ENSTAR GROUP INC
Form 10-Q
May 10, 2006

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended March 31, 2006

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 0-07477

The Enstar Group, Inc.
(Exact name of registrant as specified in its charter)

Georgia	**63-0590560**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

401 Madison Avenue
Montgomery, Alabama 36104

(Address of principal executive offices)
(334) 834-5483
(Registrant s telephone number, including area code)

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

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

Large Accelerated Filer o Accelerated Filer þ Non-Accelerated Filer o

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

The number of shares of Registrant s Common Stock, $.01 par value per share, outstanding at May 10, 2006 was 5,517,909.

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THIS FORM 10-Q AND OTHER STATEMENTS ISSUED OR MADE FROM TIME TO TIME BY THE ENSTAR GROUP, INC. OR MEMBERS OF ITS MANAGEMENT TEAM CONTAIN STATEMENTS WHICH MAY CONSTITUTE FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE SECURITIES ACT OF 1933, AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED BY THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995, 15 U.S.C.A. SECTIONS 77Z-2 AND 78U-5 (SUPP. 1996). THOSE STATEMENTS INCLUDE STATEMENTS REGARDING THE INTENT, BELIEF OR CURRENT EXPECTATIONS OF THE ENSTAR GROUP, INC. AND MEMBERS OF ITS MANAGEMENT TEAM, AS WELL AS THE ASSUMPTIONS ON WHICH SUCH STATEMENTS ARE BASED. PROSPECTIVE INVESTORS ARE CAUTIONED THAT ANY SUCH FORWARD-LOOKING STATEMENTS ARE NOT GUARANTEES OF FUTURE PERFORMANCE AND INVOLVE RISKS AND UNCERTAINTIES, AND THAT ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTEMPLATED BY SUCH FORWARD-LOOKING STATEMENTS. THERE ARE A NUMBER OF IMPORTANT FACTORS THAT COULD CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE INDICATED BY SUCH FORWARD-LOOKING STATEMENTS. THESE FACTORS INCLUDE, WITHOUT LIMITATION, THOSE SET FORTH IN ITEM 1A. RISK FACTORS TO THE ENSTAR GROUP, INC. ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005. THE ENSTAR GROUP, INC. UNDERTAKES NO OBLIGATION TO UPDATE OR REVISE FORWARD-LOOKING STATEMENTS TO REFLECT CHANGED ASSUMPTIONS, THE OCCURRENCE OF UNANTICIPATED EVENTS OR CHANGES TO FUTURE OPERATING RESULTS OVER TIME.

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PART I
FINANCIAL INFORMATION

Item 1. ***Financial Statements***

THE ENSTAR GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2006	December 31, 2005
	(Dollars in thousands) (Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 53,485	$ 54,032
Certificates of deposit	19,891	19,686
Other current assets	357	129
Total current assets	73,733	73,847
Partially owned equity affiliates	111,365	107,329
Other investments	3,486	3,542
Other assets	513	502
Total assets	$ 189,097	$ 185,220
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 850	$ 595
Income taxes payable	5,724	5,467
Total current liabilities	6,574	6,062
Deferred income tax liabilities	11,151	10,401
Accrued taxes	2,125	2,325
Deferred compensation	898	853
Other liabilities	459	456
Total liabilities	21,207	20,097
Commitments and contingencies (Note 5)		
Shareholders equity:		
Common stock ($.01 par value; 55,000,000 shares authorized, 5,960,260 shares issued at March 31, 2006 and December 31, 2005)	60	60
Additional paid-in capital	190,039	189,968
Accumulated other comprehensive income of partially owned equity affiliates, net	203	210
Accumulated deficit	(16,602)	(19,305)
Treasury stock, at cost (442,351 shares)	(5,810)	(5,810)

Total shareholders equity		167,890		165,123
Total liabilities and shareholders equity	$	189,097	$	185,220

