FORM 10-K
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(Mark One)

(X) Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended: December 31, 1995

( ) Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from: ______ to ______

XEROX CORPORATION
(Exact name of registrant as specified in its charter)

1-4471
(Commission file number)

| New York | 16-0468020 |
|---|---|
| (State of incorporation) | (I.R.S. Employer Identification No.) |
| P.O. Box 1600, Stamford, Connecticut | 06904 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (203) 968-3000

Securities registered pursuant to Section 12(b) of the Act:

| Title of Each Class | Name of Each Exchange on Which Registered |
|---|---|
| Common Stock, $1 par value | New York Stock Exchange<br>Chicago Stock Exchange |
| $3.6875 Ten-Year Sinking Fund Preferred Stock | New York Stock Exchange |

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

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: (X) No: ( )

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

The aggregate market value of the voting stock of the registrant held by non-affiliates as of February 29, 1996 was: $15,511,301,091.

(Cover Page Continued)

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

| Class | Outstanding at February 29, 1996 |
|---|---|
| Common Stock, $1 Par Value | 108,621,646 Shares |
| Class B Stock, $1 Par Value | 1,000 Shares |

## Documents Incorporated By Reference

Portions of the following documents are incorporated herein by reference:

| Document | Part of 10-K in Which Incorporated |
|---|---|
| Xerox Corporation 1995 Annual Report to Shareholders | I & II |
| Xerox Corporation Notice of 1996 Annual Meeting of Shareholders and Proxy Statement (to be filed not later than 120 days after the close of the fiscal year covered by this report on Form 10-K). | III |

# PART I

## Item 1. Business

### Overview

Xerox Corporation (Xerox or the Company) is The Document Company and a leader in the global document market, providing document services that enhance productivity. References herein to "us" or "our" refer to Xerox and consolidated subsidiaries unless the context specifically requires otherwise. We distribute our products in the Western Hemisphere through divisions and wholly-owned subsidiaries. In Europe, Africa, the Middle East and parts of Asia including Hong Kong, India and China, we distribute through Rank Xerox Limited and related companies (Rank Xerox) in which we have an 80 percent financial interest and The Rank Organisation Plc (RO) has a 20 percent financial interest. In Japan and other areas of the Pacific Rim, Australia and New Zealand, document processing products are distributed by Fuji Xerox Co. Ltd. (Fuji Xerox), an unconsolidated joint venture, which is equally owned by Fuji Photo Film Company, Ltd. of Japan and Rank Xerox. On February 28, 1995, we paid RO 620 million pounds sterling, or $972 million, to increase our financial interest in Rank Xerox to 80 percent from 67 percent.

In January 1996, we announced agreements to sell our remaining property and casualty insurance units to investor groups led by Kohlberg Kravis Roberts & Co. (KKR) and existing management for consideration totaling $2.7 billion. We expect the transactions will close in the middle of this year. As a result, results from insurance operations are now accounted for as discontinued operations and all prior periods have been restated. Therefore, the Document Processing business is the only component of Continuing Operations.

Our Document Processing activities encompass developing, manufacturing, marketing, servicing and financing a complete range of document processing products and services designed to make offices around the world more productive. We believe that documents will play a central role in business, government, education and other organizations far into the future and that efficient processing of documents offers significant opportunities for productivity improvements. The financing of Xerox equipment is generally carried out by Xerox Credit Corporation (XCC) in the United States and internationally by foreign financing subsidiaries and divisions in most countries that we operate. Document Processing operations employed 85,200 people worldwide at year-end 1995.

In 1993, we announced a worldwide Document Processing restructuring program to significantly reduce the cost base and to improve productivity. Our objectives were to reduce our worldwide work force by more than 10,000 employees and to close or consolidate a number of facilities. To date, the activities associated with the 1993 restructuring program have reduced employment by 12,000 and achieved pre-tax cost savings of approximately $650 million in 1995 and $350 million in 1994. However, we have reinvested a portion of these savings to reengineer business processes, support the expansion in growth markets, and mitigate anticipated continuing pricing pressures.

## Continuing Operations - Document Processing

### The Document Processing Strategy

We believe that documents represent the knowledge base of an organization and will play a dynamic and central role in business, government, education and other organizations far into the future:

- Increasingly, documents are being created and stored in digital electronic form.

- The use of electronically created paper documents will continue to increase.

As The Document Company, we believe that by helping our customers navigate and manage the world of documents, we can help them improve their productivity and grow their businesses. We help customers make documents better, make better documents, and work better with documents.

We create customer value by providing innovative document technologies, products, systems, services and solutions that allow our customers to:

- Move easily within and between the electronic and paper forms of documents.

- Scan, store, retrieve, view, revise and distribute documents electronically anywhere in an organization.

- Print or publish documents on demand, at the point closest to the need, including those locations of our customers' customers.

- Integrate the currently separate modes of producing documents, such as the data center, production publishing and office environments into a seamless, user-friendly enterprise-wide document systems network - with technology acting as an enabler.

We have formed alliances to bring together the diverse infrastructures that currently exist and to nurture the development of an open document services environment to support complementary products from our partners and customers. We are working with more than 50 industry organizations to make office, production and electronic printing an integrated, seamless part of today's digital work place.

### Market Overview

Our total document processing revenues were $16.6 billion in 1995, of which 49 percent were generated in the United States, 33 percent in Europe, and 18 percent in the remainder of the world (excluding the unconsolidated $8.5 billion of Fuji Xerox revenues in Japan and much of the Pacific Rim).

We have traditionally had a strong position in the black-and-white copying market, which is expected to grow at a rate approximating real economic growth in North America and Western Europe, and at a faster rate in the developing countries. The remaining enterprise services market segments, which include production publishing, electronic printing, color copying and printing and digital office systems, are expected to grow at a substantially higher rate. With our many new product introductions over the past five years, our participation in the global document processing market has been considerably broadened and is expected to increase. This growth will be driven by the transfer of document production from offset printing to digital publishing, the increase in customer requirements for network and distributed printing, accelerating demand for color documents and the combination of many document capabilities into digital office systems.

### Xerox Focus

We believe that our success is due to our ability to continually improve the

features and performance of our products based on meeting demonstrated customer needs, competitive pricing levels, our excellent reputation for performance and service, expanding sales coverage through agents and retail chains, extending our leadership position in the rapidly growing document outsourcing business, maintaining our strong market position in emerging markets and continuing to capitalize on the exploding home office market. As a result, we believe we are well positioned to participate fully in the anticipated growth in the market segments in which we compete.

## Black-and-White Copying

We estimate that the black-and-white copying market was approximately $35 billion in 1995 and growing. With about $10 billion in copier revenues, we expect our black-and-white copier business to grow faster than the industry.

We market the broadest line of black-and-white copiers and duplicators in the industry, ranging from a three copies-per-minute personal copier to a 135 copies-per-minute fully-featured duplicator to special copiers designed for large engineering and architectural drawings up to 3 feet by 4 feet in size. Many of our state-of-the-art products have improved ease of use, reliability, copy quality, job recovery and ergonomics as well as productivity-enhancing features, including zoom enlargement and reduction, highlight color, copying on both sides of the paper, and collating and stapling which allow the preparation of completed document sets. The innovative copiers we introduced in 1995 include a high-speed copier for space-conscious offices and one specially designed to eliminate stress on bindings when books are copied.

We have a strong position with major accounts who demand a consistently high level of service worldwide. Our competitive advantages include a focus on customer call response times, diagnostic equipment that is state-of-the-art and availability of twenty-four-hour-a-day, seven-day-a-week service.

We also are increasing our leadership position in small commercial accounts, the most competitive copier market segment, through marketing programs such as sales through independent agents, retail outlets and trade associations like the American Medical Association, which represents more than two million current and prospective customers.

The market for commercial copiers is expanding rapidly in emerging countries in Latin America, Eastern Europe, the Commonwealth of Independent States, Africa, China and India. 1995 revenues in all of these markets grew faster than the growth in the developed markets.

## Enterprise Services Products

Our enterprise services products fall into four digital product categories: Production Publishing, Electronic Printing, Color Copying and Printing and Digital Office Systems.

### Production Publishing

The era of production publishing was launched in 1990 when we announced the DocuTech family which was a major step beyond our traditional reprographics market into the publishing industry, a $100 billion market with enormous potential. With more than 10,000 systems installed all over the world, our production publishing revenues in 1995 were $1.4 billion.

Production publishing technology is increasingly replacing older, traditional offset printing as customers seek improved productivity and cost savings, faster turnaround of document preparation, and the ability to print documents "on demand." We offer the widest range of solutions available in the marketplace - from dial-up lines through the Internet to state-of-the-art networks - and we are committed to expanding these print-on-demand solutions as new technology and applications are developed.

The DocuTech family of digital publishers scans hard copy and converts it into

digital documents, or accepts digital documents directly from networked personal computers or workstations. A user-friendly electronic cut-and-paste workstation allows the manipulation of images or the creation of new documents. For example, in only a few minutes, a page of word-processed text, received over a network, can be combined with a photograph which is scanned from hard copy and enhanced electronically: cropped, positioned precisely, rotated, brightened or sharpened. Digital masters can be prepared in a fraction of the time necessary to prepare offset plates, thereby allowing fast turnaround time. DocuTech prints high-resolution (600 dots per inch) pages at up to 135 impressions per minute. The in-line finisher staples completed sets or finishes booklets with covers and thermal-adhesive bindings. Because the finished document can be stored as a digital document, hard copy documents can be printed on demand, or only as required, thus avoiding the long production runs and high storage and obsolescence costs associated with offset printing. The concept of print-on-demand took another major step in 1995 when we introduced the 6135 Production Publisher. It makes print-for-one publishing practical; personalized publishing runs can now be as short as one or two prints.

## Electronic Printing

We estimate that the electronic printing market was over $20 billion in 1995 and is expected to grow to $25 billion in 1998.

This market has largely consisted of high-end host-connected printers and low-end desktop printers. We expect significant future growth for robust, fully featured printers serving multiple users on networks. This growth will be driven by the increase in personal computers and workstations on networks, client-server processing, accelerating growth in the demand for enterprise-wide distributed printing, and declining electronics costs. These faster, more reliable printers will print collated multiple sets on both sides of the paper, insert covers and tabs, and staple or bind; but without the labor-intensive steps of printing an original and manually preparing the documents on copiers. In addition, documents can be printed on these printers from remote data center computers, enabling the efficiencies of distributing electronically and then printing, rather than printing paper documents and then distributing them.

We have had a strong position in the high-end, high-volume electronic printing market segment since 1977. Our high-end electronic printing revenues were approximately $2 billion in 1995 and we expect this market to grow from almost $7 billion in 1995 to more than $9 billion in 1998. We are well positioned to capitalize on the growth in the electronic printing market because of both our innovative technologies and our understanding of customer requirements for distributed printing from desktop and host computers. Our goal is to integrate office, production and data-center electronic printing into a single, seamless, user-friendly network.

Xerox pioneered and continues to be a worldwide leader in electronic laser printing, which combines computer, laser, communications and xerographic technologies. We market a broad line of robust printers with speeds that range from five pages per minute (ppm) to the industry's fastest cut-sheet printer at 135 ppm, and continuous-feed production printers at speeds up to 420 ppm. Many of these printers have simultaneous interfaces that can be connected to multiple host computers as well as local area networks.

Breakthrough technology allows printing, in a single pass through our highlight color printers, black-and-white plus one customer-changeable color (as well as shades, textures and mixtures of each) at production speeds up to 92 ppm. Other manufacturers' highlight color printers require additional passes to add variable color, which increase cost, reduce speed and reliability and introduce the possibility of color misalignment.

Productivity-enhancing features include printing collated multiple sets on both sides of the paper, inserting covers and tabs, printing checks with magnetic ink character recognition (MICR), and stapling; all on cut sheet plain paper, with sizes up to 11 by 17 inches.

During 1995, we significantly expanded our opportunities with two major new printer series that will redefine our role in the electronic production printing industry. With the DocuPrint CF Series family, we entered the market for very high-volume, continuous-feed printers at speeds up to 420 ppm. The new DocuPrint IPS Series makes the IBM Advanced Function Presentation (AFP) architecture directly available to our production printing customers.

Color Copying and Printing

We estimate that the color copying and printing market was $14 billion in 1995 and is expected to grow to $24 billion in 1998. Our revenues from color products grew 45 percent in 1995 to $600 million.

The use of color originals in the office is accelerating. Independent studies have concluded that color documents are more effective in communicating information and that decision maker performance improves with the use of color documents. The vast majority of industry shipments of workstations and personal computers have color monitors, creating the need for economical, convenient and reliable, high-quality color copying and printing.

Xerox entered the digital color market in 1991 with the introduction of the Xerox 5775 digital copier which is targeted at the production market segment. The 5775 copies high resolution full color at 7.5 ppm, black-and-white at 30 ppm, and allows the colorizing of black-and-white documents. The Xerox 4700 is a highly cost-efficient, full-color 7.5 ppm electronic printer that also prints black-and-white at 30 ppm. The 4700 prints complete collated documents incorporating both black-and-white and color pages in a single step and at optimum speeds. It offers a broad array of connectivity options for both the office network and host computer environments. The MajestiK color copier series, introduced in 1993, offers benchmark copy quality and price/performance, and prints full color at 6 ppm and black-and-white at 36 ppm. The MajestiK series is targeted at the expanding market for color in the office. In 1994, we introduced the 4900 color laser printer for networked office groups printing at up to 1200 by 300 dpi resolution and three ppm for full color and 12 ppm for black-and-white. During 1995, we introduced the XPrint family of networked desktop color laser printers using "Intelligent Color" technology allowing work groups to integrate color and black-and-white documents on a single printer at up to 600 x 600 dots per inch resolution. We also introduced the Regal color copier/printer that provides MajestiK color copy quality at a fast 9 ppm speed for full color copying and printing.

Digital Office Systems

Our digital office systems, known as Document Centre Systems, were introduced in 1995 and bring the production publishing productivity to the office. This new category of robust and extensible systems combines many capabilities - printing, scanning, faxing and copying documents - into a single digital resource that can be accessed from either a personal computer or on a walk-up basis. With interactive software, a user can easily control the various steps of the document cycle - document input, management and output - from the desktop. The seamless integration of services and interoperability will bring new levels of efficiency to the office. These new systems are a portal to the network and allow office workers to navigate between digital and paper documents, share information and knowledge, and collaborate with other members of their work groups. The multitasking architecture allows Document Centre Systems to perform multiple functions concurrently.

The two initial models in the Document Centre product family are equipped with integrated scanners for digital copying and printing services, accessible either from the PC desktop or from the user interface on the devices themselves. The Document Centre System 35 is designed for work groups of up to 50 people, and copies and prints at 35 ppm with resolutions of up to 600 by 2,400 dots per inch. It provides two-sided printing and several document finishing options. The Document Centre System 20 is targeted for work groups of up to 20 people, and copies and prints at 20 ppm with 400 dots per inch resolution. Fax services, from the desktop or at the device, are standard.

Other Products

We also offer a wide range of other document processing products including ink-jet and electrostatic printers, multifunction products, facsimile products, scanners, personal computer and workstation software, and integrated systems solutions.

We also sell cut-sheet paper to our customers for use in their Document Processing products.

## Summary of Revenues by Product Category

The following table summarizes our revenues by major product category. The revenues for black-and-white copiers and enterprise services products include equipment and supply sales, service and rental revenues, and finance income. These revenues exclude the impact of foreign currency exchange rate fluctuations which are shown combined with the revenues from paper and other products.

| Year ended December 31 (in billions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| Black-and-white copiers | $ 9.6 | $ 9.5 | $ 9.1 |
| Enterprise services products | 4.1 | 3.5 | 2.9 |
| Paper, other products, currency | 2.9 | 2.1 | 2.2 |
| Total revenues | $16.6 | $15.1 | $14.2 |

## Xerox Competitive Advantages

Although the document processing industry is highly competitive, we believe that we enjoy significant competitive advantages because of our dedication to customer satisfaction, our total quality management processes, our substantial on-going investment in research and development, and our large direct sales and service forces.

### Customer Satisfaction

Our highest priority is customer satisfaction. Our research shows that satisfied customers are far more likely to repurchase products and that the cost of selling a replacement product to a satisfied customer is far less than selling to a "new" customer. We regularly survey customers on their satisfaction, measure the results, analyze the root causes of dissatisfaction, and take steps to correct any problems.

Because of our emphasis on customer satisfaction, we offer a Total Satisfaction Guarantee, one of the simplest and most comprehensive offered in any industry: "If you are not satisfied with our equipment, we will replace it without charge with an identical model or a machine with comparable features and capabilities." This guarantee applies for three years to equipment acquired from and continuously maintained by Xerox or its authorized agents.

### Quality

We were an early pioneer in total quality management and are the only company to have won all three of the following prestigious quality awards: the Malcolm Baldrige National Quality Award in the United States in 1989, the European Quality Award in 1992 and the Deming Prize in Japan, won by Fuji Xerox in 1980. In addition, we have won top quality awards in Argentina, Australia, Belgium, Brazil, Canada, Colombia, France, Germany, Hong Kong, India, Ireland, Mexico, the Netherlands, Norway and the United Kingdom. Our "Leadership Through Quality" program has enabled us to significantly reduce our costs, accelerate the introduction of new products, improve customer satisfaction and increase market share. Xerox products have been consistently rated among the world's best by independent testing organizations.

### Research and Development

The Xerox research and development (R&D) program is directed toward the

development of new products and capabilities in support of our document processing strategy. Our research scientists are deeply involved in the formulation of corporate strategy and key business decisions. They regularly meet with customers and have dialogues with our business divisions to ensure they understand customer requirements and are focused on products that can be commercialized.

In 1995, R&D expense was $951 million compared with $895 million in 1994 and $883 million in 1993. We expect to increase our investment in technological development in 1996 and over the longer term to maintain our premier position in the rapidly changing document processing market. Our R&D spending is strategically coordinated with Fuji Xerox. The R&D investment by Fuji Xerox was approximately $600 million in 1995, bringing the total to approximately $1.5 billion.

## Marketing

Xerox document processing products are principally sold directly to users by our worldwide sales force of approximately 12,000 employees. We also market through a network of independent agents, dealers, distributors and value-added resellers and have arrangements with U.S. retail marketing channels, including Sears, Office Depot, Office Max, Service Merchandise, Staples, Wal-Mart, Costco, The Wiz, Price Club and MicroAge, to market low-end products not generally suited for distribution through our direct sales force. These products are now sold through approximately 3,000 retail stores.

In 1991, Xerox International Partners (XIP), a 51 percent-owned partnership, was formed between Xerox and Fuji Xerox to supply printer engines to original equipment manufacturers. XIP has also contracted to supply printer engines to resellers.

## Service

We have a worldwide service force of approximately 26,000 employees. In our opinion, this direct service force is a significant competitive advantage: the service force is continually trained on our new products and the diagnostic equipment is state-of-the-art. Twenty-four-hour-a-day, seven-day-a-week service is available in most metropolitan areas in the United States. We are able to guarantee a consistent level of service nationwide and worldwide because our service force is not focused exclusively on metropolitan areas and it does not rely on independent local dealers for service.

## Revenues

Revenues from supplies, paper, service, rentals, facilities management and other revenues, and income from customer financing, which represented 67 percent of total revenues in 1995, are derived from the installed base of equipment and are therefore less volatile than equipment sales revenues and provide significant stability to overall revenues. Growth in these revenues is primarily a function of the growth in our installed population of equipment, usage and pricing. The balance of our revenues are derived from equipment sales. These sales, which drive the non-equipment revenues, depend on the flow of new products and are more affected by economic cycles.

Most of our customers have their equipment serviced by and use supplies sold by us. The market for cut-sheet paper is highly competitive and revenue growth is significantly affected by pricing. Our strategy is to charge a spread over mill wholesale prices. After a number of years of decline, rental revenues increased slightly in 1995.

Our document outsourcing business provides printing, publishing, duplicating and related services at almost 4,000 customer locations in 36 countries, including legal and accounting firms, financial institutions, insurance agencies and manufacturing companies. Our revenues from these services, which are largely in the U.S., increased 50 percent to $900 million in 1995.

We offer our document processing customers financing of their purchases of Xerox equipment primarily through XCC in the United States, largely by wholly-owned financing subsidiaries in Europe, and through divisions in Canada and Latin America. Our financing operations have expanded over the past several years in recognition of customer demand and the associated profit opportunities.

While competition for this business from banks and other finance companies remains extensive, we actively market our equipment financing services on the basis of customer service, convenience and competitive rates. Approximately 80 percent of U.S. equipment sales and 70 percent of European equipment sales are financed through Xerox. Over time, the growth rate of financing income is expected to correspond to the growth rate of equipment sales and trends in interest rates.

International Operations

Our international operations account for 51 percent of Document Processing revenues. Xerox' largest interest outside the United States is the "Rank Xerox Companies" in which we have an 80 percent financial interest and The Rank Organisation Plc (RO) has a 20 percent financial interest. On February 28, 1995, Xerox paid RO 620 million pounds sterling, or $972 million, to increase the Xerox financial interest in Rank Xerox to about 80 percent from 67 percent. Marketing and manufacturing operations are also conducted through joint ventures in India and China. Marketing and manufacturing in the Americas Customer Operations organization are conducted through subsidiaries or distributors in 40 countries. Marketing and manufacturing in Japan and other areas of the Pacific Rim, Australia and New Zealand are conducted by Fuji Xerox.

Xerox' financial results by geographical area for 1995, 1994 and 1993, which are presented on pages 35, 36, 58 and 59 of the Company's 1995 Annual Report to Shareholders, is hereby incorporated by reference in this document in partial answer to this item.

Discontinued Operations - Insurance and Other Financial Services and Third-Party and Real-Estate

The discussion in the first ten paragraphs under the caption "Insurance and Other Financial Services" on pages 48 and 49 and under the caption "Discontinued Operations - Other Financial Services and Third-Party and Real-Estate" on pages 52 and 53 set forth under the caption "Financial Review" in the Company's 1995 Annual Report to Shareholders is hereby incorporated by reference in this document in partial answer to this item.

Property and Casualty Reserves

Overview

Losses from claims and related claims handling and legal expense comprise the majority of costs from providing insurance products. Therefore, unpaid losses and loss expenses is generally the largest liability on a property and casualty insurer's balance sheet. However, because insurance coverage is provided for situations in which the certainty of loss cannot be predicted, ultimate losses which will be incurred on policies issued are difficult to estimate and are subject to constant reevaluation as new information becomes available. Insurance companies utilize a variety of loss trending and analysis techniques to estimate anticipated ultimate losses and the time frames when claims are likely to be reported and paid. These patterns vary significantly by type of insurance coverage and are affected by the economic, social, judicial and weather-related/geological conditions in different geographic areas.

In order to moderate the potential impact of unusually severe or frequent losses, insurers often cede (i.e., transfer) through reinsurance mechanisms a portion of their gross policy premiums to reinsurers in exchange for the reinsurer's agreement to share a portion of the covered losses with the insurer. Although the ceding of insurance does not discharge the original

insurer from its primary liability to its policyholder, the reinsurer that accepts the risk assumes an obligation to the original insurer. The ceding insurer retains a contingent liability with respect to reinsurance ceded to the extent that the reinsurer might not be able to meet its obligations.

The net liability retained on individual risks varies by product and by the nature of the risk. Insured liabilities are reinsured either by treaty, wherein reinsurers agree in advance to provide coverage above retained limits or for a specified percentage of losses attributable to specific products, or by facultative arrangements, wherein reinsurance is provided for individual risks based on individual negotiations.

