrections impact our historical consolidated financial statements under U.S. GAAP.

Pursuant to the Agreement with MassMutual Capital and Cerberus, we made certain representations and warranties regarding the statutory financial statements of each of our insurance subsidiaries, including SRD and SRUS, for the years ended 2003, 2004 and 2005 and, with respect to SRUS but not SRD, the first three quarters of 2006, including that these statements were prepared in conformity with applicable statutory accounting practices and fairly present in accordance with such practices, in all material respects, the statutory financial condition of the relevant insurance subsidiary at the respective dates. In light of our discovery of the corrections described above, we notified MassMutual Capital and Cerberus, as required by the terms of the Agreement, of the overstatement of statutory surplus in SRD at year end 2004 and the understatement of such statutory surplus at year end 2005 resulting in a cumulative overstatement for the two year period at year end 2005 of approximately \$70 million on an after-tax basis, and the understatement of statutory surplus in SRUS for the year ended 2005 of approximately \$14.5 million on an after-tax basis. On November 16, 2007, MassMutual Capital and Cerberus responded by notifying us of their concern that the corrections described above may constitute breaches of certain of the representations and warranties made by us in the Agreement. Under the Agreement, in the event of a claim for losses resulting from a diminution in value, such losses would be determined by an independent investment banking firm of national reputation, agreed upon by us and MassMutual Capital and Cerberus, based on changes in the valuation of SRGL using the assumptions and models used by MassMutual Capital and Cerberus at the time of their decision to invest in us. Furthermore, should any claim for indemnification be made by MassMutual Capital and Cerberus, the Agreement provides that any decision regarding defending or settling such claim will be taken by a committee of independent directors of our Board of Directors. In their November 16, 2007 correspondence, MassMutual Capital and Cerberus requested that we convene a committee of independent directors. No action has since been taken by us or the Investors in respect of this claim. At this time, we do not know what the amount of any indemnifiable losses would be, if any, or what potential defenses or other limitations on indemnification may be available to us under those circumstances. The Agreement provides that any indemnification claim would be satisfied by adjusting the conversion amount at which the Convertible Cumulative Participating Preferred Shares issued to MassMutual Capital and Cerberus are convertible into our Ordinary Shares.

16. Subsequent Events

The subsequent events disclosed in these notes to the consolidated financials have been evaluated by management up to and including the filing of the financial statements on June 7, 2010.

SCOTTISH RE GROUP LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

March 31, 2010

16. Subsequent Events (continued)

Orkney Re II

On the scheduled interest payment date of May 11, 2010, Orkney Re II was unable to make scheduled interest payments on the Series A-1 Notes. As a result, Assured made guarantee payments on the Series A-1 Notes in the amount of \$0.6 million.

Deferral of Interest Payments on Floating Rate Capital Securities and Trust Preferred Securities

Subsequent to March 31, 2010, we have accrued and deferred payment of an additional \$0.4 million of interest on our floating rate capital securities and trust preferred securities. As of June 7, 2010, we have accrued and deferred payment on a total of \$7.8 million of interest.

Non-declaration of Perpetual Preferred Shares Dividends

In accordance with the relevant financial tests under the terms of the Perpetual Preferred Shares, we were precluded from declaring and paying dividends on the April 15, 2010 dividend payment date. As discussed in Note 9, "Non-cumulative Perpetual Preferred Shares", the holders of the Perpetual Preferred Shares continue to be entitled to elect two directors of SRGL's Board as a result of dividends on the Perpetual Preferred Shares having not been declared and paid for six or more dividend periods. This right has not been exercised to date.

Perpetual Preferred Shares

On May 7, 2010, SRGL launched a cash tender offer to purchase any and all of the outstanding Perpetual Preferred Shares at a purchase price of \$5.00 per share (as such tender offer may be amended or supplemented from time to time, the "Perpetual Preferred Share Offer"). The Perpetual Preferred Share Offer, which originally was to expire at 12:00 midnight, New York City time, on June 4, 2010, was extended to 5:00 p.m. on June 23, 2010 (subject to the Company's right to further extend such expiration in accordance with the terms of the Perpetual Preferred Share Offer").