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

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended March 31, 2006		Three Months Ended March 31, 2005	
	(Dollars in thousands, except per share data) (Unaudited)			
Interest income	$	782	$	482
Other investment income		199		
Earnings of partially owned equity affiliates		2,630		265
Other income (includes related party income of $100 for 2006 and 2005)		103		100
General and administrative expenses		(567)		(780)
Income before income taxes and extraordinary gain		3,147		67
Income taxes		(1,319)		(28)
Income before extraordinary gain		1,828		39
Extraordinary gain, net of income taxes of $543		875		
Net income	$	2,703	$	39
Weighted average shares outstanding basic		5,517,909		5,517,909
Weighted average shares outstanding assuming dilution		5,881,058		5,849,053
Income per common share before extraordinary gain basic	$	0.33	$	0.01
Extraordinary gain, net of income taxes basic		0.16		
Net income per common share basic	$	0.49	$	0.01
Income per common share before extraordinary gain assuming dilution	$	0.31	$	0.01
Extraordinary gain, net of income taxes assuming dilution		0.15		
Net income per common share assuming dilution	$	0.46	$	0.01

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

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended March 31,	
	2006	2005
	(Dollars in thousands) (Unaudited)	
Net income	$ 2,703	$ 39
Other comprehensive loss of partially owned equity affiliates:		
Unrealized holding losses on investments, net of income tax benefit of $15	(24)	
Currency translation adjustment, net of income tax expense (benefit) of $11 and $(15)	17	(24)
Other comprehensive loss	(7)	(24)
Comprehensive income	$ 2,696	$ 15

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

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31,	
	2006	**2005**
	(Dollars in thousands) (Unaudited)	
Cash flows from operating activities:		
Net income	$ 2,703	$ 39
Adjustments to reconcile net income to net cash used in operating activities:		
Earnings of partially owned equity affiliates	(2,630)	(265)
Dividends and distributions received from partially owned equity affiliates	11	
Extraordinary gain, net of income taxes	(875)	
Noncash compensation expense	62	
Deferred income taxes	11	(57)
Changes in assets and liabilities:		
Accounts payable and accrued expenses	512	75
Other, net	(60)	48
Net cash used in operating activities	(266)	(160)
Cash flows from investing activities:		
Purchases of certificates of deposit	(28,078)	
Maturities of certificates of deposit	27,797	
Net cash used in investing activities	(281)	
Decrease in cash and cash equivalents	(547)	(160)
Cash and cash equivalents at the beginning of the period	54,032	81,675
Cash and cash equivalents at the end of the period	$ 53,485	$ 81,515
Supplemental disclosures of cash flow information:		
Income taxes paid	$ 550	$ 1

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

THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1: General

The Enstar Group, Inc. and Subsidiaries, (the Company), is a publicly traded company engaged in the operation of several equity affiliates in the financial services industry. Enstar also continues its active search for one or more additional operating businesses which meet its acquisition criteria.

The Company, through the operations of its partially owned equity affiliates, Castlewood Holdings Limited (Castlewood Holdings) and B.H. Acquisition Limited (B.H. Acquisition), and their subsidiaries, acquires and manages insurance and reinsurance companies in run-off. The management of these businesses includes claims administration, adjustment and settlement together with the collection of reinsurance recoveries. Castlewood Holdings, a Bermuda-based company, also provides management, consulting and other services to the insurance and reinsurance industry for both fixed and success-based fee arrangements. In general, reinsurance is an arrangement in which the reinsurer agrees to indemnify an insurance or reinsurance company against all or a portion of the risks underwritten by such insurance or reinsurance company under one or more insurance or reinsurance contracts.

The Company consolidates JCF CFN LLC and related entities (collectively, the JCF CFN Entities). The JCF CFN Entities were formed to serve as members of Green Tree Investment Holdings LLC (formerly known as CFN Investment Holdings LLC) and related entities (collectively, Green Tree), which, in turn, were formed to effect the acquisition of a portfolio of home equity and manufactured housing loan securities and the associated servicing businesses from Conseco Finance Corp. (Conseco Finance). In July 2004, the JCF CFN Entities completed the sale of their entire interest in Green Tree and have been inactive since then.

The condensed consolidated financial statements of the Company are unaudited and, in the opinion of management, include all adjustments consisting solely of normal recurring adjustments necessary to fairly state the Company s financial condition, results of operations and cash flows for the interim period. The results of operations for the three months ended March 31, 2006 are not necessarily indicative of the results to be expected for the full year. These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2005 included in the Company s Form 10-K as filed with the Securities and Exchange Commission on March 16, 2006 under the Securities Exchange Act of 1934, as amended.