Reserve provisions are established by the insurer to provide for the estimated level of claim payments which will be made under the policies it writes. Over the policy period, as premiums are earned, a portion of the premiums is set aside as gross loss and loss expense reserves for incurred but not reported ("IBNR") losses in anticipation of claims which will be incurred, net of anticipated salvage and subrogation. IBNR reserves also include amounts to supplement case reserves, when established, to provide for potential further loss development. In addition, gross reserves are established for internal and external loss adjustment expenses ("LAE") associated with handling the claims inventory. These expenses are characterized as "allocated LAE" when they are attributable to a specific claim or series of claims and "unallocated LAE" when not similarly attributable. When a claim is reported, case reserves are established on the basis of all pertinent information available at the time. Legal defense costs that can be assigned to a related claim file and can be included as part of the loss under the contract are generally established as part of the gross case reserve. Reinsurance recoverables on gross reserves are recorded for amounts that are anticipated to be recovered from reinsurers and are determined in a manner consistent with the liabilities associated with the reinsured policies. Net reserves are gross reserves less anticipated reinsurance recoverables (net of uncollectible reinsurance)and salvage and subrogation on those reserves.

The effect of inflation on gross reserves is considered implicitly when estimating the liability for unpaid losses and loss expenses. The effect of inflation on individual case basis reserves reflects the direction of economic price levels as they affect the individual claims being reserved.

Estimates of the ultimate value of unpaid claims are based in part on historical data that reflect past inflation, as well as management's assessment of severity and frequency, industry trends and related costs.

Ridge Re Coverage

Under the terms of the Ridge Re reinsurance coverage and subject to the limits established for each insurance operating group, Ridge Re will reimburse the Insurance Companies within their respective insurance operating group for 85% of net increases, if any, to ultimate net unpaid loss and loss expenses and uncollectible reinsurance reserves which may develop on its 1992 and prior accident years as carried at December 31, 1992 (net of all salvage, subrogation and other recoverables). At December 31, 1995, Ridge Re has accrued approximately $750 million of the $1,245 million maximum excess of loss reinsurance coverage estimated to be required based on actuarial projections. The Ridge Re coverage is guaranteed by XFSI, and, subject to certain commutation provisions, remains in effect until all 1992 and prior accident year claims are paid. Cessions to Ridge Re, while beneficial to the Remaining Talegen insurance operating groups and TRG, do not result in a benefit to the Insurance segment or consolidated Xerox accounts. The Ridge Re coverage will continue in effect after the consummation of the sale to the KKR groups.

Monitoring of Insurance Reserves

Gross and net reserves for business written in both current and prior years is continually monitored by the Remaining insurance companies, and Talegen senior management reviews these reserves on a periodic basis. These reserves are also reviewed and certified on an annual basis by an outside actuary appointed

by the Remaining insurance companies. Overall reserve levels are impacted primarily by the types and amounts of insurance coverage currently being written and the trends developing from newly reported claims and claims which have been paid and closed. Adjustments are made to reserves in the period they can be reasonably estimated to reflect evolving changes in loss development patterns and various other factors. Such factors include increased damage awards by the courts, known changes in judicial interpretations of legal liability for asbestos-related, environmental and other latent exposure claims, changes in judicial interpretation of the scope of coverage provided by general liability and umbrella policies for "advertising injury," particularly in the area of "unfair competition," and other recently advanced new theories of liability. Many of these judicial interpretations are still evolving. Generally, the greater the projected time to settlement, the greater the complexity of estimating ultimate claim costs and the more likely that such estimates will change as new information becomes available.

Use of Reinsurance and Management of Reinsurance Collection

Most of the Remaining insurance companies made significant use of reinsurance during the 1970's and early 1980's. Since that time, the Remaining insurance companies have generally increased the portion of business they retain while reducing the number of reinsurers used for their reinsurance contracts. During 1995 and 1994, excluding the insurance operating groups sold, 85% and 63%, respectively, of total written premiums ceded to reinsurers were placed with approximately 30 reinsurers.

Talegen has a reinsurance security committee composed of senior management who approve those reinsurers with whom Talegen will do business. The criteria under which such approvals are granted have become increasingly restrictive over the past several years.

The potential uncollectibility of ceded reinsurance is an industry-wide issue. With respect to the management of recoveries due from reinsurers, the Remaining insurance companies operate under common guidelines for the early identification of potential collection problems and assign these cases to a specialized group under TRG staffed by "work-out" experts. This unit aggressively pursues collection of reinsurance recoverables through mediation, arbitration and, where necessary, litigation to enforce the Remaining insurance companies contractual rights against reinsurers. Nevertheless, periodically, it becomes necessary for management to adjust reserves for potential losses to reflect their ongoing evaluation of developments which affect recoverability, including the financial difficulties that some reinsurers can experience. Based upon the review of financial condition and assessment of other available information, the Remaining insurance companies maintain a provision for uncollectible amounts due from reinsurers. The balance of reinsurance recoverable is considered to be valid and collectible.

Statutory and GAAP Reporting of Net Unpaid Losses and Loss Expenses

The liability for unpaid losses and loss expenses required by generally accepted accounting principles ("GAAP") includes various adjustments from the liability reported in accordance with Statutory Accounting Practices ("SAP"). Because not all GAAP adjustments can be associated with subsequent developments of the liabilities on other than an arbitrary basis, developments on the loss and loss expense reserve development table are prepared in accordance with SAP. The increase in 1995 in the difference between the GAAP unpaid loss and loss expense reserve and the corresponding SAP liabilities was principally caused by the application, by Xerox, of accounting principles applicable to discontinued operations which did not result in increased liabilities for SAP purposes at the Insurance operating subsidiary level.

Loss Development Data

In Note 9 on page 59 of the Company's 1995 Annual Report to Shareholders, which is hereby incorporated by reference in this document in partial answer

to this item, the net liability for unpaid losses and loss expenses is reconciled for each of the years in the three-year period ended December 31, 1995. Included therein are current year and prior year development data.

As a result of claim activity during 1995 and after reflection of prior experience, it is management's judgment that the total liability for unpaid losses and loss expenses at December 31, 1995 is reasonably stated.

The loss and loss expense reserve development table illustrates the development of statutory balance sheet liabilities for 1985 through 1995 for the Remaining insurance companies gross of Ridge Re cessions. Unpaid loss and loss expense reserves and accident year development have been restated to exclude the reserves of Constitution Reinsurance Corporation and Viking Insurance Company of Wisconsin, which were sold during 1995. The first line of the table is the estimated liability for unpaid losses and loss expenses, net of reinsurance recoverable, recorded at the balance sheet date for each year. The lower section of the table shows the updated amount of the previously recorded liability based on experience as of the close of each succeeding year. The estimate is increased or decreased as more information becomes known about the claims until all claims are settled. Deficiencies or redundancies represent aggregate changes in estimates as calculated on a statutory basis for all prior calendar years. The effect as calculated under GAAP on income for the latest three years is shown in Note 9 on page 59 of the Company's 1995 Annual Report to Shareholders, which is hereby incorporated by reference in this document in partial answer to this item. These changes in estimates have been reflected in Talegen's calendar year operating results. As the Remaining insurance companies recognize adjustments to reserves for changes in loss development patterns and various other factors, such as social and economic trends and known changes in judicial interpretation of legal liability, in the period in which they become known, it is not appropriate to extrapolate future redundancies or deficiencies based solely on this table.

Loss and Loss Expense Reserve Development

| Year ended December 31 (in millions) | 1985 | 1986 | 1987 | 1988 |
|---|---|---|---|---|
| Liability for unpaid losses and loss expenses - GAAP (net of reinsurance) | $ 3,498 | $ 4,127 | $ 4,824 | $ 5,200 |
| Increase (decrease) for GAAP adj. | (148) | (256) | (241) | (208) |
| Liability for unpaid losses and loss expense - SAP (net of reinsurance) | 3,350 | 3,871 | 4,583 | 4,992 |
| Paid (cumulative) as of: | | | | |
| End of year | - | - | - | - |
| One year later | 1,169 | 1,187 | 1,323 | 1,246 |
| Two years later | 1,986 | 2,080 | 2,188 | 2,269 |
| Three years later | 2,596 | 2,701 | 2,933 | 3,043 |
| Four years later | 3,056 | 3,224 | 3,472 | 3,854 |
| Five years later | 3,450 | 3,611 | 4,150 | 4,053 |
| Six years later | 3,729 | 4,180 | 4,316 | 4,432 |
| Seven years later | 4,221 | 4,278 | 4,571 | 4,751 |
| Eight years later | 4,281 | 4,476 | 4,859 | |
| Nine years later | 4,449 | 4,720 | | |
| Ten years later | 4,673 | | | |
| Liability estimated as of: | | | | |
| End of year | 3,350 | 3,871 | 4,583 | 4,992 |
| One year later | 3,397 | 3,893 | 4,681 | 5,052 |
| Two years later | 3,826 | 4,314 | 4,870 | 5,247 |
| Three years later | 4,051 | 4,527 | 5,168 | 5,171 |
| Four years later | 4,311 | 4,928 | 5,073 | 5,953 |
| Five years later | 4,681 | 4,803 | 5,832 | 5,903 |
| Six years later | 4,644 | 5,495 | 5,854 | 6,029 |
| Seven years later | 5,260 | 5,546 | 5,959 | 6,381 |
| Eight years later | 5,353 | 5,673 | 6,314 | |
| Nine years later | 5,506 | 6,045 | | |
| Ten years later | 5,880 | | | |

| (Deficiency) redundancy | $(2,530) | $(2,174) | $(1,731) | $(1,389) |
|---|---|---|---|---|

End of Year:
  Gross liability
  Reinsurance recoverable
  Net liability

One Year Later:
  Gross re-estimated liability
  Re-estimated recoverable
  Net re-estimated liability

Two Years Later:
  Gross re-estimated liability
  Re-estimated recoverable
  Net re-estimated liability

Three Years Later:
  Gross re-estimated liability
  Re-estimated recoverable
  Net re-estimated liability

Gross cumulative deficiency

| 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
|---|---|---|---|---|---|---|
| $ 5,637 | $ 5,848 | $ 5,743 | $ 6,109 | $ 5,972 | $ 5,618 | $ 6,471 |
| (215) | (287) | (299) | (370) | (254) | (216) | (827) |
| 5,422 | 5,561 | 5,444 | 5,739 | 5,718 | 5,402 | 5,644 |
| - | - | - | - | - | - | - |
| 1,560 | 1,542 | 1,721 | 1,080 | 1,303 | 1,242 | |
| 2,635 | 2,882 | 2,518 | 2,153 | 2,264 | | |
| 3,690 | 3,412 | 3,381 | 2,939 | | | |
| 4,018 | 4,062 | 4,008 | | | | |
| 4,508 | 4,563 | | | | | |
| 4,887 | | | | | | |
| 5,422 | 5,561 | 5,444 | 5,739 | 5,718 | 5,402 | 5,644 |
| 5,611 | 5,658 | 6,340 | 5,734 | 5,711 | 5,944 | |
| 5,591 | 6,484 | 6,274 | 5,771 | 6,216 | | |
| 6,408 | 6,370 | 6,326 | 6,230 | | | |
| 6,329 | 6,429 | 6,747 | | | | |
| 6,428 | 6,803 | | | | | |
| 6,770 | | | | | | |
| $(1,348) | $(1,242) | $(1,303) | $ (491) | $ (498) | $ (542) | $ - |
| | | | $ 9,469 | $ 8,526 | $ 7,849 | $ 8,143 |
| | | | 3,730 | 2,808 | 2,447 | 2,499 |
| | | | 5,739 | 5,718 | 5,402 | 5,644 |

| | | | |
|---|---|---|---|
| 9,444 | 8,590 | 8,616 | |
| 3,710 | 2,879 | 2,672 | |
| 5,734 | 5,711 | 5,944 | |
| 9,482 | 9,316 | | |
| 3,711 | 3,100 | | |
| 5,771 | 6,216 | | |
| 10,188 | | | |
| 3,958 | | | |
| 6,230 | | | |
| $ (719) | $ (790) | $ (767) | $ - |

Asbestos-Related, Environmental and Other Latent Exposure Claims

The discussion under the captions "Latent Exposures," "Reserves for the Remaining Insurance Companies" and "Latent Exposure Reserves" on pages 50 through 52 in the Company's 1995 Annual Report to Shareholders is hereby incorporated by reference in this document in partial answer to this item.

Item 2. Properties

The Company owns a total of eleven principal manufacturing and engineering facilities and leases an additional such facility. The domestic facilities are located in California, New York and Oklahoma, while the international facilities are located in Brazil, Canada, England, France, Holland and Mexico. The Company also has four principal research facilities; two are owned facilities in New York and Canada, and two are leased facilities in California and France.

In addition, within the Company, there are numerous facilities which encompass general offices, sales offices, service locations and distribution centers. The principal owned facilities are located in the United States, England, and Mexico. The principal leased facilities are located in the United States, Brazil, Canada, England, Mexico, France, Germany and Italy.

The Company has closed and downsized numerous facilities as part of the worldwide Document Processing restructuring program announced in December 1993. The facilities closed or downsized encompass general offices, sales offices, and distribution centers. The principal closed or downsized domestic facilities were located in California, Connecticut and Illinois.

The Company's Corporate Headquarters facility, located in Connecticut, is leased; a training facility, located in Virginia, is owned by the Company. In the opinion of Xerox management, its properties have been well maintained, are in sound operating condition and contain all the necessary equipment and facilities to perform the Company's functions.

Item 3. Legal Proceedings

The information set forth under Note 14 "Litigation" on page 73 of the Company's 1995 Annual Report to Shareholders is incorporated by reference in this document in answer to this item.

On July 21, 1993, the Company was notified that it had been named as a respondent by the United States Environmental Protection Agency ("EPA") in a unilateral Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") section 106 (a) Administrative Order regarding the Metcoa Radiation Site in Pulaski, PA. The Order directs the Company and 21 other companies to perform remedial work at the Site. The order alleges that these parties are jointly and severally liable to perform the work. Under CERCLA, a respondent that does not comply with the Order could be subject to a civil

penalty of $25,000 for each day of noncompliance and be liable for punitive damages at least equal to treble the EPA's cost of cleaning up the Site. The Company denies that it is liable to perform the work described in the Order.

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

None.

# PART II

## Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

The information set forth under the following captions on the indicated pages of the Company's 1995 Annual Report to Shareholders is hereby incorporated by reference in this document in answer to this Item:

| Caption | Page No. |
|---|---|
| Stock Listed and Traded | 81 |
| Dividends and Stock Prices | 81 |
| Ten Years in Review - Common Shareholders of Record at Year-End | 80 and 81 |

## Item 6. Selected Financial Data

The following information, as of and for the five years ended December 31, 1995, as set forth and included under the caption "Ten Years in Review" on pages 80 and 81 of the Company's 1995 Annual Report to Shareholders, is hereby incorporated by reference in this document in answer to this Item:

- Revenues
- Income (loss) from continuing operations
- Primary earnings (loss) per common share from continuing operations
- Total assets
- Long-term debt
- Preferred stock
- Dividends declared

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

The information set forth under the caption "Financial Review" on pages 33-40, 42-45, and 47-53 of the Company's 1995 Annual Report to Shareholders other than the pictures and captions to the pictures is hereby incorporated by reference in this document in answer to this Item.

## Item 8. Financial Statements and Supplementary Data

The consolidated financial statements of Xerox Corporation and subsidiaries and the notes thereto and the report thereon of KPMG Peat Marwick LLP, independent auditors, which appear on pages 32, 41, 46, 54-77, and 79 of the Company's 1995 Annual Report to Shareholders, are hereby incorporated by reference in this document in answer to this Item. In addition, also included is the quarterly financial data included under the caption "Quarterly Results of Operations (Unaudited)" on page 78 of the Company's 1995 Annual Report to Shareholders.

The financial statement schedule required herein is filed as "Financial Statement Schedules" pursuant to Item 14 of this Report on Form 10-K.

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

Not applicable.

## PART III

The information set forth in "Proposal 1--Election of Directors" in the Company's Notice of the 1996 Annual Meeting of Shareholders and Proxy Statement, to be filed pursuant to Regulation 14A not later than 120 days after the close of the fiscal year covered by this report on Form 10-K, is hereby incorporated by reference in this document in answer to this Part III.

### Executive Officers of Xerox

The following is a list of the executive officers of Xerox, their current ages, their present positions and the year appointed to their present positions. There are no family relationships between any of the executive officers named.

Each officer is elected to hold office until the meeting of the Board of Directors held on the day of the next annual meeting of shareholders, subject to the provisions of the By-Laws.

| Name | Age | Present Position | Year Appointed to Present Position | Officer Since_ |
|---|---|---|---|---|
| Paul A. Allaire* | 57 | Chairman of the Board, Chief Executive Officer and Chairman of the Executive Committee | 1991 | 1983 |
| William F. Buehler | 56 | Executive Vice President and Chief Staff Officer | 1993 | 1991 |
| A. Barry Rand | 51 | Executive Vice President, Operations | 1992 | 1986 |
| Barry D. Romeril | 52 | Executive Vice President and Chief Financial Officer | 1993 | 1993 |
| Stuart B. Ross | 58 | Executive Vice President; Chairman and Chief Executive Officer, Xerox Financial Services, Inc. | 1990 | 1979 |
| Allan E. Dugan | 55 | Senior Vice President, Corporate Strategic Services | 1992 | 1990 |
| John A. Lopiano | 57 | Senior Vice President; President, Production Systems Group | 1995 | 1993 |
| Mark B. Myers | 57 | Senior Vice President, Corporate Research and Technology | 1992 | 1989 |
| David R. Myerscough | 55 | Senior Vice President; Corporate Business Strategy | 1996 | 1989 |

* Member of Xerox Board of Directors.

### Executive Officers of Xerox, Continued

| Name | Age | Present Position | Year Appointed to Present Position | Officer Since_ |
|---|---|---|---|---|
| Richard S. Paul | 54 | Senior Vice President and | 1992 | 1989 |

| | | General Counsel | | |
|---|---|---|---|---|
| Brian E. Stern | 48 | Senior Vice President; President, Office Document Products Group | 1996 | 1993 |
| Eunice M. Filter | 55 | Vice President, Treasurer and Secretary | 1990 | 1984 |
| Philip D. Fishbach | 54 | Vice President and Controller | 1995 | 1990 |
| James H. Lesko | 44 | Vice President; President, Desktop Products Group | 1996 | 1993 |
| Carlos Pascual | 50 | Vice President; President, U.S. Customer Operations | 1995 | 1994 |

Each officer named above, with the exceptions of William F. Buehler and Barry D. Romeril, has been an officer or an executive of Xerox or its subsidiaries for at least the past five years.

Prior to joining Xerox in 1991, Mr. Buehler was Vice President, Network Systems Sales at the American Telephone & Telegraph Company (AT&T). Mr. Buehler had been affiliated with AT&T since 1964.

Prior to joining Xerox in 1993, Mr. Romeril had been Group Finance Director at British Telecommunications PLC since 1988. From 1987 to 1988 he was Finance Director at BTR, Plc.

## PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

(a) (1) and (2) The financial statements, independent auditors' reports and Item 8 financial statement schedules being filed herewith or incorporated herein by reference are set forth in the Index to Financial Statements and Schedule included herein.

(3) The exhibits filed herewith or incorporated herein by reference are set forth in the Index of Exhibits included herein.

(b) No Current Reports on Form 8-K were filed during the last quarter of the period covered by this Report.

(c) The management contracts or compensatory plans or arrangements listed in the Index of Exhibits that are applicable to the executive officers named in the Summary Compensation Table which appears in Registrant's 1996 Proxy Statement are preceded by an asterisk (*).

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

XEROX CORPORATION

By: /s/ Barry D. Romeril_________
Executive Vice President and
Chief Financial Officer

March 28, 1996

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

March 28, 1996

| Signature | Title |
|---|---|
| Principal Executive Officer: | |
| Paul A. Allaire | /s/ Paul A. Allaire______________ |
| | Chairman, Chief Executive Officer and Director |
| Principal Financial Officer: | |
| Barry D. Romeril | /s/ Barry D. Romeril_____________ |
| | Executive Vice President and Chief Financial Officer |
| Principal Accounting Officer: | |
| Philip D. Fishbach | /s/ Philip D. Fishbach___________ |
| | Vice President and Controller |
| Directors: | |
| /s/ Robert A. Beck | Director |
| /s/ B. R. Inman | Director |
| /s/ Yotaro Kobayashi | Director |
| /s/ Ralph S. Larsen | Director |
| /s/ John D. Macomber | Director |
| /s/ George J. Mitchell | Director |
| /s/ N. J. Nicholas, Jr. | Director |
| /s/ John E. Pepper | Director |
| /s/ Martha R. Seger | Director |
| /s/ Thomas C. Theobald | Director |

Report of Independent Auditors

To the Board of Directors and Shareholders of Xerox Corporation

Under date of January 24, 1996, we reported on the consolidated balance sheets of Xerox Corporation and consolidated subsidiaries as of December 31, 1995 and 1994 and the related consolidated statements of income and cash flows for each of the years in the three-year period ended December 31, 1995, as contained in the Xerox Corporation 1995 Annual Report to Shareholders on pages 32, 41, 46, and 54-77. These consolidated financial statements and our report thereon are incorporated by reference in the 1995 Annual Report on Form 10-K. In connection with our audits of the aforementioned consolidated financial statements, we also have audited the related financial statement schedule listed in the accompanying index. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement schedule based on our audits.

In our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG PEAT MARWICK LLP

Stamford, Connecticut
January 24, 1996

Index to Financial Statements and Schedule

Financial Statements:

Consolidated statements of income of Xerox Corporation and subsidiaries for each of the years in the three-year period ended December 31, 1995

Consolidated balance sheets of Xerox Corporation and subsidiaries as of December 31, 1995 and 1994

Consolidated statements of cash flows of Xerox Corporation and subsidiaries for each of the years in the three-year period ended December 31, 1995

Notes to consolidated financial statements

Report of Independent Auditors

Quarterly Results of Operations (unaudited)

The above consolidated financial statements, related notes, report thereon and the quarterly results of operations which appear on pages 32, 41, 46, 54-77, 78, and 79 of the Company's 1995 Annual Report to Shareholders are hereby incorporated by reference in this document.

Commercial and Industrial (Article 5) Schedule:

II - Valuation and qualifying accounts

All other schedules are omitted as they are not applicable, or the information required is included in the financial statements or notes thereto.

SCHEDULE II

Valuation and Qualifying Accounts
Year ended December 31, 1995, 1994 and 1993

| (in millions) | Balance at beginning of period | Additions charged to costs and expenses | Deductions, net of recoveries | Balance at end of period |
|---|---|---|---|---|
| 1995 | | | | |
| Allowance for Losses on: | | | | |
| Accounts Receivable | $ 79 | $ 81 | $ 71 | $ 89 |
| Finance Receivables | 319 | 227 | 224 | 322 |
| Deferred Tax Valuation Allowance | 34 | - | 14 | 20 |
| | $432 | $308 | $309 | $431 |
| 1994 | | | | |
| Allowance for Losses on: | | | | |
| Accounts Receivable | $ 62 | $ 70 | $ 53 | $ 79 |
| Finance Receivables | 300 | 182 | 163 | 319 |
| Deferred Tax Valuation Allowance | 34 | - | - | 34 |
| | $396 | $252 | $216 | $432 |
| 1993 | | | | |
| Allowance for Losses on: | | | | |
| Accounts Receivable | $ 68 | $ 51 | $ 57 | $ 62 |
| Finance Receivables | 275 | 199 | 174 | 300 |
| Deferred Tax Valuation Allowance | - | 34 | - | 34 |
| | $343 | $284 | $231 | $396 |

Index of Exhibits

Document and Location

(3) (a) (1) Restated Certificate of Incorporation of Registrant filed by the Department of State of New York on June 10, 1988.

Incorporated by reference to Exhibit 3(a) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 1988.

(2) Certificate of Amendment dated July 7, 1989 to the Restated Certificate of Incorporation.

Incorporated by reference to Exhibit 3(a) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 1989.

(3) Certificate of Amendment dated October 10, 1994 to the Restated Certificate of Incorporation.

Incorporated by reference to Exhibit 3(a)(3) to Registrant's Annual Report on Form 10-K for the Year Ended December 31, 1994.

(4) Certificate of Amendment dated October 19, 1995 to the Restated Certificate of Incorporation.

(b) By-Laws of Registrant, as amended through May 29, 1991.

Incorporated by reference to Exhibit 3(b)(2) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 1991.

(4) (a) Indenture dated as of January 15, 1990 between Registrant and BankAmerica National Trust Company (as successor in interest to Security Pacific National Trust Company (New York)) relating

to unlimited amounts of debt securities which may be issued from time to time by Registrant when and as authorized by or pursuant to a resolution of Registrant's Board of Directors.

Incorporated by reference to Exhibit 4(a) to Registration No. 33-33150.

(b) Indenture dated as of December 1, 1991 between Registrant and Citibank, N.A. relating to unlimited amounts of debt securities which may be issued from time to time by Registrant when and as authorized by or pursuant to a resolution of Registrant's Board of Directors.

Incorporated by reference to Exhibit 4(a) to Registration No. 33-44597.

(c) Indenture dated as of March 1, 1988, as supplemented by the First Supplemental Indenture dated as of July 1, 1988, between Xerox Credit Corporation (XCC) and The First National Bank of Chicago relating to unlimited amounts of debt securities which may be issued from time to time by XCC when and as authorized by XCC's Board of Directors or the Executive Committee of the Board of Directors.

Incorporated by reference to Exhibit 4(a) to XCC's Registration Statement No. 33-20640 and to Exhibit 4(a)(2) to XCC's Current Report on Form 8-K dated July 13, 1988.

(d) Indenture dated as of March 1, 1989, as supplemented by the First Supplemental Indenture dated as of October 1, 1989, between XCC and Citibank, N.A. relating to unlimited amounts of debt securities which may be issued from time to time by XCC when and as authorized by XCC's Board of Directors or Executive Committee of the Board of Directors.

Incorporated by reference to Exhibit 4(a) to XCC's Registration Statement No. 33-27525 and to Exhibit 4(a)(2) to XCC's Registration Statement No. 33-31367.

(e) Indenture dated as of October 1, 1991, as supplemented by the First Supplemental Indenture dated as of May 1, 1992, between XCC and Citibank, N.A. relating to unlimited amounts of debt securities which may be issued from time to time by XCC when and as authorized by XCC's Board of Directors or Executive Committee of the Board of Directors.

Incorporated by reference to Exhibit 4(a) to XCC's Registration Statement No. 33-43470.

(f) Indenture dated as of May 1, 1994, between XCC and State Street Bank and Trust Company (formerly, The First National Bank of Boston) relating to unlimited amounts of debt securities which may be issued from time to time by XCC when and as authorized by XCC's Board of Directors or Executive Committee of the Board of Directors.

Incorporated by reference to Exhibit 4(a) to XCC's Registration Statement No. 33-53533 and to Exhibits 4(a)(1) and 4(a)(2) to XCC's Registration Statement No. 33-43470.

(g) Indenture dated as of October 2, 1995, between XCC and State Street Bank and Trust Company relating to unlimited amounts of debt securities which may be issued from time to time by XCC when and as authorized by XCC's Board of Directors or Executive Committee of the Board of Directors.

Incorporated by reference to Exhibit 4(a) to XCC's Registration Statement No. 33-61481.

(h) Instruments with respect to long-term debt where the total amount of securities authorized thereunder does not exceed 10% of the total assets of the Registrant and its subsidiaries on a consolidated basis have not been filed. The Registrant agrees to furnish to the Commission a copy of each such instrument upon request.

(10) The management contracts or compensatory plans or arrangements listed below that are applicable to the executive officers named in the Summary Compensation Table which appears in Registrant's 1996 Proxy Statement are preceded by an asterisk (*).

*(a) Registrant's 1976 Executive Long-Term Incentive Plan, as amended through February 4, 1991.

Incorporated by reference to Exhibit (10)(a) to the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 1991.

*(b) Registrant's 1991 Long-Term Incentive Plan, as amended through July 15, 1991.

Incorporated by reference to Exhibit 10(b) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 1991.

(c) Registrant's Retirement Income Plan for Directors, as amended through October 2, 1989.

Incorporated by reference to Exhibit 10(n) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 1989.

*(d) Description of Registrant's Annual Performance Incentive Plan.

*(e) Registrant's 1993 Restatement of Unfunded Retirement Income Guarantee Plan.

Incorporated by reference to Exhibit 10(e) to Registrant's Annual Report on Form 10-K for the year ended December 31, 1993.

(f) Consent Order To Cease and Desist. In the Matter of Xerox Corporation, Before the Federal Trade Commission, Docket No. 8909 dated 3/29/75.

Incorporated by reference to Exhibit I to Registrant's Report on Form 8-K for July 1975.

*(g) 1993 Restatement of Registrant's Unfunded Supplemental Retirement Plan.

Incorporated by reference to Exhibit 10(g) to Registrant's Annual Report on Form 10-K for the year ended December 31, 1993.

(h) Registrant's 1981 Deferred Compensation Plan, 1985 Restatement, as amended through April 2, 1990.

Incorporated by reference to Exhibit 10(h) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 1990.

(i) Registrant's Restricted Stock Plan for Directors, as amended through February 7, 1994.

Incorporated by reference to Exhibit 10(i) to Registrant's Annual

Report on Form 10-K for the Year Ended December 31, 1993.

*(j) Form of severance agreement entered into and to be entered into with various executive officers.

Incorporated by reference to Exhibit 10(j) to Registrant's Quarterly Report on Form 10-Q for the Quarter ended June 30, 1989.

*(k) Registrant's Contributory Life Insurance Plan.

Incorporated by reference to Exhibit 10(s) to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 1989.

(l) 1996 Amendment and Restatement of Registrant's 1989 Deferred Compensation Plan for Directors.

*(m) 1993 Amendment and Restatement of Registrant's 1989 Deferred Compensation Plan for Executives.

Incorporated by reference to Exhibit 10(m) to Registrant's Annual Report on Form 10-K for the year ended December 31, 1993.

*(n) Executive Performance Incentive Plan.

Incorporated by reference to Registrant's Notice of the 1995 Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A.

(o) Stock Purchase Agreement dated as of January 17, 1996 among Registrant, Xerox Financial Services, Inc. (XFSI) and New Talegen Holdings Corporation and Talegen Acquisition Corporation. This Agreement is for the sale of Talegen Holdings, Inc. and its subsidiaries. Copies of the exhibits to the Agreement will be furnished upon request. Copies of the schedules to the Agreement will be furnished to the Commission upon request.

(p) Stock Purchase Agreement dated as of January 17, 1996 among Registrant, XFSI and TRG Acquisition Corporation. This Agreement is for the sale of The Resolution Group, Inc. Copies of the exhibits to the Agreement will be furnished upon request. Copies of the schedules to the Agreement will be furnished to the Commission upon request.

(11) Statement re computation of per share earnings.

(12) Computation of Ratio of Earnings to Fixed charges.

(13) Pages 32 through 81 of Registrant's 1995 Annual Report to Shareholders.

(21) Subsidiaries of the Registrant.

(23) Consent of KPMG Peat Marwick LLP.

(28) P Schedule P of Annual Statements to State Regulatory Authorities.

Incorporated by reference to Exhibit (28) on the Form SE of Registrant dated March 26, 1996.

EXHIBIT 3(a)(4)

Certificate of Amendment
of the
Certificate of Incorporation
of
Xerox Corporation
Under Section 805 of the Business Corporation Law

We, the undersigned, Eunice M. Filter, Vice President and Martin S. Wagner, Assistant Secretary of Xerox Corporation (the "Corporation") hereby certify that:

1. The name of the Corporation is "XEROX CORPORATION". The name under which the Corporation was formed is "THE HALOID COMPANY".

2. The Certificate of Incorporation was filed by the Department of State on April 18, 1906 under the name The Haloid Company.

3. The Certificate of Incorporation of the Corporation is hereby being amended pursuant to Section 805 of the BCL to (a) reduce the number of authorized shares of Cumulative Preferred Stock, par value $1.00 per share, of the Corporation ("Cumulative Preferred Stock") and (b) reduce the stated capital of the Corporation resulting from the elimination, pursuant to Section 515(e) of the BCL and subdivision 4 of Article FOURTH of the Certificate of Incorporation of the Corporation, of 1,000,000 shares of Cumulative Preferred Stock (consisting of 1,000,000 shares of the Corporation's $3.6875 Ten-Year Sinking Fund Preferred Stock, a series of Cumulative Preferred Stock) heretofore acquired by the Corporation by sinking fund redemptions. Subdivision 4 of Article FOURTH of the Certificate of Incorporation of the Corporation prohibits the reissue of any shares of Cumulative Preferred Stock of any series redeemed or retired pursuant to a sinking fund and requires that such shares be eliminated in the manner provided by law from the authorized capital stock of the Corporation.

4. The lead-in paragraph of Article FOURTH of the Certificate of Incorporation of the Corporation reads as follows:

"FOURTH: The aggregate number of shares which the Corporation shall have the authority to issue is 350,000,000 shares of Common Stock, of the par value of $1.00 each (hereinafter referred to as "Common Stock"), 600,000 shares of Class B Stock of the par value of $1.00 each (hereinafter referred to as "Class B Stock"), and 23,543,067 shares of Cumulative Preferred Stock, of the par value of $1.00 each (hereinafter referred to as "Cumulative Preferred Stock")."

5. The lead-in paragraph of Article FOURTH of the Certificate of Incorporation of the Corporation is hereby amended to read as follows:

"FOURTH: The aggregate number of shares which the Corporation shall have the authority to issue is 350,000,000 shares of Common Stock, of the par value of $1.00 each (hereinafter referred to as "Common Stock"), 600,000 shares of Class B Stock of the par value of $1.00 each (hereinafter referred to as "Class B Stock"), and 22,543,067 shares of Cumulative Preferred Stock, of the par value of $1.00 each (hereinafter referred to as "Cumulative Preferred Stock")."

6. The stated capital of the Corporation is hereby reduced by $1,000,000, the amount represented by the shares of Cumulative Preferred Stock heretofore acquired by the Corporation by optional and sinking fund redemptions and thereafter cancelled or eliminated.

7. The foregoing amendment of the Certificate of Incorporation of the Corporation was authorized by the Board of Directors of the Corporation

at a meeting duly called and held on February 6, 1995.

IN WITNESS WHEREOF, we have subscribed this document on the date set forth below and do hereby affirm, under the penalties of perjury, that the statements contained therein have been examined by us and are true and correct.

Date: October 19, 1995

/s/ Eunice M. Filter
----------------------------
Name: Eunice M. Filter
Title: Vice President

/s/ Martin S. Wagner
----------------------------
Name: Martin S. Wagner
Title: Assistant Secretary

EXHIBIT 10(d)

## Annual Performance Incentive Plan

Under the Annual Performance Incentive Plan, executive officers of the Company may be entitled to receive performance related cash payments provided that annual, Committee-established performance objectives are met. At the beginning of the year, the Executive Compensation and Benefits Committee approves for each officer not participating in the Executive Performance Incentive Plan, an annual incentive target and maximum opportunity expressed as a percentage of annual base salary. The Committee also establishes overall Document Processing threshold, target and maximum measures of performance and associated payment schedules. For 1995, the performance measures are profit before tax (30%), return on assets (20%), cash generation (20%) and customer and employee satisfaction (30%). Additional goals are also established for each officer that includes business unit specific and/or individual performance goals and objectives. The weights associated with each business unit specific or individual performance goal and objective used vary and range from 10 percent to 55 percent of the total. Actual performance payments are subject to approval by the Committee following the end of the year.

Exhibit 10(l)

As amended through
February 5, 1996

XEROX CORPORATION
1989 DEFERRED COMPENSATION PLAN FOR DIRECTORS
1996 AMENDMENT AND RESTATEMENT

Preamble. This Plan is a private unfunded nonqualified deferred compensation arrangement for Directors and all rights shall be governed by and construed in accordance with the laws of New York, except where preempted by federal law. It is intended to provide a vehicle for setting aside funds for retirement.

Section 1. Effective Date. The original effective date of the Plan is January 1, 1989. The effective date of this amendment and restatement is May 16, 1996.

Section 2. Eligibility. Any Director of Xerox Corporation (the "Company") who is not an officer or employee of the Company or a subsidiary of the Company is eligible to participate in the Plan. A participant who terminates an election to defer receipt of compensation is not eligible to participate again in the Plan until twelve months after the effective date of such termination.

Section 3. Deferred Compensation Account. There shall be established for each participant a deferred compensation account.

Section 4. Amount of Deferral.

(a) A participant may elect to defer receipt of all or a specified part, expressed either in terms of a fixed dollar amount or a percentage, of the cash compensation otherwise payable to the participant for serving on the Company's Board of Directors or committees of the Board of Directors. Any amount deferred is credited to the participant's deferred compensation account on the date such amount is otherwise payable.

(b) In addition to the foregoing, there shall be credited to the deferred compensation accounts of each person who is serving as a Director on May 15, 1996 a sum computed by the Company as the present value of his or her accrued benefit under the Company's Retirement Income Plan For Directors, if any, as of such date and each such Director shall be given notice of such amount. The amount so computed shall be final and binding on the Company and each such Director. Within 30 days of giving such notice, each such Director shall make an election on a form provided by the Company as to the hypothetical investment of such amount and the payment methods as permitted under Sections 6 and 8 hereof as in effect on such date under the administrative rules adopted by the Administrator.

Section 5. Time of Election to Defer. The election to defer will be made prior to the individual's commencement of services as a Director for amounts to be earned for the remainder of the calendar year. In the case of an individual currently serving as a Director, the election to defer must be made prior to December 31, of any year for amounts to be earned in a subsequent calendar year or years. An election to totally terminate deferrals may be made at any time prior to the relevant payment date.

Section 6. Hypothetical Investment. Deferred compensation is assumed to be invested, without charge, in the Balanced Fund, Income Fund, U.S. Stock Fund, International Stock Fund, Small Company Stock Fund or Xerox Stock Fund (the "Funds") established under the Xerox Corporation Profit Sharing and Savings Plan (the "Profit Sharing Plan") as elected by the participant; provided, however, that the Administrator, as hereinafter defined, shall have the right from time to time, without adversely affecting participants'

accruals in deferred compensation accounts, to substitute for the Income Fund other hypothetical fixed return investments for the deferred compensation.

Elections to make hypothetical investments in any one or more of the Funds shall be subject to administrative rules adopted by the Administrator from time to time.

No shares of Xerox stock will ever actually be issued to a participant under the Plan.

Section 7. Value of Deferred Compensation Accounts and Installment Payments. The value of each participant's deferred compensation account shall reflect all amounts deferred, and gains and losses from the hypothetical investments, and shall be determined on the last day of each month (the "Valuation Dates"). Hypothetical investments in the Profit Sharing Plan shall be valued as of the valuation date under such Plan coincident with or last preceding the Valuation Date under this Plan. The value of hypothetical investments not made under the Profit Sharing Plan shall be determined as of each Valuation Date by the best information available to the Administrator.

Section 8. Manner of Electing Deferral. A participant may elect to defer compensation by giving written notice to the Administrator on a form provided by the Company, which notice shall include (1) the amount and/or percentage to be deferred; (2) if more than one is offered under the Plan, the hypothetical investment applicable to the amount deferred; (3) the number of installments for the payment of the deferred compensation; and (4) the date of the first installment payment. A participant may elect a single method of payment for (A) termination of service as a Director, (B) death, (C) disability or (D) while still in service as a Director, or separate methods of payment for each of these events, provided, however, that the amount credited to deferred compensation accounts under Section 4(b) shall not be payable while in service as a Director. The Administrator may adopt rules of general applicability regarding commencement and duration of payments under the Plan which may be elected by participants.

Section 9. Payment of Deferred Compensation. No withdrawal may be made from the participant's deferred compensation account, except as provided under this Section and Sections 10 and 11.

The value of a participant's deferred compensation account is payable in cash in annual installments on February 15 or August 15 following the first occurrence of one of the events elected under Section 8 or following a fixed period after one of such events based on the value of the participant's deferred compensation account as of the second preceding Valuation Date.

Unless otherwise elected by a participant with the written approval of the Administrator, payments of deferred compensation shall be made pursuant to the following formula: the amount of the first payment shall be a fraction of the value of the participant's deferred compensation account on the second preceding Valuation Date, the numerator of which is one and the denominator of which is the total number of installments elected, and the amount of each subsequent payment shall be a fraction of the value on the second Valuation Date preceding each subsequent payment date, the numerator of which is one and the denominator of which is the total number of installments elected minus the number of installments previously paid. There shall be added to each payment determined in accordance with the foregoing, imputed interest for a period of one month at the same annual rate credited to accounts invested in the Income Fund under the Profit Sharing Plan for the month of December or June, as the case may be. Any other payment method selected with the written approval of the Administrator must in all events provide for payments in substantially equal installments.

Section 10. Acceleration of Payment for Hardship.

(a) For Hardship. Upon written approval from the Board of Directors, a participant may be permitted to receive all or part of his accumulated benefits if, in the discretion of the Board of Directors, it is determined that an emergency event beyond the participant's control exists and which

would cause such participant severe financial hardship if the payment of his benefits were not approved. Any such distribution for hardship shall be limited to the amount needed to meet such emergency. A participant who makes a hardship withdrawal cannot reenter the Plan for twelve months after the date of withdrawal.

(b) Upon a Change in Control. Within 5 days following the occurrence of a change in control of the Company (as hereinafter defined), each participant shall be entitled to receive a lump sum payment equal to the value of his deferred compensation account. For purposes hereof, a "change in control of the Company" shall be deemed to have occurred if (A) any "person", as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") other than the Company, any trustee or other fiduciary holding securities under an employee benefit plan of the Company, or any company owned, directly or indirectly, by the shareholders of the Company in substantially the same proportions as their ownership of stock of the Company, is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 20 percent or more of the combined voting power of the Company's then outstanding securities; or (B) during any period of two consecutive years, individuals who at the beginning of such period constitute the Board, including for this purpose any new director (other than a director designated by a person who has entered into an agreement with the Company to effect a transaction described in this Section) whose election or nomination for election by the Company's shareholders was approved by a vote of at least two-thirds of the directors then still in office who were directors at the beginning of the period or whose election or nomination for election was previously so approved, cease for any reason to constitute a majority thereof.

Section 11. Other Penalized Withdrawals. Notwithstanding the provisions of Sections 9 and 10, a participant may be permitted to receive all or part of his accumulated benefits at any time provided that (A) the Administrator approves such distribution in his or her sole discretion, and (B) the participant forfeits a portion of his account balance equal to a percentage of the amount distributed. The percentage reduction shall be the greater of (A) six percent, or (B) a percentage equal to one-half of the prime interest rate, as determined by the Administrator.

Section 12. Time Of Hypothetical Investment. The amount in the participant's deferred compensation account as of each Valuation Date which has not been previously deemed invested shall be deemed invested in a hypothetical investment on such date, based on the value of the hypothetical investment on such date.

Section 13. Participant's Rights Unsecured. The benefits payable under this Plan shall be unfunded. Consequently, no assets shall be segregated for purposes of this Plan and placed beyond the reach of the Company's general creditors. The right of any participant to receive future installments under the provisions of the Plan shall be an unsecured claim against the general assets of the Company.

Section 14. Statement of Account. Statements will be sent to each participant during February and August and more frequently if the Administrator so determines as to the value of their deferred compensation accounts as of the end of December and June, respectively.

Section 15. Assignability. No right to receive payments hereunder shall be transferable or assignable by a participant, except by will or by the laws of descent and distribution.

In the event of a participant's death without having an election under Section 8 (B) in effect regarding payment of his account after death, the value of the participant's deferred compensation account shall be determined as of the Valuation Date coincident with or immediately following death and such amount shall be paid in a single payment to the participant's estate (a) the first January 15 or July 15 following such Valuation Date, or (b) if such payment cannot be made at the time specified in (a), it shall be made within

30 days after the participant's death. There shall be added to such payment, interest for the full calendar months elapsed following such Valuation Date to the payment date at the same annual rate credited to accounts invested in the Income Fund under the Profit Sharing Plan for the month of such Valuation Date.

In the event of a participant's death after installment payments have commenced to be paid, the balance of the deferred compensation account shall be paid to the participant's estate.

Section 16. Business Days. In the event any date specified herein falls on a Saturday, Sunday or legal holiday, such date shall be deemed to refer to the next business day thereafter.

Section 17. Administration. The Plan shall be administered by the Vice President of the Company having responsibility for human resources (the "Administrator"). The Administrator shall have the authority to adopt rules and regulations for carrying out the plan, and interpret, construe and implement the provisions of the Plan.

Section 18. Amendment. The Plan may at any time or from time to time be amended, modified or terminated by the Board of Directors or the Executive Committee of the Board of Directors of the Company. Upon termination the Administrator in his or her sole discretion may pay out account balances to participants. No amendment, modification or termination shall, without the consent of a participant, adversely affect such participant's accruals in his/her deferred compensation account.

Exhibit 10(o)

# STOCK PURCHASE AGREEMENT

dated as of January 17, 1996

among

XEROX CORPORATION

XEROX FINANCIAL SERVICES, INC.

and

NEW TALEGEN HOLDINGS CORPORATION

and

TALEGEN ACQUISITION CORPORATION

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| | |
|---|---|
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# STOCK PURCHASE AGREEMENT

STOCK PURCHASE AGREEMENT dated as of January 17, 1996 among Xerox Corporation, a New York corporation ("Parent"), Xerox Financial Services, Inc., a Delaware corporation and a wholly-owned subsidiary of Parent ("Seller"), New Talegen Holdings Corporation, a Delaware corporation ("Holdings"), and Talegen Acquisition Corporation, a Delaware corporation and a wholly-owned subsidiary of Holdings ("Buyer").

## RECITALS

Seller is the beneficial and record owner of 1,000 shares of common stock, par value $1.00 per share, of Talegen Holdings, Inc., a Delaware corporation (the "Company"), constituting all of the issued and outstanding capital stock (the "Stock") of the Company.

Buyer desires to purchase from Seller, and Seller desires to sell to Buyer, all of the Stock subject to the terms and conditions of this Agreement.

Parent is the sole stockholder of Seller and desires that Seller sell to Buyer all of the Stock, subject to the terms and conditions of this Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements contained herein and for other good and valuable consideration the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:follows:

## ARTICLE I

## DEFINITIONS

1.1 Defined Terms. As used herein, the terms below shall have the following meanings:

"Affiliate" shall mean a Person that directly or indirectly through one or more intermediaries controls, is controlled by or is under common control with the Person specified. For purposes of this definition and the definition of "Subsidiary" set forth below, the term "control" (including the terms "controlling," "controlled by" and "under common control with") of a Person means the possession, direct or indirect, of the power to (i) vote 50% or more of the voting securities of such Person or (ii) direct or cause the direction of the management and policies of such Person, whether by contract or otherwise.