Note 2: Significant Accounting Policies

(a) *Principles of Consolidation* The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Enstar Financial Services, Inc. and Enstar Group Operations, Inc., both of which are currently inactive. In addition, the Company consolidates the JCF CFN Entities, recording a minority interest in its financial statements for Castlewood Holdings 40% interest. All significant intercompany balances and transactions have been eliminated in consolidation.

(b) *Use of Estimates* The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The estimates susceptible to significant change are those related to the valuation allowance for deferred tax assets and loss and loss adjustment expenses included in earnings of partially owned equity affiliates.

(c) *Cash Equivalents* Cash equivalents consist of short term, highly liquid investments with original purchased maturities of three months or less.

THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(d) *Partially Owned Equity Affiliates* Partially owned equity affiliates are accounted for under the equity method of accounting. Equity method investments are recorded at cost and are adjusted periodically to recognize the Company s proportionate share of the investee s income or loss, additional contributions made and dividends and capital distributions received. In the event any of the partially owned equity affiliates were to incur a loss and the Company s cumulative proportionate share of the loss exceeded the carrying amount of the equity method investment, application of the equity method would be suspended and the Company s proportionate share of further losses would not be recognized until the Company committed to provide further financial support to the investee. The Company would resume application of the equity method once the investee becomes profitable and the Company s proportionate share of the investee s earnings equals its cumulative proportionate share of losses that were not recognized during the period the application of the equity method was suspended.

(e) *Comprehensive Income* The Company reports comprehensive income in accordance with Statement of Financial Accounting Standards (SFAS) 130, Reporting Comprehensive Income which defines comprehensive income as certain changes in equity from non-owner sources. The Company recorded other comprehensive income from its partially owned equity affiliates. This other comprehensive income arose from unrealized holding gains and losses from debt and equity securities that are classified as available for sale and are carried at fair value, and currency translation adjustments resulting from the translations of financial information of subsidiaries into U.S. dollars.

The components of accumulated other comprehensive income are as follows:

	March 31, 2006		December 31, 2005	
Currency translation adjustment, net of income tax expense of $141 and $130	$	227	$	210
Unrealized holding losses, net of income tax benefit of $15		(24)		
Total accumulated other comprehensive income	$	203	$	210

(f) *Revenue Recognition* Revenue includes interest income earned from cash, cash equivalents and certificates of deposit, the Company s proportionate share of earnings from partially owned equity affiliates, investment income and other income. Interest income is recorded when earned. The Company s proportionate share of earnings from partially owned equity affiliates is recorded as such earnings are recognized by the partially owned equity affiliate.

(g) *Stock-Based Compensation* The Company utilizes various stock-based compensation plans for the benefit of non-employee directors and certain officers. In 1997, the Company adopted the Deferred Compensation and Stock Plan for Non-Employee Directors and a long-term incentive program made up of three stock option/incentive plans. Additionally, in 2001, the Company adopted the 2001 Outside Directors Stock Option Plan.

The options granted under the plans are exercisable during the period commencing from the date they vest until expiring according to the terms of the grant. Options generally expire no later than ten years from the grant date. Options under the various plans had original vesting schedules that ranged from one to four years. Any shares issued from the exercise of options would be from newly issued shares. There are a total of 817,500 shares authorized under the Company s various stock option plans, 52,500 of which are available to be granted at March 31, 2006. Prior to 2006, no compensation expense was recognized in net earnings for grants under stock option/incentive plans that had an exercise price equal to the market value of the Company s underlying common stock on the date of grant. In connection with options granted in November 2001, the market value of the Company s common stock on the date of grant exceeded the exercise price, resulting in a

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

charge to earnings for that year. In addition, compensation expense was recognized over the vesting life of these options through June 2004.