"Agreement" shall mean this Stock Purchase Agreement (together with all schedules and exhibits referenced herein), as amended, modified or

supplemented from time to time.

"Ancillary Agreements" shall mean, collectively, the Ridge Re Endorsements, the Guarantees, the Tax Agreement and the TOPrS Side Letter.

"Apprise" shall mean Apprise Corp., a New Jersey corporation and a direct wholly-owned subsidiary of the Company.

"Balance Sheet Date" shall mean June 30, 1995.

"Cash Equivalents" shall mean (a) securities with maturities of one year or less from the date of acquisition issued or fully guaranteed or insured by the United States Government or any agency thereof, (b) certificates of deposit and eurodollar time deposits with maturities of one year or less from the date of acquisition and overnight bank deposits of any commercial bank having capital and surplus in excess of $500,000,000, (c) repurchase obligations of any commercial bank satisfying the requirements of clause (b) of this definition, having a term of not more than 30 days with respect to securities issued or fully guaranteed or insured by the United States government, (d) commercial paper of a domestic issuer rated at least A-2 by S&P or P-2 by Moody's, (e) securities with maturities of one year or less from the date of acquisition issued or fully guaranteed by any state, commonwealth or territory of the United States, by any political subdivision or taxing authority of any such state, commonwealth or territory or by any foreign government, the securities of which state, commonwealth, territory, political subdivision, taxing authority or foreign government (as the case may be) are rated at least A by S&P or A by Moody's, (f) securities with maturities of one year or less from the date of acquisition backed by standby letters of credit issued by any commercial bank satisfying the requirements of clause (b) of this definition or (g) shares of money market mutual or similar funds which invest exclusively in assets satisfying the requirements of clauses (a) through (f) of this definition.

"CFI" shall mean Crum & Forster Holdings, Inc., a Delaware corporation and a direct wholly-owned subsidiary of the Company.

"CGI" shall mean Coregis Group, Inc., a Delaware corporation and a direct wholly-owned subsidiary of the Company.

"Closing Date" shall mean the date on which the Closing occurs.

"Code" shall have the meaning ascribed in the Tax Agreement.

"Company GAAP Financial Statements" shall mean the audited Consolidated Balance Sheets of the Company (or its predecessors) as of December 31, 1994 and 1993 and the Consolidated Statements of Operations, Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of the Company (or its predecessors) for each of the three fiscal years included in the three-year period ended December 31, 1994, prepared in accordance with GAAP, together with the notes thereon and the related reports of KPMG Peat Marwick LLP.

"Company Interim Financial Statements" shall mean the unaudited Consolidated Balance Sheets and the unaudited Consolidated Statements of Operations, Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of the Company for the nine-month periods ended September 30, 1994 and 1995, together with the notes thereon.

"Constitution Re" shall mean Constitution Re Corporation, a Delaware corporation.

"Constitution Re Sale" shall mean the sale of the capital stock of Constitution Re pursuant to the Stock Purchase Agreement dated December 16, 1994 between the Company and EXOR America Inc., as amended by an amendment dated December 22, 1994.

"Contracts" shall mean all agreements, contracts, commitments and undertakings (other than contracts of insurance or reinsurance or retrocession

agreements) to which the Company or any of the Subsidiaries is a party, an obligor or a beneficiary and (i) the performance or non-performance of which is individually or, with respect to any related series of agreements, in the aggregate, material to the Company and the Subsidiaries, taken as a whole, or (ii) which provide for an aggregate purchase price or payments of more than $1,000,000 under any agreement during any two-year period (or $1,000,000 in the aggregate, during any two-year period, in the case of any related series of agreements).

"Convention Statements" shall mean (i) the annual convention statements and the quarterly statement of each Insurance Subsidiary as filed with the insurance regulatory authorities in its jurisdiction of domicile for the years ended December 31, 1992, 1993 and 1994 and for the quarterly period ended September 30, 1995, and (ii) the annual convention statements of Ridge Re as filed with the insurance regulatory authorities in Bermuda for the period from December 14, 1992 to December 31, 1993 and for the year ended December 31, 1994.

"Credit Corp." shall mean Xerox Credit Corporation, a Delaware corporation and a wholly-owned subsidiary of Seller.

"Crostex/Camfex Contracts" shall mean all contracts, agreements or arrangements of the Company or any Subsidiary relating to the real property and improvements located at (i) 255 California Street, San Francisco, California, (ii) 5724 W. Los Positos Blvd., Pleasonton, California, (iii) 299 Madison Avenue, Morris Township, New Jersey, (iv) 305 Madison Avenue, Morris Township, New Jersey and (v) 4040 North Central Expressway, Dallas, Texas, including, without limitation, any notes held by the Company or any Subsidiary (the "Crostex/Camfex Purchase Money Notes").

"Debentures" shall mean the debentures to be issued pursuant to the Indenture.

"Encumbrances" shall mean any claim, lien (statutory or other), pledge, option, charge, easement, security interest, right-of-way, encroachment, encumbrance, mortgage, or other rights of third parties.

"Environmental Laws" shall mean any and all applicable Federal, state or local laws or regulations relating to the protection of the environment or of human health as it may be affected by the environment.

"Environmental Permit" shall mean any license, permit, order, consent, approval, registration, authorization, qualification or filing required under any Environmental Law.

"Environmental Report" shall mean any report, study, assessment, audit, or other similar document that addresses any issue of actual or potential noncompliance with, or actual or potential liability under, any Environmental Law that may in any way affect the Company or any Subsidiary other than to the extent such document addresses any issue of actual or potential noncompliance with, or actual or potential liability under, any Environmental Law by reason of any policy of insurance, reinsurance, indemnity, guaranty or assumption of liability of any party entered into by the Company or any Insurance Subsidiary.

"Envision" shall mean Envision Claims Management Corporation, a New Jersey corporation and a direct wholly-owned subsidiary of TRG.

"Excluded Activities" shall mean, with respect to the Company and the Subsidiaries, activities relating to insurance reserves, claims under, related to or in respect of insurance policies or any disputes related thereto, loss adjustments and loss adjustment expenses and reinsurance receivables, provided, however, that "Excluded Activities" shall not be deemed to include any (i) of the matters covered by the representations contained in Section 4.6, 4.9(c), 4.12 (to the extent it applies to Ridge Re) or 4.26 or other representations regarding Ridge Re or the Ridge Re Treaties or Ridge Re Endorsements or (ii) actions, suits, proceedings or claims pending by any governmental or regulatory authority to the extent based upon a violation of

any law, statute, ordinance, rule or regulation.

"Filoli" shall mean Filoli Information Systems Company, a Delaware corporation.

"First Quadrant" shall mean First Quadrant Corp., a New Jersey corporation.

"First Quadrant Asset Sale" shall mean the sale of certain assets of First Quadrant pursuant to an Asset Purchase Agreement dated as of August 11, 1995 between First Quadrant and American Re Asset Management, Inc.

"First Quadrant Final Sale" shall mean the sale of the capital stock of First Quadrant by the Company.

"GAAP" shall mean generally accepted accounting principles in the United States of America in effect from time to time.

"GAAP Subsidiaries" shall mean Apprise, CFI, CGI, Envision, II and WSG.

"Guarantees" shall mean the guarantees referred to in Section 8.18.

"Holdings Common Stock" shall mean common stock, par value $.01 per share, of Holdings.

"HSR Act" shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

"II" shall mean Industrial Indemnity Holdings, Inc., a Delaware corporation and a direct wholly-owned subsidiary of the Company.

"IIC" shall mean Industrial Indemnity Company, a California corporation and direct wholly-owned subsidiary of II.

"Indenture" shall mean the Indenture to be dated as of the Closing Date between Holdings and the trustee named therein, (i) with the terms of the Debentures, the covenants and events of default set forth in Exhibit A and (ii) otherwise substantially in the form of Exhibit A, except, in the case of clause (ii), for such changes required by the trustee thereunder which do not have an adverse effect on the holders of the Debentures or the Preferred Securities.

"Information Returns" shall have the meaning ascribed in the Tax Agreement.

"Insurance Subsidiaries" shall mean the Subsidiaries listed on Schedule 1.1A.

"Investment Policy" shall mean, with respect to certain Subsidiaries, the policy for each such Subsidiary set forth on Exhibit B.

"KKR" shall mean Kohlberg Kravis Roberts & Co.

"Knowledge of Seller" shall mean (i) with respect to matters relating to Parent or Seller, actual knowledge of any officer of Parent, Seller or Ridge Re set forth in Schedule 1.1B, and (ii) with respect to any matters relating to the Company or any Subsidiary, actual knowledge of any such officer of Parent or Seller, or the actual knowledge of the persons set forth in Schedule 1.1C.

"Material Adverse Effect" with respect to any Person shall mean a material adverse effect on the business, financial condition, assets or operations of such Person, but shall exclude any effect resulting from general economic conditions.

"Materials of Environmental Concern" shall mean any waste, pollutant, or contaminant or substance (including, without limitation, petroleum or petroleum products, asbestos or asbestos-containing materials, urea-formaldehyde insulation, polychlorinated biphenyls, odors, radioactivity, and electro-magnetic fields) regulated by or under, or which may otherwise give

rise to liability under, any Environmental Law.

"Moody's" shall mean Moody's Investors Service, Inc.

"1992/93 Restructuring" shall mean the restructuring of the Company and its subsidiaries pursuant to the Restructuring Agreement dated as of September 3, 1993 among Seller, Ridge Re, the Company and certain of the Subsidiaries.

"Permits" shall mean all licenses, permits, orders, consents, approvals, registrations, authorizations, qualifications and filings with and under all Federal, state, local or foreign laws and governmental or regulatory bodies and all industry or other non-governmental self-regulatory organizations (including, without limitation, Environmental Permits).

"Person" shall mean an individual, a partnership, a joint venture, a corporation, a business trust, a limited liability company, a trust, an unincorporated organization, a government or any department or agency thereof or any other entity.

"Preferred Securities" shall mean the Trust Originated Preferred Securities to be issued pursuant to the Trust Agreement.

"Qualified Transferee" shall mean a corporation (or the wholly-owned direct or indirect subsidiary thereof) which, as of the date of the consummation of a sale pursuant to Section 9.8, is an insurance company engaged in the business of reinsurance and has at least $2 billion in assets and a rating of "A+" or better by A.M. Best.

"Ridge Re" shall mean Ridge Reinsurance Limited, a Bermuda corporation and a wholly-owned subsidiary of Seller.

"Ridge Re Endorsements" shall mean the endorsements to the Ridge Re Treaties referred to in Section 8.17.

"Ridge Re GAAP Financial Statements" shall mean the audited Consolidated Balance Sheets of Ridge Re as of December 31, 1994 and 1993 and the related Statements of Operations and Retained Earnings and Cash Flows for the year ended December 31, 1994 and the period from December 14, 1992 to December 31, 1993, prepared in accordance with GAAP, together with the notes thereon and the related reports of KPMG Peat Marwick LLP.

"Ridge Re Interim Financial Statements" shall mean the unaudited Consolidated Balance Sheet of Ridge Re as of September 30, 1995, and the related Statements of Operations and Retained Earnings for the nine-month periods ended September 30, 1994 and September 30, 1995.

"Ridge Re Treaties" shall mean the agreements, as amended by the applicable Endorsement No. 1 thereto, contained in Schedule 1.1D.

"S&P" shall mean Standard and Poor's Rating Group.

"Securities" shall mean (a) the Preferred Securities and (b) any shares of Holdings Common Stock purchased by Seller in accordance with Section 11.3.

"Statutory Accounting Principles" shall mean, as applied to any Subsidiary, the statutory accounting practices prescribed or permitted by the jurisdiction of domicile of such Subsidiary.

"Subsidiaries" shall mean all corporations, partnerships, joint ventures or other entities which the Company controls, directly or indirectly through one or more intermediaries. See definition of "Affiliate" in this Section 1.1 for the meaning of "control."

"Subsidiary GAAP Financial Statements" shall mean the audited Consolidated Balance Sheets of each of the GAAP Subsidiaries as of December 31, 1994 and December 31, 1993 and the Consolidated Statements of Operations, Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of each such Subsidiary for each of the three fiscal years included in the

three-year period ended December 31, 1994 (except 1992 financial statements for Apprise and Envision), prepared in accordance with GAAP together with the notes thereon and the related reports of KPMG Peat Marwick LLP.

"Subsidiary Interim Financial Statements" shall mean the unaudited Consolidated Balance Sheets of each of the GAAP Subsidiaries as of September 30, 1995, and the unaudited Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of each such Subsidiary for the nine-month periods ended September 30, 1994 and 1995, together with the notes thereon.

"Tax Agreement" shall mean the Tax Allocation and Indemnification Agreement dated as of the date hereof among Parent, Seller, the Company, Holdings and Buyer.

"Tax Returns" shall have the meaning ascribed in the Tax Agreement.

"Taxes" shall have the meaning ascribed in the Tax Agreement.

"Third Party Amount" shall mean any amount paid by the transferee (which may be Seller or any of its Affiliates (other than the Company or any Subsidiary)) to the Company or the Subsidiaries of all or a portion of the Seller Notes or Leesburg Training Facility, as the case may be, pursuant to Sections 6.12 or 6.13.

"Third Party Expenses" shall mean all expenses paid or payable by Buyer or Holdings to other Persons in connection with the transactions contemplated by this Agreement, the Ancillary Agreements and the Financing Documents other than expenses contingent upon a payment to Buyer or Holdings or which are not payable unless there has been a breach of this Agreement by Parent, Seller, the Company or any Subsidiary, but shall in no event include any amount payable to KKR or its Affiliates (other than to Am-Re Consultants, Inc. in connection with reserve analyses) or any officer, director or employee of the Company or the Subsidiaries.

"TOPrS Side Letter" shall mean the letter among an investment partnership affiliated with Holdings, Holdings and Seller to be dated the Closing Date, substantially in the form of Exhibit C.

"TRG" shall mean The Resolution Group, Inc., a Delaware corporation and a direct wholly-owned subsidiary of Seller.

"TRG Acquisition" shall mean TRG Acquisition Corporation, a Delaware corporation.

"TRG Agreement" shall mean the Stock Purchase Agreement dated as of the date hereof among Parent, Seller and TRG Acquisition, as amended, modified or supplemented from time to time, which contemplates that TRG Acquisition will purchase all of the outstanding capital stock of TRG from Seller, subject to the terms and conditions thereof.

"TRG Dividend Replacement Amount" shall mean an amount equal to (i) $15,000,000 plus (ii) $7,500,000 for each calendar quarter from July 1, 1996 to the Closing Date, provided that if the Closing Date is in the middle of a calendar quarter the amount for such calendar quarter shall be pro rated from the first day of such calendar quarter to the Closing Date based on actual number of days elapsed.

"Trust" shall mean the Delaware business trust referred to in the Trust Agreement.

"Trust Agreement" shall mean the Amended and Restated Trust Agreement to be dated the Closing Date between Holdings and the trustees named therein (the "Trustees"), (i) with the terms of Preferred Securities set forth in Exhibit D and (ii) otherwise substantially in the form of Exhibit D, except, in the case of clause (ii), for such changes required by the Property Trustee (as defined in the Trust Agreement) which do not have an adverse effect on the holders of the Debentures or the Preferred Securities.

"Underwriter Letter" shall mean that certain letter dated January 17, 1996 between a nationally recognized underwriter and Buyer stating that such underwriter is highly confident that Buyer will be able to obtain funds referenced therein, before underwriting discounts and commissions, from the sale of subordinated debt of Buyer.

"Underwritten Notes" shall mean the subordinated debt securities of Buyer issued by Buyer in an offering underwritten by a nationally recognized underwriter pursuant to the Underwriter Letter.

"Viking" shall mean Viking Insurance Holdings, Inc., a Delaware corporation.

"Viking Sale" shall mean the sale of the capital stock of Viking pursuant to a Stock Purchase Agreement dated as of April 26, 1995 between the Company and Guaranty National Corporation.

"WSG" shall mean Westchester Specialty Group, Inc., a Delaware corporation and a direct wholly-owned subsidiary of the Company.

1.2 Other Defined Terms. The following terms shall have the meanings defined for such terms in the Sections set forth below:

| Term | Section |
|---|---|
| "AARG" | 4.7 |
| "Actions" | 4.13 |
| "A.M. Best" | 6.15 |
| "Assets" | 4.8 |
| "Closing" | 3.1 |
| "Common Securities" | 2.4 |
| "Company Plans" | 4.21 |
| "Confidentiality Agreement" | 6.4 |
| "Crostex/Camfex Purchase Money Notes" | 1.1 |
| "Damages" | 10.2 |
| "ERISA" | 4.21 |
| "ESOP" | 9.5 |
| "Excluded Business" | 10.2 |
| "Exchange Act" | 4.11 |
| "Financing" | 5.3 |
| "Financing Documents" | 5.3 |
| "Indemnitee" | 10.3 |
| "Indemnitor" | 10.3 |
| "Indenture" | 6.19 |
| "Intellectual Property" | 4.20 |
| "Leesburg Training Facility Amount" | 6.13 |
| "Leesburg Training Facility" | 6.13 |
| "Liabilities" | 4.14 |
| "Long Term Incentive Program" | 4.7 |
| "Notice" | 10.3 |
| "Personnel" | 4.13 |
| "Section 4.5 Subsidiaries" | 4.5 |
| "Securities Act" | 4.3 |
| "Seller Notes" | 4.23 |
| "Subsidiary Credit Agreements" | 4.14 |
| "TRG Contributed Dividends" | 6.20 |
| "Trustees" | 1.1 |

1.3 Other Definitional Provisions. (a) The words "hereof", "herein" and "hereunder" and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement, and Section, Schedule and Exhibit references are to this Agreement unless otherwise specified.

(b) The meanings given to terms defined herein shall be equally applicable to both the singular and plural forms of such terms.

## ARTICLE II

## PURCHASE AND SALE OF STOCK AND PREFERRED SECURITIES

2.1 Transfer of Stock. Upon the terms and subject to the conditions contained herein, Seller will sell, convey, transfer, assign and deliver to Buyer, and Buyer will acquire from Seller on the Closing Date, all of the Stock for the consideration set forth in Section 2.2.

2.2 Consideration for Stock. Upon the terms and subject to the conditions contained herein, as consideration for the purchase of the Stock, on the Closing Date Buyer will pay to Seller cash in an amount equal to $1,750,000,000, payable by wire transfer in immediately available funds to an account which Seller will designate in writing to Buyer no less than two business days prior to the Closing Date, subject to adjustment as described in Section 2.7(a).

2.3 Transfer of Debentures. Simultaneously with Buyer making the payment provided for in Section 2.2, (i) Holdings will issue Debentures to Trust in the aggregate principal amount of $450,000,000, subject to adjustment as described in Sections 2.7(a) and 2.7(b), and (ii) Holdings will issue additional Debentures to Trust in an aggregate principal amount equal to the aggregate liquidation amount of the common securities referred to in clause (ii) of Section 2.4.

2.4 Consideration for Debentures. As consideration for the purchase of the Debentures, on the Closing Date, Holdings and Buyer will cause Trust (i) to pay to Holdings cash in an amount equal to $450,000,000, payable by intrabank transfer (at a bank to be mutually agreed) in immediately available funds to an account which Holdings will designate in writing to Trust no less than two business days prior to the Closing Date, subject to adjustment as described in Sections 2.7(a) and 2.7(b), and (ii) to issue and deliver to Holdings common securities of Trust ("Common Securities") with a liquidation amount of 3% of the aggregate liquidation amount of securities of Trust which will be outstanding at Closing (after giving effect to the issuance of Preferred Securities provided for in Section 2.5).

2.5 Transfer of Preferred Securities. Simultaneously with the payments provided for in Sections 2.2 and 2.4, Holdings and Buyer will cause Trust to issue and deliver to Seller, and Seller will acquire from Trust, Preferred Securities with an aggregate liquidation amount of $450,000,000, subject to adjustment as described in Sections 2.7(a) and 2.7(b).

2.6 Consideration for Preferred Securities. As consideration for the purchase of the Preferred Securities, on the Closing Date Seller will pay to Trust cash in an amount equal to $450,000,000, payable by intrabank transfer (at a bank to be mutually agreed) in immediately available funds to an account which Buyer will designate in writing to Seller no less than two business days prior to the Closing Date, subject to adjustment as described in Sections 2.7(a) and 2.7(b).

2.7 Adjustments. (a) If the Closing shall not have occurred on or prior to July 1, 1996, the amount of cash payable by Buyer to Seller pursuant to Section 2.2, the principal amount of Debentures to be issued by Holdings pursuant to Section 2.3, the amount of cash payable by Trust pursuant to Section 2.4, the aggregate liquidation amount of Preferred Securities to be issued by the Trust pursuant to Section 2.5 and the amount of cash payable by Seller pursuant to Section 2.6 shall each be increased by $10,000,000 for each full calendar month until the Closing Date, and with respect to any partial calendar month commencing with July 1, 1996 until the Closing Date, by an amount equal to the product obtained by multiplying $10,000,000 by a fraction the numerator of which is equal to the number of days in such partial month which have elapsed prior to the Closing Date and the denominator of which is equal to the number of calendar days in such month.

(b) To the extent that IIC shall not have paid an extraordinary dividend to II after the date hereof but prior to the Closing Date, the principal amount of Debentures to be issued by Holdings pursuant to Section 2.3, the amount of

cash payable by Trust pursuant to Section 2.4, the aggregate liquidation amount of Preferred Securities to be issued by Trust pursuant to Section 2.5 and the amount of cash payable by Seller pursuant to Section 2.6 shall each be increased by $50,000,000, and to the extent that IIC shall have paid an extraordinary cash dividend of less than $50,000,000 to II after the date hereof but prior to the Closing Date, the principal amount of Debentures to be issued by Holdings pursuant to Section 2.3, the amount of cash payable by Trust pursuant to Section 2.4, the aggregate liquidation amount of Preferred Securities to be issued by Trust pursuant to Section 2.5 and the amount of cash payable by Seller pursuant to Section 2.6 shall each be increased to the extent any such dividend is less than $50,000,000.

## ARTICLE III

## CLOSING

3.1 Closing. The closing of the transactions contemplated herein (the "Closing") shall take place as soon as practicable but in no event later than five business days after satisfaction or waiver of the conditions set forth in Articles VII and VIII, and shall be held at 9:00 a.m. local time on the Closing Date at the offices of Simpson Thacher & Bartlett, 425 Lexington Avenue, New York, New York 10017, unless the parties hereto otherwise agree. The parties agree that the effective time of the Closing for Federal income tax purposes shall be at the close of business on the Closing Date.

3.2 Documents to be Delivered. To effect the transfers referred to in Sections 2.1, 2.3 and 2.5 and the delivery of the consideration described in Sections 2.2, 2.4 and 2.6 hereof, Seller and Buyer shall, and Holdings and Buyer shall cause Trust to, on the Closing Date, deliver the following:

(a) Seller shall deliver to Buyer certificate(s) evidencing the Stock, free and clear of any Encumbrances of any nature whatsoever (except Encumbrances arising as a result of any action taken by Buyer or any of its Affiliates), duly endorsed in blank for transfer or accompanied by stock powers duly executed in blank.

(b) Buyer shall deliver to Seller immediately available funds as provided in Section 2.2.

(c) Holdings shall issue Debentures to Trust as provided in Section 2.3.

(d) Trust shall deliver to Holdings immediately available funds as provided in clause (i) of Section 2.4.

(e) Trust shall deliver to Holdings certificate(s) evidencing Common Securities as provided in clause (ii) of Section 2.4.

(f) Trust shall deliver to Seller certificate(s) evidencing the Preferred Securities as provided in Section 2.5, free and clear of any Encumbrances of any nature whatsoever (except Encumbrances arising as a result of any action taken by Seller or any of its Affiliates) in the form of one or more certificates in the name of Seller.

(g) Seller shall deliver to Trust immediately available funds as provided in Section 2.6.

(h) Seller and Buyer shall each deliver all documents required to be delivered pursuant to Articles VII and VIII.

(i) All instruments and documents executed and delivered to Buyer pursuant hereto shall be in form and substance, and shall be executed in a manner, reasonably satisfactory to Buyer. All instruments and documents executed and delivered to Seller pursuant hereto shall be in form and substance, and shall be executed in a manner, reasonably satisfactory to Seller.

## ARTICLE IV

## REPRESENTATIONS AND WARRANTIES OF PARENT AND SELLER

Parent and Seller hereby represent and warrant to Buyer and Holdings as follows:

4.1 Organization of Seller and Parent. Seller is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business as it is presently being conducted and to own the Stock. Parent is duly organized, validly existing and in good standing under the laws of the State of New York and has full corporate power and authority to conduct its business as it is presently being conducted.

4.2 Organization of the Company. The Company is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business as it is presently being conducted and to own, lease and operate its properties and assets. The Company is duly qualified or otherwise authorized as a foreign corporation to conduct the business conducted by it and is in good standing in each jurisdiction in which such qualification or authorization is necessary under the applicable law and where the failure to be so qualified or otherwise authorized, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Seller has provided to Buyer a complete and correct copy of the certificate of incorporation, bylaws and other organizational documents of the Company and the minute books of the Company. The Company's minute books include copies of minutes of all meetings of the directors or shareholders of the Company held on or after January 1, 1993 and complete and accurate copies of all resolutions passed by the directors or actions by written consent of the shareholders on or after January 1, 1993.

4.3 Capital Stock. The Company has authorized 1,000 shares of common stock, $1.00 par value, 1,000 shares of which are issued and outstanding, and no shares of any other class or series of capital stock are authorized, issued or outstanding. All of the shares of the Stock have been duly and validly authorized and issued, and are fully paid and nonassessable. Seller owns of record and beneficially all of the Stock free and clear of all Encumbrances, including without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to the Stock; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such Stock without registration or qualification under, or in compliance with, applicable Federal or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act of 1933, as amended (the "Securities Act")) or without compliance with applicable insurance laws. There are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding for the purchase of, nor any securities convertible or exchangeable for, any equity interests of the Company. There are no restrictions upon the voting or transfer of any shares of the Stock pursuant to the Company's Certificate of Incorporation or Bylaws or any agreement or other instrument to which the Company or Seller is a party or by which the Company or Seller is bound. Upon consummation of the transactions contemplated by this Agreement, Buyer will acquire from Seller good and marketable title to such Stock, free and clear of all Encumbrances, except Encumbrances arising as a result of any action taken by Buyer or any of its Affiliates; provided that Parent and Seller make no representation regarding the ability of any Person other than Seller to transfer or otherwise dispose of such Stock without registration or qualification under, or in compliance with, applicable Federal securities or state securities or insurance laws.

4.4 Authorization. Each of Parent and Seller has all necessary corporate power and authority to enter into this Agreement and the Ancillary Agreements to which it is or will be a party, and has taken all corporate action necessary to consummate the transactions contemplated hereby and thereby and to perform its obligations hereunder and thereunder. This Agreement and the Tax Agreement have each been duly executed and delivered by each of Seller and Parent. Assuming the due execution of this Agreement and the Tax Agreement by

Holdings and Buyer, each of this Agreement and the Tax Agreement is a legal, valid and binding obligation of each of Seller and Parent enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing. Subject to the occurrence of the Closing, the Guarantees and the TOPrS Side Letter will be duly executed and delivered by Parent and Seller, as applicable, on the Closing Date. Upon execution and delivery by Parent or Seller, as the case may be, each Guarantee and the TOPrS Side Letter will be a legal, valid and binding obligation of such Person enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing, assuming, in the case of the TOPrS Side Letter, the due execution of such letter by Holdings and the partnership party thereto.

4.5 Subsidiaries. Schedule 4.5 sets forth a complete and accurate list of all of the Subsidiaries, other than Subsidiaries which are not Insurance Subsidiaries and which do not hold any assets (including capital stock) with a fair market value in excess of $1,000 or insurance licenses (the "Section 4.5 Subsidiaries"). Schedule 4.5 also contains the jurisdiction of incorporation or formation of each of the Section 4.5 Subsidiaries, each jurisdiction in which such Subsidiary is licensed, qualified or otherwise authorized to conduct insurance business, the number of shares of capital stock of any Section 4.5 Subsidiary which is a corporation issued and outstanding and the percentage ownership interest of the Company in each such Subsidiary. All outstanding shares of capital stock of such Subsidiaries have been duly and validly authorized and are fully paid and nonassessable. Except as set forth on Schedule 4.5, all such outstanding shares are owned by the Company and/or one or more of its Subsidiaries free and clear of any Encumbrances, including, without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to such shares; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such shares without registration or qualification under, or in compliance with, applicable Federal securities or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 under the Securities Act) or without compliance with applicable insurance laws. Except as set forth on Schedule 4.5, there are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding for the purchase of, nor any securities convertible or exchangeable for, any equity interests of any of the Section 4.5 Subsidiaries. Schedule 4.5 contains true and complete copies of all agreements and other instruments pursuant to which the Company or any Section 4.5 Subsidiary is obligated or required, under any circumstance, to make contributions to the capital of any Subsidiary. Each of the Insurance Subsidiaries is a corporation duly licensed, organized, validly existing and in good standing under the jurisdiction of its organization and each of the other Subsidiaries is a corporation duly organized, validly existing and in good standing under the jurisdiction of its organization, in each case, with corporate power to own its properties and conduct its business as now being conducted and is duly licensed (in the case of the Insurance Subsidiaries), qualified and in good standing to transact business in each jurisdiction (as listed in Schedule 4.5) where, by virtue of its business carried on or properties owned, it is required to be so licensed (in the case of the Insurance Subsidiaries) or qualified and where the failure to be so licensed (in the case of the Insurance Subsidiaries) or qualified, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. To the extent requested of Seller by Buyer, Seller has made available to Buyer a complete and correct copy of the certificates of incorporation, bylaws and other organizational documents of each Section 4.5 Subsidiary and the minute books of each such Subsidiary. The minute books include copies of minutes of all meetings of the directors or shareholders of each such Subsidiary held on or after January 1, 1993 and complete and accurate copies of all resolutions passed by the directors or actions by written consent of the shareholders on or after

January 1, 1993.

4.6 Ridge Re. (a) Ridge Re is duly organized, validly existing and in good standing under the laws of Bermuda and has full corporate power and authority to conduct its business as it is presently being conducted and to own, lease and operate its properties and assets. Ridge Re is duly licensed, qualified or otherwise authorized as an alien corporation to conduct the reinsurance business conducted by it and is in good standing in each jurisdiction in which such license, qualification or authorization is necessary under the applicable law and where the failure to be so licensed, qualified or otherwise authorized, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(b) Seller owns of record and beneficially all of the outstanding capital stock of Ridge Re free and clear of all Encumbrances, including without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to such shares; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such shares without registration or qualification under, or in compliance with, applicable Federal or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act) or without compliance with applicable insurance laws. There are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding to which Parent, Seller, Ridge Re or any of their respective Affiliates is a party for the purchase of, nor any securities convertible or exchangeable for, any equity interests of Ridge Re, except as set forth in Schedule 4.6. Schedule 4.6 contains a true and complete list of all agreements and other instruments pursuant to which Parent, Seller or any Affiliate is obligated or required, under any circumstance, to make contributions to the capital of Ridge Re.

(c) Each of Ridge Re and each Insurance Subsidiary has all necessary corporate authority to enter into the Ridge Re Endorsements to which it will be a party and has taken all necessary corporate authority to consummate the transactions contemplated thereby and to perform its obligations thereunder. Subject to the occurrence of the Closing, each of the Ridge Re Endorsements will be duly executed and delivered by Ridge Re in Bermuda and by the Insurance Subsidiaries parties thereto. Upon execution and delivery by the parties thereto, each of the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsement, will be a legal, valid and binding obligation of Ridge Re, enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

4.7 Absence of Certain Changes or Events. To the Knowledge of Seller, except as expressly contemplated by this Agreement or as described on Schedule 4.7 or reflected in the Company Interim Financial Statements, since June 30, 1995, there has not been any:

(a) change in the business, condition (financial or otherwise), Permits, assets, Liabilities, working capital, earnings or operations of the Company or any Subsidiary, except for changes which have not, individually or in the aggregate, had or are not reasonably likely to have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole;

(b) acquisition of material assets or properties or of securities or business of any other Person by the Company or any Subsidiary (in each case, other than acquisitions in the ordinary course of business consistent with past practice) or any merger, consolidation or amalgamation involving the Company or any Subsidiary, except (i) the acquisition of Cash Equivalents as part of the process of converting substantially all of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents prior to the date of this Agreement and the reinvestment thereof in accordance with the Investment Policy after the date of this Agreement and (ii) the purchase by the Company of preferred stock of Filoli for a purchase price of $2,500,000;

(c) sale, assignment, lease or transfer of (i) the Crostex/Camfex Contracts, the Seller Notes (except transfers in accordance with, and to the extent Parent and Seller comply with, Section 6.12) or any interest in the Leesburg Training Facility (except transfers in accordance with, and to the extent Parent and Seller comply with, Section 6.13) or (ii) any other material assets (including any portion of the investment portfolio) of the Company or any Subsidiary, other than in the case of (ii) (W) in the ordinary course of business consistent with past practices, (X) converting substantially all of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents prior to the date of this Agreement and dispositions of securities in accordance with the Investment Policy after the date of this Agreement, (Y) the First Quadrant Asset Sale and (Z) the First Quadrant Final Sale;

(d) incurrence by the Company or any Subsidiary of any indebtedness for borrowed money or incurrence, assumption or guarantee of, or any other act to become responsible for, any obligations of any other Person, or making of loans or advances by the Company or any Subsidiary to any Person (including, without limitation, any broker or agent), except (i) advances to American All Risk Group ("AARG") to the extent required under a credit agreement in effect on the date hereof, a true and complete copy of which has been previously made available to Buyer, (ii) loans by IIC to Filoli in an aggregate principal amount of up to $17,500,000, (iii) loans to employees made in the ordinary course of business consistent with past practice for relocation expenses and (iv) the issuance of insurance policies in the ordinary course of business consistent with past practice;

(e) cancellation of any indebtedness or waiver or compromise of any rights (including agent balances) having a value to the Company or any Subsidiary of $500,000 or more, including the Seller Notes and the Crostex/Camfex Purchase Money Notes, whether or not in the ordinary course of business (other than settlements in the ordinary course of business of claims and salvage and subrogation rights arising under contracts of insurance underwritten, assumed or ceded by the Company or any Subsidiary which settlements have not had nor would be reasonably likely to have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole and the terminations, modifications and commutations permitted by clause (j) below), provided that for purposes of this paragraph the Company's elimination of a deferred tax asset in an amount equal to $7,000,000 relating to the Company's former participation in the ESOP shall not constitute a cancellation;

(f) failure of the Company or any Subsidiary to pay any creditor any amount owed to such creditor (in excess of $1,000,000 in the aggregate for all such creditors) when due (after the expiration of any applicable grace periods) except for failures to pay in the ordinary course of business or if the Company or any Subsidiary is disputing the amount due in good faith;

(g) payment by the Company or any Subsidiary of any material Liability before the same became due in accordance with its terms other than in the ordinary course of business consistent with past practice;

(h) material change in the underwriting, reinsurance, marketing, claim processing and payment, financial or accounting practices or policies of the Company or any Subsidiary, except as required by law, generally accepted accounting principles or Statutory Accounting Principles;

(i) except to the extent required under employee and director benefit plans or policies, agreements or arrangements as in effect on the Balance Sheet Date and except in connection with the Long Term Incentive Program attached as Attachment A and the Stock Option Agreement attached as Exhibit A to the Employment Agreement among Joseph W. Brown, Jr., Parent and the Company and the five related agreements with management of the Company or TRG (collectively, the "Long Term Incentive Program"), (1) increase in the compensation or fringe benefits of any of the directors, officers or employees of the Company or any Subsidiary (except for increases in salary or wages of employees of the Company or any Subsidiary who are not officers of the Company in the ordinary course of business in accordance with past practice), (2)

except for the letter agreement dated June 1, 1995 between II and Robert Puccinelli, and the Employment Agreement (and related grants of stock options and restricted stock) dated as of January 1, 1996 between Infocus Employee Services, Inc. and Andrew Vadyak (on terms and conditions reasonably satisfactory to Buyer), grant of any severance or termination pay or entrance into any employment, consulting or severance agreement or arrangement with any present or former director, officer or employee of the Company or any Subsidiary or amendment of any such arrangement or agreement or (3) establishment, adoption, entrance into, amendment of or termination of any (X) collective bargaining agreement or (Y) plan or agreement to provide bonuses, profit sharing, stock options, restricted stock, pensions, retirement benefits, deferred compensation, employment or benefits upon termination for the benefit of any directors, officers or any group of other employees of the Company or any Subsidiary;

(j) (i) entry into or modification of any reinsurance or retrocession agreement by the Company or any Subsidiary other than in the ordinary course of business consistent with past practice, except for those which have not had nor are reasonably likely to have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole or (ii) termination or commutation of any reinsurance or retrocession agreement legally carried on the books of the Subsidiaries at the time of such termination or commutation at $5,000,000 or more;

(k) entry into, termination or modification by the Company or any Subsidiary of any Contract, agreement, commitment, transaction, or instrument (including, without limitation, relating to any borrowing, lending, capital expenditure, capital contribution or capital financing), except entering into, terminating or modifying contracts, agreements, commitments, transactions, or instruments (i) in the ordinary course of business, (ii) as permitted by clauses (i) and (j) above and (iii) for a contribution of an amount not to exceed $4,000,000 by CGI to Coregis Managers Corporation (Il.); provided that except as disclosed on Schedule 4.7, no modifications shall have been made to the Crostex/Camfex Contracts, the Subsidiary Credit Agreements or the Ridge Re Treaties;

(l) entry into a material joint venture, partnership or similar arrangement by the Company or any Subsidiary with any Person;

(m) any capital expenditure or execution of any lease or commitment for the foregoing by the Company or any Subsidiary involving annual payments in excess of $100,000;

(n) lapse or termination or failure to renew any Permit of the Company or any Subsidiary, in each case other than with respect to Permits the failure of which to be in effect would not have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole;

(o) (i) declaration, setting aside or payment of any dividends or distributions (whether in cash, stock or property) in respect of any capital stock of the Company or (ii) any redemption, purchase or other acquisition of any of the capital stock of the Company or any Subsidiary (other than a wholly owned Subsidiary),except for payments permitted under the Tax Agreement;

(p) issuance by the Company or any Subsidiary of, or commitment of the Company or any Subsidiary to issue, any shares of capital stock or obligations or securities convertible into or exchangeable for shares of capital stock except for issuances or commitments by any Subsidiary to issue any such securities to the Company or any wholly owned Subsidiary;

(q) amendment of the certificate of incorporation or bylaws of the Company or any Subsidiary; or

(r) agreement by the Company or any Subsidiary to do any of the foregoing.

4.8 Title to Assets, Etc. The Company and the Subsidiaries have good title to or valid and subsisting leasehold interests in all real and material personal property and other material assets on their books and reflected on

the balance sheets included in the Company Interim Financial Statements and the Subsidiary Interim Financial Statements, as applicable, or acquired in the ordinary course of business since September 30, 1995 which would have been required to be reflected on such balance sheets if acquired on or prior to September 30, 1995, other than (i) assets which have been disposed of in the ordinary course of business or pursuant to the First Quadrant Final Sale and (ii) assets which were disposed in connection with the conversion of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents (the "Assets"). None of the Assets is subject to any Encumbrance, except for Encumbrances reflected in the financial statements contained in Schedule 4.12, as applicable, or which in the aggregate are not substantial in amount and do not materially detract from the value of the property or assets subject thereto or interfere with the present use.

4.9 Contracts and Commitments. (a) None of the Company or any Subsidiary is a party to any written or oral:

(i) Contracts not otherwise listed in Schedule 4.9;

(ii) except as listed on Schedule 4.9, treaties and agreements with, and undertakings or commitments to, any governmental or regulatory authority materially affecting the business of the Company and the Subsidiaries taken as a whole and not made in the ordinary course of business;

(iii) except as described in Schedule 4.9, contracts or agreements containing covenants limiting the freedom of the Company or any Subsidiary to engage in any line of business in any geographic area or to compete with any Person or to incur indebtedness for borrowed money;

(iv) except as described in Schedule 4.9 and for reinsurance and retrocession agreements, contracts or agreements containing "change in control" or similar provisions;

(v) except as listed on Schedule 4.9, employment contracts or agreements, including without limitation contracts to employ executive officers and other contracts with officers or directors of the Company or any Subsidiary which cannot be terminated by the Company or the Subsidiary upon notice of sixty days or less without penalty or premium and involve annual compensation in excess of $100,000 individually; or

(vi) contracts or agreements providing for the indemnification by the Company or any Subsidiary of any Person except for contracts entered into in the ordinary course of business consistent with past practice.

(b) Except as set forth on Schedule 4.9, none of the Company or any Subsidiary is (and, to the Knowledge of the Seller, no other party is) (i) in material breach of or materially in default under, any of the Contracts (or with or without notice or lapse of time or both, would be in material breach of or materially in default under any of the Contracts) or (ii) in breach or default under any of the Contracts (with or without notice or lapse of time or both) if such breach or default would permit a party other than the Company or a Subsidiary to terminate such Contract. None of Parent, Seller, the Company or any Subsidiary has delivered or received notice of termination or written notice of an intention to terminate to or from any other party to any Contract except as described on Schedule 4.9.

(c) Other than the Ridge Re Treaties and treaties between Ridge Re and subsidiaries of TRG, Viking and Constitution Re, respectively (copies of which have been provided to Buyer), Ridge Re is not a party to any reinsurance or retrocession agreement or treaty, and, except in connection with such treaties, does not engage in any business. Set forth in Schedule 4.9 is the amount of cover as of the date of this Agreement available under each of the Ridge Re Treaties. True and complete copies of the Ridge Re Treaties are contained in Schedule 1.1D. Each of the Ridge Re Treaties is in full force and effect and constitutes a legal, valid and binding obligation of the parties thereto, enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in

equity or at law) and an implied covenant of good faith and fair dealing. None of Parent, Seller, the Company or any Subsidiary has received any notice from Ridge Re or any governmental or regulatory authority (i) that any Ridge Re Treaty is not enforceable against any party thereto or (ii) regarding the availability or enforceability of the cover under any Ridge Re Treaty. No party to a Ridge Re Treaty has received notice of termination of, or written notice of an intention to terminate, any Ridge Re Treaty. No party to a Ridge Re Treaty is in breach of or violation of or default under any Ridge Re Treaty (or with or without notice or lapse of time or both, would be in breach of or violation of or default under any Ridge Re Treaty), except for breaches, violations or defaults by an Insurance Subsidiary which would not permit Ridge Re to terminate the applicable Ridge Re Treaty or which would not provide Ridge Re with a defense to any payment obligation of Ridge Re thereunder.

4.10 No Conflict or Violation. Except as set forth in Schedule 4.10, neither the execution, delivery and performance of this Agreement or any of the Ancillary Agreements nor the consummation of the transactions contemplated hereby or thereby will result in (a) a violation of or a conflict with any provision of the certificate of incorporation or bylaws of Parent, Seller, Ridge Re, the Company or any Section 4.5 Subsidiary, (b) a breach of, or a default under, any term or provision of any contract, agreement, indebtedness, lease, Encumbrance, commitment, license, franchise, Permit, authorization or concession to which (i) Parent, Seller or Ridge Re is a party or is subject or by which any assets (including investments) of any of them are bound or (ii) the Company or any Subsidiary is a party or is subject or by which any assets (including investments) of any of them are bound, which breach or default in the case of clause (ii) would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or in the case of clauses (i) and (ii) would interfere in any material way with the ability of Parent or Seller to consummate the transactions contemplated by this Agreement or any of the Ancillary Agreements or the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsements, (c) subject to obtaining the approvals referred to in Section 4.11, a violation by Parent, Seller, Ridge Re, the Company or any Subsidiary of any statute, rule, regulation, ordinance, code, order, judgment, writ, injunction, decree or award, which violation would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or interfere in any material way with the ability of Parent, Seller or Ridge Re to consummate the transactions contemplated by this Agreement or any of the Ancillary Agreements, (d) the imposition of any Encumbrance, restriction or charge on the business of the Company or any Subsidiary or on any material assets of the Company or the Subsidiaries, (e) the creation or exercisability of any right of termination, cancellation or acceleration under any Contract or (f) result in the breach of any of the terms or conditions of, constitute a default under, or otherwise cause any impairment of, any Permit, which breach, default or impairment would result, individually or in the aggregate, in a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.11 Consents and Approvals. Except for (i) the approval of this Agreement, the Ancillary Agreements and the transactions contemplated hereby and thereby (including, without limitation, the Financing), and the new intercompany tax agreements among the Company and the Subsidiaries which shall be effective as of the Closing, by each of the governmental and regulatory authorities listed on Schedule 4.11, (ii) the approval of this Agreement, the Ancillary Agreements and the transactions contemplated hereby and thereby (including, without limitation, the Financing), and the new intercompany tax agreements among the Company and the Subsidiaries which shall be effective as of the Closing, by any other governmental or regulatory authorities, the failure of which to obtain would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, (iii) filings in respect of the transactions contemplated hereby required to be made for compliance with the applicable provisions of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the rules and regulations promulgated thereunder, (iv) filings under the Securities Act and the rules promulgated thereunder in connection with the sale of the Underwritten Notes, (v) the filing of premerger notification reports under the HSR Act and (vi) consents, approvals, authorizations, declarations, filings and registrations required (x) by the nature of the business or ownership of Holdings and Buyer

or (y) solely by reason of the Financing (excluding any consents, approvals, authorizations, declarations, filings or registrations otherwise required in connection with this Agreement, the Ancillary Agreements or the transactions contemplated hereby or thereby), no consent, approval or authorization of, or declaration, filing or registration with, any governmental or regulatory authority, or any other Person, is required to be made or obtained by Parent, Seller, Ridge Re, the Company, any Subsidiary, Buyer or Holdings on or prior to the Closing Date in connection with the execution or delivery of this Agreement or any of the Ancillary Agreements, the performance of this Agreement, the Guarantees, the Tax Agreement, or the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsements, or the consummation of the transactions contemplated hereby and thereby.

4.12 Financial Statements. (a) Seller has heretofore delivered to Buyer the Company GAAP Financial Statements, the Subsidiary GAAP Financial Statements, the Ridge Re GAAP Financial Statements, the Company Interim Financial Statements, the Subsidiary Interim Financial Statements, the Ridge Re Interim Financial Statements and the Convention Statements. A copy of each of the foregoing financial statements is included in Schedule 4.12.