As of January 1, 2006, the Company adopted SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R). This Statement requires companies to recognize an expense in their financial statements for stock options based on the fair value method. The fair value method requires that a fair value be assigned to a stock option on its grant date and that this value be amortized over the grantees service period. Prior to January 1, 2006, the Company accounted for stock options in accordance with SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123) as amended by SFAS 148, Accounting for Stock-Based Compensation Transition. These Statements permitted companies to choose between two methods of recording the expense for stock options in their financial statements; either the fair value method, or the intrinsic value method, in accordance with Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and related interpretations. Under the intrinsic value method, compensation expense for the Company s option grants was only recognized if the exercise price of the employee stock option was less than the market price of the underlying stock on the date of grant. If a company elected to use the intrinsic value method, pro forma disclosures of earnings and earnings per share were required as if the fair value method of accounting had been applied. The Company previously elected to account for its stock options under the intrinsic value method and therefore computed and disclosed the required pro forma disclosures.

SFAS 123R provides for two alternative methods of adoption: the modified retrospective method and the modified prospective method. While the modified retrospective method permits restatement of prior periods for comparability, the Company has elected to apply the modified prospective method. The modified prospective method calls for unvested options as of January 1, 2006 and options granted after January 1, 2006 to be expensed in accordance with SFAS 123R after that date. Compensation expense under the fair value method for prior periods is not reflected in the financial statements of those periods but was disclosed on a pro forma basis. The table below presents the Company s pro forma earnings information as if stock options issued prior to January 1, 2006, were expensed in prior periods.

		Three Months Ended March 31, 2005 (Dollars in thousands, except per share data) (Unaudited)
Net income, as reported	$	39
Add: Stock-based employee compensation expense included in reported net income, net of income taxes		22
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of income taxes		(78)
Pro forma net loss	$	(17)
Income per common share:		
Basic as reported	$	0.01
Basic pro forma	$	0.00

Assuming dilution	as reported	$	0.01
Assuming dilution	pro forma	$	0.00

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The fair values for options granted under the Company s stock option plans were calculated at the date of grant using the Black-Scholes option pricing model. The estimated weighted average fair value at the date of grant for options vesting during the three months ended March 31, 2006 and 2005 was $9.50.

The adoption of SFAS 123R has not altered the Company s methodology of computing option expense from that used to prepare the pro forma disclosures in previous years. Furthermore, at the present time, the Company does not plan to change its policies of stock option compensation with respect to the number of grants, terms, or alternative instruments as a result of the adoption of SFAS 123R. Stock-based employee compensation is based on the application of Emerging Issues Task Force No. 00-23, Issues Related to the Accounting for Stock Compensation under APB 25 and FASB Interpretation No. 44, to the straight-line vesting of such awards over the full vesting period. At this time, the Company anticipates that 2006 after-tax stock option expense will be approximately $124,000 or $.02 per diluted share.

The effect of the adoption of SFAS 123R on selected line items is as follows for the three months ended March 31, 2006:

	Increase (Decrease)
General and administrative expense	$ 62
Income before income taxes	(62)
Income tax expense (benefit)	(26)
Net income	(36)
Net income per common share basic	(.01)
Net income per common share assuming dilution	(.01)

No stock option expense was capitalized during the three months ended March 31, 2006.

A summary of option activity for the three-month period ended March 31, 2006 is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2005	725,000	$ 20.47		
Outstanding at March 31, 2006	725,000	20.47	4.20	$ 50,220
Exercisable at March 31, 2006	640,000	17.74	3.76	46,081
Vested or expected to vest at March 31, 2006	725,000	20.47		

The total fair value of shares vesting during the three months ended March 31, 2006 was $380,000.

There were no options granted, exercised, forfeited or expired during the three months ended March 31, 2006.

Information about the Company s unrecognized stock-based compensation at March 31, 2006 is as follows:

Unrecognized compensation	$ 239,000
Weighted average period of expected recognition (in years)	.82

THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 3: Partially Owned Equity Affiliates

B.H. Acquisition

In July 2000, the Company, through B.H. Acquisition, a joint venture with Castlewood Limited (Castlewood) and an entity controlled by Trident II, L.P. (Trident), acquired as an operating business two reinsurance companies, Brittany Insurance Company Ltd. (Brittany) and Compagnie Europeenne d Assurances Industrielles S.A. (CEAI). Brittany and CEAI are principally engaged in the active management of books of reinsurance business from international markets. The Company owns 50% of the voting stock and a 33% economic interest in B.H. Acquisition. As part of the transaction, Castlewood owns 33% of the voting stock and a 45% economic interest in B.H. Acquisition. The Company s ownership in B.H. Acquisition is accounted for using the equity method of accounting.