(b) Except as otherwise set forth therein, (i) the Company GAAP Financial Statements are based on the books and records of the Company and its Subsidiaries, fairly present in all material respects the financial condition and consolidated results of operations of the Company and its Subsidiaries, as of the dates and for the periods indicated therein, have been prepared in accordance with GAAP (as in effect at the time of the respective financial statements) consistently applied, and have been audited by KPMG Peat Marwick LLP, (ii) each of the Subsidiary GAAP Financial Statements are based on the books and records of the GAAP Subsidiaries to which such statements relate, fairly present in all material respects the financial condition and consolidated results of operations of such Subsidiaries, as of the dates and for the periods indicated therein, have been prepared in accordance with GAAP (as in effect at the time of the respective financial statements) consistently applied, and have been audited by KPMG Peat Marwick LLP and (iii) the Ridge Re GAAP Financial Statements are based on the books and records of Ridge Re, fairly present in all material respects the financial condition and results of operation of Ridge Re, as of the dates and for the periods indicated therein, have been prepared in accordance with GAAP (as in effect at the time of the respective financial statements) consistently applied, and have been audited by KPMG Peat Marwick LLP.

(c) The Company Interim Financial Statements, the Subsidiary Interim Financial Statements and the Ridge Re Interim Financial Statements were prepared in the ordinary course of business and have been prepared on a consistent basis through the periods indicated and in a manner consistent with that employed in the Company GAAP Financial Statements, the Subsidiary GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be. The Company Interim Financial Statements, the Subsidiary Interim Financial Statements and the Ridge Re Interim Financial Statements do not contain full footnote disclosures in accordance with United States generally accepted accounting principles and are subject to normal recurring year-end adjustments, but otherwise fairly present in all material respects the financial condition and results of operations of the Company, the GAAP Subsidiaries and Ridge Re, as the case may be, as of the dates and for the periods indicated therein except as otherwise set forth therein.

(d) Except as otherwise set forth therein, the Convention Statements and the statutory balance sheets and income statements included in such Convention Statements fairly present in all material respects the statutory financial condition and results of operations of the respective Insurance Subsidiaries and Ridge Re, as the case may be, as of the dates and for the periods indicated therein and have been prepared in accordance with Statutory Accounting Principles (as in effect at the time of the respective financial statements) consistently applied throughout the periods indicated, except as expressly set forth therein. The statutory balance sheets and income statements included in the Convention Statements for the years ended December 31, 1993 and 1994 have been audited by KPMG Peat Marwick LLP.

4.13 Litigation. To the Knowledge of Seller, except as set forth on Schedule 4.13, there is no action, order, writ, injunction, judgment, fine or decree outstanding or suit, litigation, proceeding, labor dispute (other than routine grievance procedures or routine, uncontested claims for benefits under any benefit plans for any officers, employees or agents of the Company or any Subsidiary (collectively, "Personnel")), arbitral action, investigation or reported claim, in each case including, without limitation, those involving any governmental or regulatory authority and excluding those relating to insurance and reinsurance policies (collectively, "Actions") pending or threatened by or against or relating to (i) the Company or any Subsidiary, (ii) any benefit plan for Personnel or any fiduciary or administrator thereof or (iii) the transactions contemplated by this Agreement and the Ancillary Agreements. None of the Company or any Subsidiary is in default with respect to any order, writ, injunction, judgment, fine or decree of any court or governmental or regulatory agency, and there are no unsatisfied judgments against the Company or any Subsidiary which would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.14 Liabilities. (a) Except as set forth in Schedule 4.14, the Company and the Subsidiaries do not have any direct or indirect indebtedness, liability, claim, loss, damage, deficiency, obligation or responsibility, fixed or unfixed, choate or inchoate, liquidated or unliquidated, secured or unsecured, accrued, absolute, contingent or otherwise ("Liabilities"), other than (i) Liabilities fully and adequately reflected (including by reducing any numerical amount set forth) in one or more line items on, reserved on, or disclosed in the footnotes to, the balance sheets included in the Company Interim Financial Statements or the Subsidiary Interim Financial Statements, or disclosed in the footnotes to the Company GAAP Financial Statements or the Subsidiary GAAP Financial Statements, (ii) Liabilities incurred in the ordinary course of business, consistent with past practice and the provisions of this Agreement and the Ancillary Agreements, (iii) Liabilities relating to future benefits, losses, claims and expenses arising under insurance and reinsurance policies of the Insurance Subsidiaries, (iv) Liabilities disclosed in response to any other representation, (v) Liabilities of a type that are subject to any other representation (without regard to any specific exclusions from such representation, including any specific exclusions from the definitions used therein) and (vi) Liabilities which have, or are reasonably likely to have a net ultimate cost of $25,000 or less, on an individual basis or in the aggregate to the extent such Liabilities arise out of a related series of events.

(b) As of the date of this Agreement, no more than $358,500,000 aggregate principal amount of indebtedness is outstanding under the credit agreements contained in Schedule 4.14 (the "Subsidiary Credit Agreements").

(c) The Company and the Subsidiaries have no Liabilities for rate roll-backs or refunds under California Proposition 103 and all proceedings thereunder relating to the Company and the Subsidiaries have ceased.

(d) Each of the Company and each Subsidiary has paid in full all guaranty fund assessments required by any regulatory authority to be paid by it prior to the date of this Agreement. As of the date of this Agreement, except as set forth in Schedule 4.14 and except as and to the extent paid prior to June 30, 1995 or reserved against in the Convention Statements or disclosed in the notes thereto, the Company and the Subsidiaries have not received any guarantee fund assessments.

4.15 Investments. (a) As of the date of this Agreement, at least 85% of the investment portfolio for the Company and the Subsidiaries consists of cash and Cash Equivalents and at least 61% of the investment portfolio (excluding cash and Cash Equivalents) for the Company and the Subsidiaries consists of fixed income securities rated at least AA by Moody's or by S&P. As of the date hereof, at least 57% of the fixed income portfolio (excluding cash and Cash Equivalents) has a maturity of one year or less.

(b) To the Knowledge of Seller, as of the Closing Date, the Company and the Subsidiaries have good and marketable title to the investments in their

investment portfolios, provided that no representation is made as to the transferability thereof.

4.16 Reserves. Seller has delivered to Buyer true and complete copies of all actuarial reports or actuarial certificates in the possession or control of Parent, Seller, the Company or any of the Subsidiaries relating to the adequacy of the claims reserves of any of the Subsidiaries for any period ended on or after December 31, 1993. Notwithstanding the foregoing representations contained in this Section or anything contained in Section 4.12, 4.14 or 6.2, Holdings and Buyer acknowledge that Parent and Seller are not making any representations, express or implied in or pursuant to this Agreement, concerning the loss reserves or loss adjustment expense reserves of the Company or any of the Subsidiaries including, without limitation, (i) whether such reserves are adequate or sufficient, or (ii) whether such reserves were determined in accordance with any actuarial, statutory or other standard, or concerning any other "line item" or asset, liability or equity amount which would be affected thereby.

4.17 Compliance with Law; Permits; Regulatory Matters. (a) Except as set forth on Schedule 4.17, the Company and the Subsidiaries are in compliance with all applicable laws, statutes, ordinances and regulations, whether Federal, foreign, state or local, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Since January 1, 1993, none of the Company or any Subsidiary has received any written notice to the effect that, or otherwise been advised that, it is not in compliance with any such statute, regulation, order, ordinance or other law where the failure to comply would, prior to June 30, 1998, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(b) Except as set forth on Schedule 4.17, the Company and the Subsidiaries hold all Permits necessary for the ownership and conduct of the respective businesses of the Company and the Subsidiaries in each of the jurisdictions in which the Company and the Subsidiaries conduct or operate their respective businesses in the manner now conducted, and such Permits are in full force and effect except where the failure to hold any Permit or the failure of any Permit to be in full force and effect would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. The consummation of the transactions contemplated by this Agreement will not result in any revocation, cancellation or suspension of any such Permit except as a result of the status of Buyer and its Affiliates, and, there are no pending or threatened suits, proceedings or investigations with respect to revocation, cancellation, suspension or nonrenewal thereof, and, there has occurred no event which (whether with notice or lapse of time or both) will result in such a revocation, cancellation, suspension or nonrenewal thereof, in any such case except where such a revocation, cancellation, suspension or non-renewal would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(c) All insurance policies issued by the Insurance Subsidiaries, as now in force are, to the extent required under applicable law, are in a form acceptable to applicable regulatory authorities or have been filed and not objected to (or such objection has been withdrawn or resolved) by such authorities within the period provided for objection, except where such failure or objection would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Neither the Company nor any Subsidiary which is not an Insurance Subsidiary has issued any insurance policies. Except as set forth on Schedule 4.17, (i) all material reports, statements, documents, registrations, filings and submissions to state insurance regulatory authorities complied in all material respects with applicable law in effect when filed and (ii) no material deficiencies have been asserted by any such regulatory authority with respect to such reports, statements, documents, registrations, filings or submissions that have not been satisfied or that would, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Except as set forth on Schedule 4.17, all premium rates established by the Insurance Subsidiaries that are required to be filed with or approved by insurance regulatory authorities have been so filed or approved, the premiums

charged conform to the premiums so filed or approved and comply (or complied at the relevant time) with the insurance laws applicable thereto except where such failures to comply, individually or in the aggregate, would not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.18 No Brokers. Except as previously disclosed in writing to Buyer, neither Parent, Seller nor the Company has employed, or is subject to any valid claim of, any broker, finder, consultant or other intermediary in connection with the transactions contemplated by this Agreement who will be entitled to a fee or commission in connection with such transactions. Parent is solely responsible for any such payment, fee or commission that may be due to any Person so previously disclosed to Buyer in connection with the transactions contemplated hereby.

4.19 No Other Agreements to Sell the Assets or the Company. Except as set forth in Schedule 4.19, none of Parent, Seller, the Company or any Subsidiary has any agreement, absolute or contingent, with any other Person to sell the capital stock, assets (other than sales of assets that would not be prohibited under Section 4.7(c)) or business of the Company or any Subsidiary or to effect any merger, consolidation or other reorganization of the Company or any Subsidiary or to enter into any agreement with respect thereto, except for any agreements regarding the First Quadrant Final Sale.

4.20 Proprietary Rights. (a) Except as set forth in Schedule 4.20, Parent, Seller and their Affiliates (other than the Company and the Subsidiaries) have no right or title to or interest in the trademarks, service marks, copyrights, trade names and the applications and registrations therefor and the trade secrets, software and other proprietary rights used in and material to the business of the Company or any of its Subsidiaries (collectively, "Intellectual Property").

(b) Schedule 4.20 sets forth a complete and correct list and brief description of all Intellectual Property that is material to the Company or any Subsidiary. With respect to intellectual property owned by the Company or a Subsidiary, such entity has the sole and exclusive right to use and is the sole and exclusive registered owner of all right, title and interest in and to the Intellectual Property. The Intellectual Property which is not owned by the Company or a Subsidiary is being used by the Company or a Subsidiary only with the consent of or license from the rightful owner thereof, and all such licenses are in full force and effect.

(c) To the Knowledge of Seller no activity in which the Company or a Subsidiary is engaged or any product which the Company or a Subsidiary sells, or any advertising that they employ, or the use of any of the Intellectual Property, breaches, violates, infringes or interferes with any rights of any third party or, except for the payment of computer software licensing fees, requires payment for the use of any patent, trade-name, trade secret, trade-mark, copyright or other intellectual property right or technology of another.

4.21 Employee Benefit Plans. (a) Schedule 4.21 contains a true and complete list of each "employee benefit plan" (within the meaning of section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), including, without limitation, multiemployer plans within the meaning of ERISA section 3(37)), stock purchase, stock option, severance, employment, change-in-control, fringe benefit, collective bargaining, bonus, incentive, deferred compensation and all other employee benefit plans, agreements, programs, policies or other arrangements, whether or not subject to ERISA (including any funding mechanism therefor now in effect or required in the future as a result of the transactions contemplated by this Agreement or otherwise), whether formal or informal, oral or written, legally binding or not, under which any employee or former employee of the Company or any Subsidiary has any present or future right to benefits or under which the Company or any Subsidiary has any present or future liability. All such plans, agreements, programs, policies and arrangements shall be collectively referred to as the "Company Plans".

(b) With respect to each Company Plan, the Company has delivered to the Buyer a current, accurate and complete copy (or, to the extent no such copy exists,

an accurate description) thereof and, to the extent applicable, (i) any related trust agreement, annuity contract or other funding instrument; (ii) the most recent determination letter; (iii) any summary plan description and other written communications (or a description of any oral communications) by the Company or any Subsidiary to their employees concerning the extent of the benefits provided under a Company Plan; and (iv) for the three most recent years (A) the Form 5500 and attached schedules; (B) audited financial statements; (C) actuarial valuation reports; and (D) attorney's response to an auditor's request for information.

(c) (i) Each Company Plan, in all material respects, has been established and administered in accordance with its terms and in compliance with the applicable provisions of ERISA, the Code and other applicable laws, rules and regulations; (ii) each Company Plan which is intended to be qualified within the meaning of Code section 401(a) is so qualified and has received a favorable determination letter as to its qualification and nothing has occurred, whether by action or failure to act, which would cause the loss of such qualification; (iii) except as listed on Schedule 4.21, with respect to any Company Plan, no actions, suits or claims (other than routine claims for benefits in the ordinary course) are pending or threatened, no facts or circumstances exist which could give rise to any such actions, suits or claims, and the Company will promptly notify Buyer in writing of any pending or threatened claims arising between the date hereof and the Closing Date; (iv) neither the Company, any Subsidiary nor any other party has engaged in a prohibited transaction, as such term is defined under Code section 4975 or ERISA section 406, which would subject the Company, any Subsidiary or the Buyer to any material taxes, penalties or other liabilities under Code section 4975 or ERISA sections 409 or 502(i); (v) no event has occurred and no condition exists that would subject the Company, either directly or by reason of its affiliation with any member of its "Controlled Group" (defined as any organization which is a member of a controlled group of organizations within the meaning of Code sections 414(b), (c), (m) or (o)), or any Subsidiary to any material tax, fine or penalty imposed by ERISA, the Code or other applicable laws, rules and regulations including, but not limited to the taxes imposed by Code sections 4971, 4972, 4977, 4979, 4980B, 4976(a) or the fine imposed by ERISA section 502(c); (vi) all insurance premiums required to be paid with respect to Company Plans as of the Closing Date have been or will be paid prior thereto and adequate reserves have been provided for on the Company's Interim Financial Statements as of September 30, 1995, to the extent required by GAAP, for any premiums (or portions thereof) attributable to service on or prior to the Closing Date; (vii) for each Company Plan with respect to which a Form 5500 has been filed, no material change has occurred with respect to the matters covered by the most recent Form since the date thereof; (viii) all contributions required to be made prior to the Closing Date under the terms of any Company Plan, the Code, ERISA or other applicable laws, rules and regulations have been or will be timely made and adequate reserves have been provided for on the Company's Interim Financial Statements as of September 30, 1995, to the extent required by GAAP, for all benefits attributable to service on or prior to the Closing Date; (ix) no Company Plan provides for an increase in benefits on or after the Closing Date; and (x) no Company Plan (excluding any agreement between the Company and individual employees) contains any contractual language which limits the Company's ability to amend or terminate such Company Plan without obligation or liability (other than those obligations and liabilities for which specific assets have been set aside in a trust or other funding vehicle or reserved for on the Company's Interim Financial Statements as of September 30, 1995).

(d) (i) No Company Plan has incurred any "accumulated funding deficiency" as such term is defined in ERISA section 302 and Code section 412 (whether or not waived); (ii) no event or condition exists which would be deemed a reportable event within the meaning of ERISA section 4043 which could result in a material liability to the Company, any member of its Controlled Group or any Subsidiary, and no condition exists which could subject the Company, any member of its Controlled Group or any Subsidiary to a material fine under ERISA section 4071; (iii) as of the Closing Date, the Company, each member of its Controlled Group and each Subsidiary will have made all premium payments required to be made prior to the Closing Date to the PBGC; (iv) neither the Company, any member of its Controlled Group nor any Subsidiary is subject to

any liability to the PBGC for any plan termination occurring on or prior to the Closing Date; (v) no amendment has occurred which has required or would require the Company, any member of its Controlled Group or any Subsidiary to provide security pursuant to Code section 401(a)(29); and (vi) neither the Company, any member of its Controlled Group nor any Subsidiary has engaged in a transaction which could subject it to material liability under ERISA section 4069.

(e) With respect to each of the Company Plans which is not a multiemployer plan within the meaning of section 4001(a)(3) of ERISA but is subject to Title IV of ERISA, the funded status of each such Company Plan, as of January 1, 1995, is as reported in the actuarial valuation reports dated as of January 1, 1995. To the Knowledge of Seller, no material adverse change in the funded status of such Company Plans has occurred since January 1, 1995, and no material defects or omissions existed in the data provided to the preparers of the actuarial valuation reports discussed in the preceding sentence.

(f) There are no multiemployer plans (within the meaning of section 4001(a)(3) of ERISA) to which the Company, any member of its Controlled Group or any Subsidiary has or had any liability or contributes (or has at any time contributed or had an obligation to contribute).

(g) (i) Each Company Plan which is intended to meet the requirements for tax-favored treatment under Subchapter B of Chapter 1 of Subtitle A of the Code meets such requirements; and (ii) the Company and the Subsidiaries have no trusts intended to be qualified within the meaning of Code section 501(c)(9), and, except as listed on Schedule 4.21, had no such trusts in the past.

(h) Schedule 4.21 sets forth, on a plan-by-plan basis, the present value of any benefits payable presently or in the future to present or former employees of the Company or any Subsidiary under any Company Plan (excluding any agreements between the Company and individual employees which were not entered into as part of any plan or program) that is not fully funded and not subject to the reporting requirements of ERISA (if such amounts are not reflected in the financial statements included in Schedule 4.12) which present value is as reported in the most recent actuarial valuation or other reports done with respect to each such plan. To the Knowledge of Seller, no material adverse increase in the amount of such present values has occurred since the date of the most recent report, and no material defects or omissions existed in the reports, or, if applicable, in the data provided to the preparers of the reports.

(i) Except as set forth on Schedule 4.21 or referenced in Section 9.5, no Company Plan exists which could result in the payment to any Company employee or Subsidiary employee of any money or other property or accelerate or provide any other rights or benefits to any Company employee or Subsidiary employee as a result of the transactions contemplated by this Agreement, whether or not such payment would constitute a parachute payment within the meaning of Code section 280G. The aggregate cost to the Company and its Subsidiaries, in the event that all Company Plans set forth in Schedule 4.21 are triggered, shall not exceed $1,050,000.

(j) Neither the Company nor any Subsidiary is obligated or otherwise required to pay any bonuses (annual or otherwise) to Joseph W. Brown, Jr., or to any managing director of the Company on or after the date of the Closing.

(k) No Company Plan operates within or is subject to the jurisdiction of any foreign country, other than as described on Schedule 4.21.

(l) None of the amounts payable to any Company employee or any Subsidiary employee as a result of the transactions contemplated by this Agreement will be non-deductible under Section 280G of the Code.

4.22 Employment-Related Matters. Except as set forth in Schedule 4.22, (a) none of the Company or the Subsidiaries is a party to, or otherwise bound by, any consent decree with, or citation by, any government agency relating to employees or employment practices, (b) none of the Company or any of the Subsidiaries has closed any plant or facility, or effectuated any layoffs of

employees within the past six months, nor have the Company or the Subsidiaries planned or announced any such action or programs for the future, and (c) the Company and the Subsidiaries are in compliance with their respective obligations pursuant to the Worker Adjustment and Retraining Notification Act of 1988 and any similar state notification law.

4.23 Transactions with Certain Persons. (a) To the Knowledge of Seller, neither any officer, director or employee of Parent, Seller, the Company or any Subsidiary nor any member of any such Person's immediate family is presently a party to any material transaction with the Company or any Subsidiary, including, without limitation, any Contract, or other binding arrangement (i) providing for the furnishing of material services (except in such Person's capacity as an officer, director, employee or consultant) by, (ii) providing for the rental of material real or personal property from, or (iii) otherwise requiring material payments to (other than for services as officers, directors or employees of Parent, Seller, the Company or any Subsidiary) any such Person.

(b) Schedule 4.23 sets forth all contracts, agreements and arrangements in effect on or after January 1, 1995, and all transactions (including, without limitation, the provision of any services or the sale of any goods) since January 1, 1994 between the Company or any Subsidiary, on the one hand, and Parent or any Affiliate of Parent (excluding the Company and the Subsidiaries, but including TRG and any of its subsidiaries), on the other, excluding contracts, agreements and arrangements (i) relating to the use or purchase of products leased or sold by Parent in the ordinary course of Parent's document processing business, (ii) involving payments by or to the Company or any Subsidiary that do not exceed $100,000 in the aggregate or (iii) specifically referred to in the financial statements contained in Schedule 4.12. Certain Subsidiaries hold $275,000,000 aggregate principal amount of promissory notes issued by Seller and unconditionally guaranteed by Parent and $75,000,000 aggregate principal amount of notes issued by Credit Corp. (such notes, collectively, the "Seller Notes"). Schedule 4.23 identifies the current holders of each of the Seller Notes.

(c) Except in the ordinary course of business consistent with past practice, since the Balance Sheet Date, Seller and the Company and/or any Subsidiary have not settled any intercompany trade receivables and payables.

4.24 Taxes. (a) Filing of Tax Returns. Seller and the Company (and any affiliated group of which the Company is now or has been a member) have timely filed with the appropriate taxing authorities all Federal, and to the Knowledge of Seller, state and local Tax Returns and Information Returns required to be filed through the date hereof. All such Federal, and to the Knowledge of Seller, state and local Tax Returns and Information Returns are complete and accurate in all material respects. The Company is a member of an affiliated group of corporations, within the meaning of Section 1504 of the Code, that includes Seller and Parent, and Parent is the common parent of the affiliated group.

(b) Payment of Taxes. All Taxes shown in the Tax Returns referred to in Section 4.24(a) above that are due and payable by the Company and its Subsidiaries before the date hereof have been paid.

(c) Liens for Taxes. There are no liens or other Encumbrances on any of the assets of the Company or any Subsidiary that arose in connection with any failure (or alleged failure) to pay any Tax.

(d) Audit History. Except as set forth in Schedule 4.24, there is no action, suit, proceeding, investigation, audit or claim now pending or, to the Knowledge of Seller, proposed against or with respect to the Company or any of its Subsidiaries or any affiliated group of which the Company and its Subsidiaries is or has been a member that relates to Tax liabilities attributable to items of income, gain, deduction, loss or credits of the Company or any of its Subsidiaries.

(e) Prior Affiliated Groups. Except as set forth in Schedule 4.24 and except for the affiliated group of corporations of which the Company and the

Subsidiaries is currently a member and of which Parent is the common parent, the Company and the Subsidiaries have never been members of an affiliated group of corporations, within the meaning of Section 1504 of the Code.

(f) Withholding. The Company and the Subsidiaries have withheld and paid all Federal, and to the Knowledge of Seller, state and local Taxes required to have been withheld and paid in connection with amounts paid or owing to any employee, independent contractor, creditor, stockholder or other third party.

(g) FIRPTA. Neither the Company nor any of the Subsidiaries have been a United States real property holding corporation within the meaning of Section 897(c)(2) of the Code during the five-year period ending on the date hereof.

(h) Material Adverse Effect. A representation with respect to Taxes contained in this Section 4.24 shall be deemed to be accurate unless an inaccuracy contained therein has a Material Adverse Effect on the Company and the Subsidiaries.

4.25 Reinsurance and Retrocessions. Schedule 4.25 contains a list as of the date of this Agreement of all treaty reinsurance or retrocession treaties and agreements in force to which any Subsidiary is a party (including any terminated or expired treaty or agreement under which there remains any outstanding liability with respect to paid or unpaid case reserves in excess of $500,000), any terminated or expired treaty or agreement under which there remains any outstanding liability from one reinsurer with respect to paid or unpaid case reserves in excess of $100,000 and any treaty or agreement with any Affiliate of such Subsidiary, the effective date of each such treaty or agreement, and the termination date of any treaty or agreement which has a definite termination date. To the Knowledge of Seller, no Subsidiary is in default in any respect as to any provision of any reinsurance or retrocession treaty or agreement or has failed to meet the underwriting standards required for any business reinsured thereunder except for defaults which, individually or in the aggregate, would not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.26 1992/93 Restructuring. All novations made pursuant to the 1992/93 Restructuring and any amendments to the Ridge Re Treaties made prior to the date hereof, were made in accordance with all applicable laws, rules and regulations at the time such novations or amendments were completed except where the failure to do so (i) would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or (ii) was a result of the failure by the Company or any Subsidiary to obtain the consent of any insured or policyholder to the novation or assumption of the relevant insurance policy. Notwithstanding the foregoing, Buyer and Holdings acknowledges that Seller and Parent shall have no liability to Buyer or Holdings for breach of this representation with respect to any novation or assumption, or any amendment to the Ridge Re Treaties, which results in any liability for the Company or any of its Subsidiaries, if there is a corresponding benefit realized (or any liability avoided) by the Company or any other Subsidiary or TRG or any of its subsidiaries.

4.27 Capital Commitments. Schedule 4.27 contains a list of all capital commitments as of the date of this Agreement of the Company or any Subsidiary in excess of $100,000.

4.28 Environmental Laws. (a) Except as set forth on Schedule 4.28, each of the Company and each Subsidiary complies and has complied with all applicable Environmental Laws, and possesses and complies with and has possessed and complied with all Environmental Permits required under such laws except where the failure to be in possession of or to comply with such Environmental Permits, or where the failure to be in compliance with any Environmental Law, would not have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. There are no past, present, or anticipated future events, conditions, circumstances, practices, plans or legal requirements that could reasonably be expected to prevent, or materially increase the burden on the Company or any Subsidiary of their complying with applicable Environmental Laws or of their obtaining, renewing, or complying with all Environmental Permits required under such laws. There

are and have been no Materials of Environmental Concern or other conditions at any property owned, operated or otherwise used by the Company or any Subsidiary now or in the past, or at any other location, that could reasonably be expected to give rise to liability of the Company or any Subsidiary under any Environmental Law. Parent, Seller and the Company have provided to Buyer true and complete copies of all Environmental Reports prepared within the last five years in their possession or control.

(b) Notwithstanding the representations contained in this Section, Buyer acknowledges that Parent and Seller are not making any representations (express or implied in or pursuant to this Agreement) with respect to any violation of or noncompliance with Environmental Law or Environmental Permits, or failure to obtain Environmental Permits, in each case by reason of any policy of insurance, reinsurance, indemnity, guaranty or assumption of liability of any party, entered into by the Company or any Insurance Subsidiary.

4.29 Acquisition for Investment. Each of Seller and Parent acknowledges that the Securities have not been registered under the Securities Act, or under any state securities laws. Each of Seller and Parent (to the extent Parent acquires Securities pursuant to Section 11.3) is acquiring the Securities solely for its own account and not with a view to any distribution or other disposition of such Securities or any part thereof, or interest therein, except in accordance with the Securities Act. Each of Seller and Parent is an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act).

## ARTICLE V

## REPRESENTATIONS AND WARRANTIES OF BUYER AND HOLDINGS

Buyer and Holdings hereby represent and warrant to Seller and Parent as follows:

5.1 Organization of Buyer and Holdings. Each of Buyer and Holdings is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business and to own and lease its properties.

5.2 Authorization. Each of Buyer and Holdings has all necessary corporate authority to enter into this Agreement and the Tax Agreement and has taken all necessary corporate action to consummate the transactions contemplated hereby and thereby and to perform its obligations hereunder and thereunder. This Agreement and the Tax Agreement have been duly executed and delivered by each of Buyer and Holdings. Assuming the due execution of this Agreement by Parent and Seller, this Agreement is a legal, valid and binding obligation of each of Buyer and Holdings enforceable against each of them in accordance with its terms, and assuming the due execution of the Tax Agreement by Parent, Seller and the Company, the Tax Agreement is a legal, valid and binding obligation of Buyer enforceable against Buyer in accordance with its terms, in each case, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing. Subject to the occurrence of the Closing, the TOPrS Side Letter will be duly executed and delivered by Holdings and the partnership party thereto. Upon execution and delivery by Holdings and such partnership of the TOPrS Side Letter and assuming the due execution of the TOPrS Side Letter by Seller, the TOPrS Side Letter will be a legal, valid and binding obligation of Holdings and such partnership, enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

5.3 No Conflict or Violation. Neither the execution, delivery and performance of this Agreement or the Tax Agreement by Holdings and Buyer, nor

the execution, delivery and performance of the Indenture or the TOPrS Side Letter or the issuance of Debentures by Holdings, nor the execution, delivery and performance of the Trust Agreement by Holdings, as depositor, nor the issuance of the Preferred Securities by Trust, nor the issuance, if issued, of Holdings Common Stock by Holdings pursuant to the provisions of Section 11.3 nor the consummation by Buyer, Holdings or Trust of the transactions contemplated hereby or thereby will result in (a) a violation of or a conflict with any provision of the certificate of incorporation or bylaws, in the case of Holdings or Buyer, or any provisions of the Trust Agreement, in the case of Trust, (b) a breach of, or a default under, any term or provision of any contract, agreement, indebtedness, lease, Encumbrance, commitment, license, franchise, Permit, authorization or concession (including any agreements, documents or instruments (the "Financing Documents") constituting part of the financing required to consummate the transactions contemplated by this Agreement (the "Financing")) to which Buyer, Holdings or Trust is a party or is subject or by which any assets of Buyer, Holdings or Trust are bound, which breach or default is in a Financing Document or would, individually or in the aggregate, have a Material Adverse Effect on Buyer or Holdings or interfere in any material way with the ability of Buyer or Holdings to consummate the transactions contemplated by this Agreement, the TOPrS Side Letter and the Tax Agreement, to the extent a party thereto, or (c) subject to obtaining the approvals referred to in Section 4.11, a violation by Buyer, Holdings or Trust of any statute, rule, regulation, ordinance, code, order, judgment, writ, injunction, decree or award, which violation would, individually or in the aggregate, have a Material Adverse Effect on Buyer or Holdings or their respective ability to consummate the transactions contemplated by this Agreement and the Tax Agreement, to the extent a party thereto.

5.4 No Brokers. Except for the services of Merrill Lynch & Co., neither Buyer nor Holdings has employed, or is subject to the valid claim of, any broker, finder, consultant or other intermediary in connection with the transactions contemplated by this Agreement who will be entitled to a fee or commission in connection with such transactions. Buyer is solely responsible for any such payment, fee or commission that may be due to Merrill Lynch & Co. in connection with the transactions contemplated by this Agreement.

5.5 Acquisition for Investment. Buyer acknowledges that the Stock has not been registered under the Securities Act or under any state securities laws. Buyer is acquiring the Stock solely for its own account and not with a view to any distribution or other disposition of the Stock or any part thereof, or interest therein, except in accordance with the Securities Act. Buyer is an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act).

5.6 Organizational Documents. Copies of the certificate of incorporation and bylaws of Buyer and Holdings have heretofore been delivered to Seller and such copies are true, accurate and complete, without any amendment, modification or supplement, as of the date of this Agreement and the Closing Date (except such amendments, modifications or supplements which would not have a Material Adverse Effect on Seller or which change the amount of authorized capital stock).

5.7 Capitalization of Buyer. (a) All the outstanding shares of capital stock of Buyer are owned, directly or indirectly, by Holdings. As of the Closing Date, investment partnerships affiliated with KKR shall own, directly or indirectly, no less than 70% of the common stock of Holdings, which percentage shall be reduced to reflect any investment made by Parent and/or Seller pursuant to Section 11.3.

(b) In the event that Parent and/or Seller acquires any of the Holdings Common Stock as provided in Section 11.3 hereof, such shares will be duly authorized, validly issued, fully paid and nonassessable, and free of preemptive rights.

5.8 Consents and Approvals. Except for (i) consents, approvals, authorizations, declarations, filings and registrations required by the nature of the business or ownership of Parent, Seller, the Company and the Subsidiaries, (ii) filings in respect of the transactions contemplated hereby

required to be made for compliance with the applicable provisions of the Exchange Act and the rules and regulations promulgated thereunder, (iii) filings under the Securities Act and the rules promulgated thereunder in connection with the sale of the Underwritten Notes and (iv) the filing of premerger notification reports under the HSR Act, no consents, approval or authorization of, or declaration, filing or registration with, any governmental or regulatory authority, or any other Person, is required to be made or obtained by Buyer, Holdings or any of their respective Affiliates in connection with the execution, delivery and performance of this Agreement, the Ancillary Agreements and the consummation of the transactions contemplated hereby and thereby.

5.9 Financial Obligations. Buyer has received and delivered copies to Seller of (i) a commitment letter from senior lenders regarding the transactions contemplated by this Agreement, (ii) the Underwriter Letter, (iii) a letter with respect to equity Financing (other than that to be provided by management of the Company), which letter is addressed to Seller and (iv) an agreement in principal between Buyer and management of the Company with respect to the investment by management referred to in Section 8.19.

5.10 Solvency. At the Closing (after and giving effect to the acquisition of the Stock and the Financing), neither Buyer, Holdings, Trust nor the Company will (i) be insolvent (either because its financial condition is such that the sum of its debts is greater than the fair value of its assets or because the present fair saleable value of its assets will be less than the amount required to pay its probable liability on its debts as they become absolute and matured), (ii) has unreasonably small capital with which to engage in its business or (iii) has incurred or plan to incur debts beyond its ability to pay as they become absolute and matured.

5.11 Trust. (a) As of the Closing, (i) Trust shall have been duly created and be validly existing in good standing as a business trust under the Business Trust Act of the State of Delaware with full business trust power and authority to (A) own property and to conduct its business, (B) issue and perform its obligations under the Preferred Securities and the Common Securities and (C) consummate the transactions contemplated by the Trust Agreement; (ii) Trust shall be duly qualified to transact business as a foreign company and shall be in good standing in any other jurisdiction in which such qualification is necessary, except to the extent that the failure to so qualify or be in good standing would not have a Material Adverse Effect on Trust; (iii) Trust shall not be a party to or otherwise bound by any material agreement other than those listed in Schedule 5.11; (iv) Trust shall be treated for United States federal income tax purposes as a grantor trust and not as an association taxable as a corporation; and (v) Trust shall be reported as a consolidated subsidiary of Holdings pursuant to GAAP.

(b) At the Closing, the Common Securities shall be duly authorized by the Trust Agreement and, when issued and delivered by Trust to Holdings against payment therefor, will be validly issued and (subject to the terms of the Trust Agreement) fully paid and non-assessable undivided beneficial interests in the assets of Trust; the issuance of the Common Securities shall not be subject to preemptive or other similar rights; and at the Closing all of the issued and outstanding Common Securities will be directly owned by Holdings free and clear of any Encumbrances.

(c) Prior to the Closing, the Trust Agreement shall have been duly authorized by Holdings and, at the Closing, will have been duly executed and delivered by Holdings and the Trustees, and will be a legal, valid and binding obligation of Holdings (as depositor) and the Trustees enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

(d) Prior to the Closing, the guarantee agreements relating to Trust shall have been duly authorized by Holdings and, when validly executed and delivered by Holdings, will be a legal, valid and binding obligation of Holdings

enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

(e) Prior to the Closing, the Preferred Securities shall have been duly authorized by the Trust Agreement and, when issued and delivered against payment of the consideration therefor, will be validly issued and (subject to the terms of the Declaration) fully paid and nonassessable undivided beneficial interests in Trust, and will be entitled to the benefits of the Trust Agreement; the issuance of the Preferred Securities shall not be subject to preemptive or other similar rights; and (subject to the terms of the Trust Agreement) holders of Preferred Securities will be entitled to the same limitation of personal liability under Delaware law as extended to stock-holders of private corporations for profit.

(f) Prior to the Closing, the Indenture shall have been duly authorized by Holdings and, assuming due authorization by the trustee thereunder, when validly executed and delivered by Holdings and such trustee, will be a legal, valid and binding obligation of Holdings enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

(g) Prior to the Closing, the Debentures shall have been duly authorized by Holdings and, at the Closing, will have been duly executed by Holdings and, when authenticated in the manner provided for in the Indenture and delivered against payment therefor, will be a legal, valid and binding obligation of Holdings enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing, and will be in the form contemplated by the Indenture.

## ARTICLE VI

## ACTIONS BY PARENT, SELLER, HOLDINGS AND BUYER PRIOR TO THE CLOSING

Parent, Seller, Holdings and Buyer covenant as follows for the period from the date hereof to the Closing Date (except, in the case of Section 6.16, for the period specified in such Section):

6.1 Maintenance of Business and Preservation of Permits and Services. Except as expressly contemplated by this Agreement, Seller shall cause the Company and each Subsidiary to carry on its business, in the ordinary course consistent with past practice. Neither Parent nor Seller shall cause the Company or any Subsidiary to terminate an officer thereof or to diminish the duties or responsibilities of such officer.

6.2 Additional Financial. As soon as reasonably practicable after the end of the applicable period, Seller shall furnish to Buyer (a) the quarterly convention statements of the Subsidiaries for all interim quarterly periods subsequent to September 30, 1995, which shall have been prepared on a basis consistent with the Convention Statements and, with respect to the financial statements included therein, in accordance with Statutory Accounting Principles, (b) the quarterly financial statements of the Company, the GAAP Subsidiaries and Ridge Re for all quarterly periods subsequent to September 30, 1995, which shall have been prepared in accordance with generally accepted accounting principles and on a basis consistent with the Company GAAP Financial Statements, the Subsidiary GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be, subject to normal year-end adjustments and the absence of footnote disclosure, (c) the consolidated financial statements for the Company, each of the GAAP Subsidiaries and Ridge

Re for the year ended December 31, 1995, which shall have been prepared in accordance with generally accepted accounting principles and on a basis consistent with the Company GAAP Financial Statements, the Subsidiary GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be, and (d) (to the extent ordinarily prepared) all monthly financial statements of the Company, the Subsidiaries and Ridge Re (for months subsequent to June 1995), which shall have been prepared in a manner consistent with past practice.

6.3 Certain Prohibited Transactions. Parent and Seller agree to cause the Company and each Subsidiary not to, without the prior written approval of Buyer or except as expressly contemplated by this Agreement:

(a) terminate, cancel or amend any insurance coverage maintained by the Company or any of its Subsidiaries with respect to any material assets of the Company or any Subsidiary which is not replaced by an adequate amount of insurance coverage or is not deemed unnecessary in the reasonable judgment of the Company;

(b) settle any pending or threatened Action relating to an insurance claim in an amount in excess of $5,000,000 above the policy limit relating to such claim or settle any other pending or threatened Action in an amount in excess of $1,000,000; or

(c) take any action which causes any representation or warranty (other than Section 4.7(a)) of Parent or Seller in this Agreement to be or become untrue at Closing or results in a material breach of any covenant made by Parent or Seller in this Agreement.

6.4 Investigation by Buyer. Parent and Seller shall, and shall use their reasonable efforts to cause the Company and the Subsidiaries to, allow Buyer during regular business hours through Buyer's employees, agents and representatives, to make such investigation of the business, properties, books and records of the Company and the Subsidiaries, and to conduct such examination of the condition of the Company and the Subsidiaries, as Buyer reasonably deems necessary or advisable to familiarize itself with such business, properties, books, records, condition and other matters, and to verify the representations and warranties of Seller hereunder; provided, however, that any information obtained from Seller or the Company shall be deemed to be Evaluation Material for purposes of the Confidentiality Agreement dated August 3, 1995, between Seller and Kohlberg Kravis Roberts Co., L.P. (the "Confidentiality Agreement") and shall be subject to the Confidentiality Agreement.

6.5 Consents. (a) As soon as practicable after execution and delivery of this Agreement, Buyer and Seller shall make all filings required under the HSR Act. Buyer and Seller will each furnish all information as may be required by any other state regulatory agency properly asserting jurisdiction or by the Federal Trade Commission and the United States Department of Justice under the HSR Act in order that the requisite approvals for the purchase and sale of the Stock pursuant hereto, and the transactions contemplated hereby, be obtained or to cause any applicable waiting periods to expire.

(b) Buyer shall use its best efforts to file Form A change of control applications with the applicable state insurance regulators referred to in Schedule 4.11 within 45 days from the date hereof. Buyer will use its reasonable efforts to obtain insurance regulatory approvals as soon as possible following the Form A change of control filings. Parent and Seller shall cooperate with Buyer to obtain such approvals.

(c) Seller and Buyer will, as soon as practicable, commence to take all other action required to obtain as promptly as practicable all necessary consents, approvals, authorizations and agreements of, and to give all notices and make all other filings with, any third parties, including governmental authorities, necessary to authorize, approve or permit the consummation of the transactions contemplated hereby and by the Ancillary Agreements, including all consents, approvals and waivers referred to in Sections 7.4 and 8.2 hereof, and Buyer, Parent and Seller shall cooperate with each other with respect thereto.

(d) Buyer and Seller will cooperate in seeking applicable regulatory approval so as to permit the Subsidiaries to continue to pay management fees to the Company following the Closing at the same level as are currently being paid.

(e) Buyer and Seller will cooperate in seeking applicable regulatory approval so as to permit IIC to pay to II prior to Closing an extraordinary dividend of at least $50,000,000. To the extent such approval is obtained, Seller shall cause IIC to pay to II prior to Closing an extraordinary dividend of at least $50,000,000.

(f) Notwithstanding the foregoing, however, none of Parent, Seller, Holdings, Buyer, the Company or the Subsidiaries shall be required to agree to any limitations, requirements or conditions of, any third party including, but not limited to, any insurance regulatory body, or make any payment to any party including the Company or any Subsidiary in order to obtain consents referred to in Sections 7.4 and 8.2. Parent and Seller shall be entitled to have a representative or representatives present at all meetings that may be held by Buyer, Holdings or Trust with insurance regulators.

6.6 Notification of Certain Matters. Parent and Seller, to the extent within the actual knowledge of an officer of Parent or Seller listed on Schedule 1.1B, shall give prompt notice to Buyer, and Buyer, to the extent within the knowledge of Buyer, shall give prompt notice to Seller, of (i) the occurrence, or failure to occur, of any event which occurrence or failure would be likely to cause any representation or warranty contained in this Agreement to be untrue or inaccurate in any material respect any time from the date hereof to the Closing Date, (ii) any material failure of Parent, Seller, Holdings or Buyer, as the case may be, to comply with or satisfy any covenant, condition or agreement to be complied with or satisfied by it hereunder (and each party shall use all reasonable efforts to remedy such failure), (iii) any notice or other communication from any Person alleging that the consent of such Person is or may be required in connection with the transactions contemplated by this Agreement and the Ancillary Agreements, (iv) any notice or other communication from any governmental or regulatory agency or authority in connection with the transactions contemplated by this Agreement and the Ancillary Agreements, (v) any Actions that, if pending or threatened on the date hereof, would have been required to have been disclosed pursuant to Section 4.13 and (vi) any Actions that relate to the consummation of the transactions contemplated by this Agreement and the Ancillary Agreements.

6.7 No Solicitations. (a) Parent, Seller and each of their respective Affiliates, including the Company and the Subsidiaries, will not, directly or indirectly, solicit any inquiries or proposals or enter into or continue any discussions, negotiations, understandings, arrangements or agreements relating to the sale or exchange of any Stock, the merger or amalgamation of the Company or any of its Subsidiaries with, or the direct or indirect disposition of a significant amount of the Company's assets or any Subsidiary's assets or business to any Person other than Buyer and Holdings or their Affiliates or provide any assistance or any information to or otherwise cooperate with any Person in connection with any such inquiry, proposal or transaction (except that the Company may direct inquiries to Buyer, which shall not disclose confidential information about the Company or any of its Subsidiaries in connection with responding to such inquiries). In the event that Parent, Seller or any of their Affiliates, including the Company and the Subsidiaries receives a solicited or unsolicited inquiry, proposal or offer for such a transaction or obtains information that such an offer is likely to be made, Parent and Seller will provide Buyer with notice thereof as soon as practical after receipt thereof, including the identity of the prospective purchaser or soliciting party. Buyer and Holdings agree that to the extent they engage in any discussions regarding the Company or the Subsidiaries with potential purchasers of the capital stock or businesses thereof, Buyer and Holdings shall not include officers or employees of the Company or the Subsidiaries in such discussions.

(b) The parties acknowledge that there may be no adequate remedy at law for a breach of Section 6.7(a) and that money damages may not be an adequate remedy for breach of such Section. Therefore, the parties agree that Buyer shall

have the right, in addition to any other rights it may have, to injunctive relief and specific performance of Section 6.7(a) in the event of any breach of such Section. The remedy set forth in the preceding two sentences is cumulative and shall in no way limit any other remedy any party hereto has at law, in equity or pursuant hereto.

6.8 Cooperation; Accounting and Other. (a) Seller shall, and Seller shall use its reasonable efforts to cause the Company to, cooperate with Buyer in respect of any proposed public offering or private placement of securities, and arrangements of other financing by Buyer, the proceeds of which are to be used to finance a portion of the purchase of the Stock by Buyer (provided, however, that Seller shall not be obligated to participate in such financing or the marketing thereof and shall not be obligated to be a party to any underwriting, private placement or other agreement with respect thereto), and shall, without limitation of the foregoing, cause such Company financial statements to be prepared as may be required by the rules and regulations of the Securities and Exchange Commission promulgated under the Securities Act.

(b) Buyer shall give Seller and Parent a reasonable opportunity to review any references to Seller, Parent, this Agreement or the transactions contemplated hereby in any registration statement or private placement memorandum relating to the sale of securities the proceeds of which are to be used to finance a portion of the purchase of the Stock by Buyer and any amendments or supplements thereto by providing to Seller and Parent drafts of such registration statement or private placement memorandum or any amendments or supplements thereto prior to filing such documents with the Securities and Exchange Commission or distributing such documents to potential purchasers of privately placed securities and allow Seller and Parent a reasonable opportunity (as determined under the circumstances and consistent with the overall timing constraints applicable to preparation of such registration statement, private placement memorandum, amendment or supplement) to review and comment thereon.

6.9 Investment Portfolio. (a) Parent and Seller shall cause the Company and the Subsidiaries to manage the investment portfolio for the Company and the Subsidiaries in accordance with the Investment Policy.

(b) Five days prior to the Closing Date, Parent and Seller shall cause the Company to deliver to Buyer a list of all Investments in the investment portfolio for the Company and the Subsidiaries as of such date.