Castlewood Holdings Limited

In November 2001, the Company, together with Trident and the shareholders and senior management of Castlewood (the Castlewood Principals), completed the formation of a new venture, Castlewood Holdings, to acquire and manage insurance and reinsurance companies, including companies in run-off (insurance and reinsurance companies that have ceased the underwriting of new policies), and to provide management, consulting and other services to the insurance and reinsurance industry (the Castlewood Holdings Transaction). The Company owns 50% of the voting stock of Castlewood Holdings and the Castlewood Principals and Trident each own 25% of Castlewood Holdings voting stock. The Company owns a 32.63% economic interest in Castlewood Holdings. Castlewood is a private Bermuda-based firm, experienced in managing and acquiring reinsurance operations. The Company s ownership in Castlewood Holdings is accounted for using the equity method of accounting.

As a result of this transaction, the Company s 33% direct economic interest in B.H. Acquisition increased by an additional indirect economic interest through Castlewood Holdings. At March 31, 2006, the Company s beneficial ownership in B.H. Acquisition was 47.68%. The Company s combined voting interest in B.H. Acquisition is limited to 50%.

In conjunction with the closing of the Castlewood Holdings Transaction, a wholly owned subsidiary of Castlewood Holdings completed the acquisition of two reinsurance companies in run-off, River Thames Insurance Company Limited (River Thames), based in London, England, and Overseas Reinsurance Corporation Limited (Overseas Reinsurance), based in Bermuda (collectively, the River Thames Transaction). The total purchase price of River Thames and Overseas Reinsurance was approximately $15.2 million.

In August 2002, Castlewood Holdings purchased Hudson Reinsurance Company Limited (Hudson), a Bermuda-based company, for approximately $4.1 million. Hudson reinsured risks relating to property, casualty and workers compensation, on a worldwide basis, and is now administering the run-off of its claims.

Also in 2002, Castlewood Holdings capitalized Fitzwilliam (SAC) Insurance Limited (Fitzwilliam), a wholly owned subsidiary. Fitzwilliam, based in Bermuda, offers specialized reinsurance protections to related companies, clients of Castlewood Holdings and other third-party companies.

In March 2003, Castlewood Holdings and Shinsei Bank, Limited (Shinsei) completed the acquisition of all of the outstanding capital stock of The Toa-Re Insurance Company (UK) Limited (Toa-UK), a London-based subsidiary of The Toa Reinsurance Company, Limited, for approximately $46 million. Toa-UK underwrote reinsurance business throughout the world between 1980 and 1994, when it stopped writing new business and is currently operating in run-off. The acquisition was effected through Hillcot Holdings Ltd. (Hillcot), a newly formed Bermuda company, in which Castlewood Holdings has a 50.1% economic interest and a 50% voting interest. Upon completion of the transaction, Toa-UK s name was changed to Hillcot Re

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THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Limited. Hillcot is included in Castlewood Holdings consolidated financial statements, with the remaining 49.9% economic interest reflected as minority interest. J. Christopher Flowers (Mr. Flowers), a member of the Company s board of directors and the Company s largest shareholder, is a director and the largest shareholder of Shinsei.

In August 2004, Castlewood Holdings implemented an employee stock-based compensation plan. The plan allows for the award of Castlewood Holdings Class D non-voting shares to certain senior employees up to a maximum of 7.5% of the total issued share capital of Castlewood Holdings. As a result of awards made in 2005 and 2004, the Company s economic interest in Castlewood Holdings of $33\frac{1}{3}$ % has been diluted by 0.70% to 32.63% as of March 31, 2006. As awarded shares vest and as additional shares are awarded in the future, the Company s economic interest could decrease to a minimum of 30.83%. The Company s voting interest will remain at 50%.

During 2004, Castlewood Holdings, through one of its subsidiaries, invested a total of approximately $9.1 million in Cassandra Equity LLC and Cassandra Equity (Cayman) LP, (collectively, Cassandra), for a 27% interest in each. Cassandra was formed to invest in equity shares of a publicly traded international reinsurance company. J.C. Flowers I LP also owned a 27% interest in Cassandra. J.C. Flowers I LP is a private investment fund, the general partner of which is JCF Associates I LLC. Mr. Flowers is the managing member of JCF Associates I LLC. In March 2005, Cassandra sold all of its holdings for total proceeds of approximately $40.0 million. Castlewood Holdings proportionate share of the proceeds was approximately $10.8 million.

Also during 2004, Castlewood Holdings, through one of its subsidiaries, completed the acquisition of Mercantile Indemnity Company Ltd., Harper Insurance Limited (formerly Turegum Insurance Company) and Longmynd Insurance Company Ltd. (formerly Security Insurance (UK) Ltd.) for a total purchase price of approximately $4.5 million. Castlewood Holdings recorded an extraordinary gain of approximately $21.8 million relating to the excess of the fair value of the net assets acquired over the cost of these acquisitions.

In May 2005, Castlewood Holdings, through one of its subsidiaries, purchased Fieldmill Insurance Company Limited (formerly known as Harleysville Insurance Company (UK) Limited) for approximately $1.4 million.

In December 2005, Castlewood Holdings, through two of its wholly-owned subsidiaries, invested approximately $24.5 million in New NIB Partners LP (NIB Partners), a newly formed Province of Alberta limited partnership, in exchange for an approximately 1.4% interest. NIB Partners was formed for the purpose of purchasing, together with certain affiliated entities, 100% of the outstanding share capital of NIBC N.V. (formerly, NIB Capital N.V.) and its affiliates (NIBC). NIBC is a merchant bank focusing on the mid-market segment in northwest Europe with a global distribution network.

New NIB Partners and certain related entities are indirectly controlled by New NIB Limited, an Irish corporation. Mr. Flowers is a director of New NIB Limited and is on the supervisory board of NIBC. Certain affiliates of J.C. Flowers I LP also participated in the acquisition of NIBC.

In March 2006, Castlewood Holdings and Shinsei completed the acquisition of Aioi Insurance Company of Europe Limited (Aioi Europe), a London-based subsidiary of Aioi Insurance Company, Limited, for £62 million (approximately $108 million), with £50 million in cash upon the closing of the transaction and £12 million in the form of a promissory note, payable twelve months from the date of the closing. Aioi Europe underwrote general insurance and reinsurance business in Europe for its own account until 2002 when it generally ceased underwriting, and placed into run-off, its general insurance and reinsurance business. The acquisition was effected through Hillcot. The acquisition has been accounted for using the purchase method of accounting. Castlewood Holdings recorded an extraordinary gain of approximately $4.3 million (net of minority

THE ENSTAR GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

interest of $4.3 million) relating to the excess of the fair value of the assets acquired over their cost. Upon completion of the transaction, Aioi Europe s name was changed to Brampton Insurance Company Limited.

Also in March 2006, Castlewood Holdings approved a commitment of up to $75.0 million in J.C. Flowers II LP (the J.C. Flowers Fund), a private investment fund to be formed by J.C. Flowers & Co. LLC. The transaction is expected to close in the second quarter of 2006. Castlewood Holdings intends to use cash on hand to fund its commitment.

J.C. Flowers & Co. LLC is controlled by Mr. Flowers. No fees will be payable by Castlewood Holdings to J.C. Flowers II LP, J.C. Flowers & Co. LLC, or Mr. Flowers in connection with Castlewood Holdings investment in the J.C. Flowers Fund.

Affirmative Investment LLC

In June 2005, the Company committed to contribute up to $10 million for a 14%, non-voting interest in Affirmative Investment LLC (Affirmative Investment), a newly formed Delaware limited liability company. J.C. Flowers I LP committed the capital necessary for the remaining 86% interest in Affirmative Investment. Both J.C. Flowers I LP and Affirmative Associates LLC, the managing member of Affirmative Investment, are controlled by Mr. Flowers, a member of the Company s board of directors and the Company s largest shareholder. In July 2005, the Company funded its initial capital contribution of approximately $2.6 million. Since that time, the Company has funded additional capital contributions of approximately $5.7 million. At March 31, 2006, the Company s total investment in Affirmative Investment was approximatel