6.10 Reinsurance Agreements. Seller shall cause the Company and each Subsidiary not to, without the prior written approval of Buyer (which approval shall not be unreasonably withheld), except in the ordinary course of business consistent with past practice (i) except for the Ridge Re Endorsements, amend any reinsurance or retrocession agreement, (ii) enter into or commit to enter into any loss portfolio transfer or other similar transaction, agreement or arrangement or series of related transactions, agreements or arrangements involving any ceded reinsurance of the Company or any Subsidiary, (iii) enter into or commit to enter into any reinsurance or retrocession contract or treaty except to replace, renew or extend existing reinsurance and retrocession agreements and treaties on terms which are not different in any material respect from the terms of the agreement or treaty being replaced, renewed or extended, as the case may be, or (iv) commute or terminate any contract of reinsurance, provided that Seller shall cause the Company and each Subsidiary not to commute or terminate any such contract which at the time of commutation or termination is legally carried on the books of the Company and the Subsidiaries in an amount of $5,000,000 or more. All reinsurance or retrocession agreements or treaties permitted by this Section shall not have a change of control or similar provision which would require the Company or any Subsidiary to obtain a consent to consummate the transactions contemplated hereby (unless such provisions shall have been waived prior to Closing).

6.11 Dividends. Seller and Parent shall cause the Company not to (i) declare, set aside or pay any dividends or distributions (whether in cash, stock or property) in respect of any capital stock of the Company, (ii) make any other payment or distribution to Parent, Seller or any Affiliate of Parent (excluding the Company and the Subsidiaries, but including TRG and its

subsidiaries), or (iii) redeem, purchase or otherwise acquire any of the capital stock of the Company or any Subsidiary, except for (A) payments permitted under the Tax Agreement, (B) payments under the contracts, agreements or arrangements referred to in Schedule 4.23 or described in clauses (i), (ii) or (iii) of Section 4.23(b), (C) the dividends contemplated by Sections 6.18(i) and 9.7 and (D) distributions to Seller of any proceeds received by the Company (gross of any income tax obligations) from the First Quadrant Final Sale or of any amounts received by the Company (gross of any income tax obligations) as proceeds or purchase price adjustments from the Viking Sale or Constitution Re Sale. For purposes of the exception set forth in (D) in the preceding sentence, proceeds shall include any amounts (net of any state tax obligations for which the Company is liable under the stock purchase agreement for the company whose sale generated such proceeds) subsequently received after the date of this Agreement with respect to tax payments from such companies but shall not include any tax payments previously received. In addition, as soon as practicable after the date of this Agreement, the Company shall distribute $100,000 to Seller in respect of the Constitution Re 1994 tax shortfall.

6.12 Seller Notes. The Company and the Subsidiaries shall not dispose of the Seller Notes to a Person other than a Subsidiary, except that the Company and the Subsidiaries may dispose of all or a portion of the Seller Notes prior to Closing to a Person other than a Subsidiary if upon such disposition Seller shall pay to the Company the excess of (i) the aggregate principal amount of the Seller Notes so disposed plus accrued but unpaid interest through the date of such disposition over (ii) the Third Party Amount. To the extent not already disposed of, immediately prior to Closing, (i) Seller shall repay the outstanding principal amounts and any accrued but unpaid interest thereon under the Seller Notes issued by it and held at that time by the Company or any Subsidiary and (ii) Parent shall cause Credit Corp. to repay the outstanding principal amounts and any accrued but unpaid interest thereon under the Seller Notes issued by Credit Corp. and held at that time by the Company or any Subsidiary.

6.13 Leesburg Training Facility. The Company and the Subsidiaries shall not dispose of any of their interests in the ground lease agreement among Parent and certain of the Subsidiaries or the lease agreement among Seller and such Subsidiaries, each dated as of December 1, 1985 and each relating to approximately six acres of land in Loudon County, Virginia and a training facility located thereon or their fee interests in such facility (the "Leesburg Training Facility"), to a Person other than a Subsidiary, except that the Company and the Subsidiaries may dispose of their interests (in whole or in part) in the Leesburg Training Facility prior to Closing to a Person other than a Subsidiary if upon such disposition Seller pays to the Company the excess of (i) the greater of $118,000,000 and the statutory carrying value of the Leesburg Training Facility as of December 31, 1995 over (ii) the Third Party Amount. If no Third Party Amount has been received by the Company or any Subsidiary prior to the Closing, immediately prior to Closing, Parent and Seller agree to cause an amount equal to the greater of (i) the statutory carrying value of the Leesburg Training Facility as of December 31, 1995 and (ii) $118,000,000, to be contributed to such Subsidiaries, allocated to such Subsidiaries in accordance with Schedule 6.13 (such contributed amount, the "Leesburg Training Facility Amount"). At Closing, the Company shall cause to be transferred to Seller or an Affiliate of Seller any remaining interests the Company or any of the Subsidiaries has in the Leesburg Training Facility. Upon any transfer of the Leesburg Training Facility in accordance with this Section 6.13, the Company and the Subsidiaries shall have no further rights or obligations relating to the Leesburg Training Facility.

6.14 Reserves and Book-Up. (a) Effective as of December 31, 1995, Parent and Seller shall cause the reserves of CFI and its subsidiaries and WSG and its subsidiaries for periods prior to December 31, 1992 to be increased for statutory accounting and GAAP purposes in an amount so that after 85% of such increase is ceded to Ridge Re pursuant to the applicable Ridge Re Treaties, CFI and its subsidiaries and WSG and its subsidiaries shall have ceded to Ridge Re the maximum amount of losses and loss adjustment expenses permitted under the applicable Ridge Re Treaties. Immediately following such increases and effective as of December 31, 1995, Parent and Seller shall cause CFI and

its subsidiaries and WSG and its subsidiaries to make the cession referred to in the immediately preceding sentence.

(b) Effective as of December 31, 1995 Parent and Seller shall cause II and its subsidiaries to increase their reserves for statutory accounting and GAAP purposes by an additional $50,000,000 and cede 85% of such increase to Ridge Re pursuant to the applicable Ridge Re Treaty.

(c) During 1996 and at least one day prior to the Closing Date, Parent and Seller shall cause the reserves of CFI and its subsidiaries and WSG and its subsidiaries to be increased for statutory accounting and GAAP purposes in the amounts specified by Buyer and/or Seller, but not to exceed an additional $115,000,000 and $100,000,000, respectively (beyond the increases required by paragraph (a) above).

6.15 Rating Agency Presentations. Buyer shall give Seller reasonable notice of any meetings prior to the Closing Date with A.M. Best & Co. ("A.M. Best") to discuss the insurance claims paying ratings of the Insurance Subsidiaries, and Seller at its option may have a representative at such meetings.

6.16 Certain Admitted Assets. Parent and Seller shall indemnify, guaranty or otherwise post credit support to the extent that as of the Closing Date the Insurance Subsidiaries shall not have received credit for statutory purposes for the Crostex/Camfex Purchase Money Notes in an amount equal to at least $35 million. Such indemnity, guaranty or credit support shall continue until final maturity of such notes but only in the amount provided in the preceding sentence.

6.17 Intercompany Accounts. (a) Except as provided in Sections 6.12 and 6.13, all intercompany accounts (other than those relating to Taxes and those under or relating to reinsurance contracts and arrangements) between the Company and any Subsidiary, on the one hand, and Parent and any of its Affiliates (other than the Company and its Subsidiaries), on the other hand, as of the Closing shall be settled at fair value (irrespective of the terms of payment of such intercompany accounts) in the manner provided in this Section. At least five business days prior to the Closing, Seller shall prepare and deliver to Buyer a statement setting out in reasonable detail the calculation of all such intercompany account balances based upon the latest available financial information as of such date and, to the extent reasonably requested by Buyer, provide Buyer with supporting documentation to verify the underlying intercompany charges and transactions. All such intercompany account balances shall be paid in full in cash prior to the Closing. All intercompany reinsurance agreements shall remain in effect and shall be settled in the ordinary course of business. All intercompany accounts relating to Taxes will be governed by the Tax Agreement.

(b) As promptly as practicable, but no later than 60 days after the Closing Date, Seller shall cause to be prepared and delivered to Buyer a statement setting out in reasonable detail the calculation of such intercompany account balances as of the Closing Date (giving effect to any settlement under subsection (a) and any other payments). Buyer and Seller shall cooperate in the preparation of any such calculation including the provision of supporting documentation to verify the underlying intercompany charges, transactions and payments. If Buyer disagrees with Seller's calculation of such intercompany balances Buyer may, within 30 days after delivery of such statement, deliver a notice to Seller disagreeing with such calculation and setting forth Buyer's calculation of such amount. If Buyer and Seller are unable to resolve such disagreement within 30 days thereafter, such disagreement shall be resolved by independent accountants of nationally recognized standing reasonably satisfactory to Buyer and Seller. The net amount of any such intercompany balance shall be paid in cash promptly thereafter, together with interest thereon from and including the Closing Date to but excluding the date of payment at a rate equal to 5% per annum. Such interest shall be payable at the same time as the payable to which it relates and shall be calculated daily on the basis of a year of 365 days and the actual number of days elapsed.

6.18 Certain Required Transfers. Prior to the Closing Date, Parent and Seller shall cause TRG to transfer all of the outstanding capital stock of

Envision to the Company.

6.19 Financing. Buyer shall use its reasonable efforts to obtain financing that will satisfy the condition in Section 8.9 hereof.

6.20 Dividends Received by TRG. In the event that Seller receives cash dividends from TRG between January 1, 1996 and the Closing, immediately prior to Closing Seller shall make a capital contribution to the Company in an amount (the "TRG Contributed Dividends") equal to the lesser of the dividends so received and the TRG Dividend Replacement Amount. Seller shall use reasonable efforts to have TRG's subsidiaries distribute the fullest amount permitted by insurance regulators and applicable law (not to exceed the TRG Dividend Replacement Amount) to it prior to Closing.

6.21 Capital Contribution by Seller. Immediately prior to Closing, Seller shall make a capital contribution to the Company in an amount equal to $1,700,000.

6.22 TOPrS. Seller and Buyer shall, and Holdings shall cause an affiliated investment partnership to, execute and deliver the TOPrS Side Letter at the Closing.

6.23 Subsidiary Credit Agreements. In the event any indebtedness under any Subsidiary Credit Agreement is prepaid, including by reason of any acceleration thereof, with funds contributed by Seller for the purpose of such prepayment, the cash payable pursuant to Section 2.2 shall be increased by an amount equal to such indebtedness. No such prepayment shall constitute a breach of this Agreement.

# ARTICLE VII

## CONDITIONS TO OBLIGATIONS OF PARENT AND SELLER

The obligations of Parent and Seller to consummate the transactions contemplated hereby on the Closing Date are subject, in the discretion of Parent and Seller, to the satisfaction or waiver, on or prior to the Closing Date, of each of the following conditions:

7.1 Representations, Warranties and Covenants. All representations and warranties of Buyer and Holdings contained in this Agreement and the Ancillary Documents to which Buyer or Holdings is a party shall be true and correct in all material respects (except that such representations and warranties specifically qualified by materiality shall be read for purposes of this Section so as not to require an additional degree of materiality) as of the date of this Agreement and (except to the extent such representations and warranties speak as of an earlier date) as of the Closing Date as if such representations and warranties were made on and as of the Closing Date, any breaches of such representations and warranties as of the Closing Date (determined for purposes of this clause without regard to any materiality qualifications in such representations and warranties) taken together shall not have a Material Adverse Effect on Holdings, Buyer, the Company and the Subsidiaries, taken as a whole (assuming that the Closing shall have occurred), or on Parent or Seller, and Buyer and Holdings shall have performed in all material respects all agreements and covenants required hereby to be performed by them prior to or at the Closing Date. There shall be delivered to Seller a certificate (signed by the President of Buyer and the President of Holdings) to the foregoing effect.

7.2 HSR Act. The applicable waiting period, including any extension thereof, under the HSR Act shall have expired.

7.3 No Governmental or Other Proceeding; Illegality. (a) No Action shall be pending or threatened which seeks to enjoin, restrain or prohibit the consummation of the transactions contemplated by this Agreement (including, without limitation, the execution, delivery and performance of any Ancillary Agreement by the parties thereto) which either Parent or Seller reasonably believes presents a material risk that it or its Affiliates would suffer

substantial monetary damage (whether or not indemnified under this Agreement).

(b) There shall not be in effect any statute, rule, regulation or order of any court, governmental or regulatory body which prohibits or makes illegal the transactions contemplated hereby, including, without limitation, the execution or delivery of any of the Ancillary Agreements or the performance of any of the Guarantees, the Tax Agreement or the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsements.

7.4 Consents. All consents, approvals and waivers from governmental authorities and other parties necessary to permit Seller and Parent to consummate the transactions contemplated hereby shall have been obtained, unless the failure to obtain any such consent, approval or waiver would not have a Material Adverse Effect on Seller or Parent, as the case may be, provided, however, that no such consent, approval or waiver shall contain any limitations, requirements or conditions on Parent or Seller or require Parent or Seller to make any payment to any party including the Company or any Subsidiary.

7.5 Opinion of Counsel. Buyer shall have delivered to Seller an opinion of Simpson Thacher & Bartlett, substantially in the form of Exhibit E-1, an opinion of King & Spalding, special tax counsel to Holdings and Buyer, substantially in the form of Exhibit E-2, and an opinion of Richards, Layton & Finger, special Delaware counsel to Holdings and Buyer, substantially in the form of Exhibit E-3.

7.6 Certificates. Buyer and Holdings will furnish Seller with such certificates of their respective officers, directors and others to evidence compliance with the conditions set forth in this Article VII as may be reasonably requested by Seller.

7.7 Corporate Documents. Seller shall have received from Buyer and Holdings resolutions adopted by the Board of Directors of Buyer and Holdings approving this Agreement, the Tax Agreement, the TOPrS Side Letter and the Debentures, as applicable, and the transactions contemplated hereby and thereby, certified by the corporate secretary or assistant secretary of Holdings and Buyer, as applicable.

7.8 TRG Closing. TRG Acquisition shall have simultaneously purchased all of the outstanding shares of TRG capital stock pursuant to the TRG Agreement.

7.9 Registration Rights Agreement. Trust and Holdings shall have executed and delivered to Seller a Registration Rights Agreement substantially in the form of Exhibit F.

7.10 Solvency Matters. Buyer shall have provided to Seller, any solvency letters or similar opinions or certificates relating to the solvency and adequate capitalization of Buyer, Holdings or the Company and/or the ability of Buyer, Holdings or the Company to pay its debts that are given to any banks or other lenders in connection with the acquisition of the Stock at the same time as such letters, opinions or certificates are provided to such banks or other lenders.

7.11 Capitalization. Holdings shall have received no less than $500,000,000 in equity and the amount of indebtedness for borrowed money of Holdings and Buyer shall be no more than $1,325,000,000 (excluding the Debentures).

7.12 Company Certificates. Seller shall have received (i) a certificate signed by each of the persons listed on Schedule 1.1C dated as of the date of this Agreement, and (ii) a certificate signed by each of such persons dated as of the Closing Date, in each case substantially in the form of Exhibit G.

7.13 Subsidiary Releases. All of the domestic U.S. Subsidiaries included in the consolidated federal income tax return of Parent which are Subsidiaries as of Closing shall have executed and delivered to Parent and Seller the releases of any and all obligations under existing tax sharing agreements substantially in the form of Exhibit H.

## ARTICLE VIII

## CONDITIONS TO OBLIGATIONS OF HOLDINGS AND BUYER

The obligations of Holdings and Buyer to consummate the transactions contemplated hereby are subject, in the discretion of Buyer, to the satisfaction or waiver, on or prior to the Closing Date, of each of the following conditions:

8.1 Representations, Warranties and Covenants. All representations and warranties of Parent and Seller contained in this Agreement and the Ancillary Agreements to which Parent or Seller is a party shall be true and correct in all material respects (except that such representations and warranties specifically qualified by materiality shall be read for purposes of this Section so as not to require an additional degree of materiality) as of the date of this Agreement and (except to the extent such representations and warranties speak as of an earlier date) as of the Closing Date as if such representations and warranties were made on and as of the Closing Date, any breaches of such representations and warranties as of the Closing Date (determined for purposes of this clause without regard to any materiality qualifications in such representations and warranties) taken together shall not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, and Parent and Seller shall have performed in all material respects all agreements and covenants (other than those contained in Section 6.3(c) and clauses (i), (ii) and (v) of Section 6.6) required hereby to be performed by them, respectively, prior to or at the Closing Date. There shall be delivered to Buyer a certificate of each of Parent and Seller (signed by an Executive Vice President of Parent and the President of Seller) to the foregoing effect.

8.2 Consents. All consents, approvals and waivers (a) referred to in clauses (i) and (ii) of Section 4.11, (b) referred to on Schedule 4.10, (c) under reinsurance and retrocession agreements for the accident year in which the Closing occurs that would be terminable as a result of consummation of the transactions contemplated by this Agreement and the Ancillary Agreements, (d) under all other reinsurance and retrocession agreements that would be terminable as a result of consummation of the transactions contemplated by this Agreement and the Ancillary Agreements and (e) under the reinsurance treaties described in Ex. 1 (part A) of Schedule 4.25 shall have been obtained in form and substance satisfactory to Buyer, acting reasonably, and shall be in full force and effect, except, in the case of consents, approvals and waivers referred to in clauses (b), (c) and (d), consents, approvals or waivers the failure of which to obtain would not, individually or in the aggregate, result in a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, provided, however, that in the case of clauses (a), (b), (c), (d) and (e), no such consent, approval or waiver shall contain any limitations, requirements or conditions on Holdings, Buyer, the Company or a Subsidiary or require Holdings, Buyer, the Company or a Subsidiary to make any payment to any party including in the case of Holdings or Buyer, to the Company or, in the case of Holdings, Buyer or the Company, to any Subsidiary, provided further, that the approval of any intercompany tax agreements referred to in either Section 4.11(i) or (ii) for a period after Closing shall not be a condition to the obligations of Buyer and Holdings hereunder, and provided still further, that with respect to any intercompany tax agreement among the Company and the Subsidiaries for the period January 1, 1995 through Closing, the obligations of Buyer and Holdings hereunder shall be conditioned only on the approval of an agreement that is reasonably consistent with those provisions of the Tax Agreement that provide for the amount and time for payments attributable to Taxes.

8.3 HSR Act. The applicable waiting period, including any extension thereof, under the HSR Act shall have expired.

8.4 No Governmental or Other Proceeding; Illegality. (a) No Action shall be pending or threatened which seeks to enjoin, restrain or prohibit the consummation of the transactions contemplated by this Agreement (including, without limitation, the execution, delivery and performance of any Ancillary Agreement by the parties thereto) or to impose limitations on the ability of

Buyer to exercise full rights of ownership of the Stock or to require the divestiture by Buyer of the Stock or by the Company, Buyer, Holdings or any of their Affiliates of any assets or businesses, which either Holdings or Buyer reasonably believes presents a material risk that it or its Affiliates (including the Company and the Subsidiaries after the Closing Date) would not realize substantially all of the benefits of the transactions contemplated by this Agreement or would suffer substantial monetary damages (whether or not indemnified under this Agreement).

(b) There shall not be in effect any statute, rule, regulation or order of any court, governmental or regulatory body which prohibits or makes illegal the transactions contemplated hereby, including, without limitation, the execution or delivery of any of the Ancillary Agreements or the performance of any of the Guarantees, the Tax Agreement or the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsements.

8.5 Opinion of Counsel. Seller shall have delivered to Buyer an opinion of Skadden, Arps, Slate, Meagher & Flom, substantially in the form of Exhibit I-l, an opinion of Richard S. Paul, Senior Vice President and General Counsel of Seller, substantially in the form of Exhibit I-2, an opinion of Richard N. Frasch, general counsel of the Company, substantially in the form of Exhibit I-3, an opinion of Cox & Wilkinson, special Bermuda counsel to Parent and Seller, substantially in the form of Exhibit I-4, an opinion of LeBoeuf, Lamb, Greene & MacRae, special tax counsel to Parent and Seller, as to the matters set forth in Exhibit I-5, which opinion shall otherwise be in form and substance reasonably satisfactory to Buyer, an opinion of counsel (who shall be reasonably acceptable to Buyer) as to matters of Indiana law set forth in Exhibit I-6, which opinion shall otherwise be in form and substance reasonably satisfactory to Buyer, and an opinion of counsel (who shall be reasonably acceptable to Buyer) as to matters of New Jersey law set forth in Exhibit I-7, which opinion shall otherwise be in form and substance reasonably satisfactory to Buyer.

8.6 Certificates. Parent and Seller shall furnish Buyer with such certificates of the respective officers of Parent and Seller and others to evidence compliance with the conditions set forth in this Article VIII as may be reasonably requested by Buyer.

8.7 Corporate Documents. Buyer shall have received from Parent and Seller resolutions adopted by the respective boards of directors of Parent and Seller approving this Agreement and the other Ancillary Agreements to which Parent or Seller is or will be a party and the transactions contemplated hereby and thereby, certified by the corporate secretary or assistant secretary of Parent and Seller, as applicable.

8.8 Closing. TRG Acquisition shall have simultaneously purchased all of the outstanding shares of TRG's capital stock pursuant to the TRG Agreement.

8.9 Financing. Buyer shall have obtained proceeds from financing sources on terms and conditions consistent with the Underwriter Letter and with the senior bank commitment letter provided by Buyer to Seller prior to the date hereof, and otherwise reasonably satisfactory to Buyer.

8.10 No Material Adverse Effect. Since June 30, 1995, there shall not have occurred any event, change or development (including, without limitation, the suspension, revocation or other termination of any Permit) which individually or in the aggregate, has had or is reasonably likely to have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

8.11 No Change in Rating. Buyer shall have received confirmation from A.M. Best that upon Closing the A.M. Best's policyholder's rating for each Insurance Subsidiary will be "A-" (without negative implications) or better, and after giving effect to the transactions contemplated by this Agreement, the Ancillary Agreements and the Financing Documents.

8.12 Resignation of Officers and Directors. All Persons who are directors and/or officers of the Company and/or any of the Subsidiaries whose principal employment is as an officer and/or employee of Seller and/or Parent, shall

have resigned such directorships and/or such offices.

8.13 Transfer Taxes. Seller shall have caused all appropriate stock transfer tax stamps to be affixed to the certificate or certificates representing the Stock.

8.14 Seller Notes. Seller and Credit Corp. shall have made the payments contemplated by Section 6.12 and repaid all amounts outstanding under any Seller Notes that are still held by the Company and any Subsidiary together with any accrued but unpaid interest thereon.

8.15 Leesburg Training Facility Amount. The Leesburg Training Facility Amount shall have been paid, as provided in Section 6.13.

8.16 Reserves and Book-Up. All of the transactions described in Section 6.14 shall have been consummated.

8.17 Ridge Re Endorsements. Ridge Re, Seller and each Subsidiary listed on Schedule 8.17 shall have executed and delivered to Buyer endorsements to the Ridge Re Treaties substantially in the form of Exhibit J.

8.18 Guarantees. Parent shall have executed and delivered to Buyer guarantees for the benefit of each Subsidiary listed on Schedule 8.18 substantially in the form of Exhibit K and Parent and Seller shall have executed and delivered to Buyer guarantees for the benefit of each Subsidiary listed on Schedule 8.18 substantially in the form of Exhibit L.

8.19 Management Investment. Members of the management of the Company and the Subsidiaries designated by Holdings shall have invested in the capital stock of Holdings on terms substantially consistent with the agreements in principle delivered to Seller prior to the date hereof or otherwise satisfactory to Holdings.

## ARTICLE IX

## ACTIONS BY PARENT, SELLER,AND BUYER AFTER THE CLOSING

9.1 Books and Records. Parent, Seller and Buyer agree that so long as any books, records and files relating to the business, properties, assets or operations of the Company or the Subsidiaries, to the extent that they pertain to the operations of the Company or the Subsidiaries prior to the Closing Date, remain in existence and available, each party (at its expense) shall have the right to inspect and to make copies of the same at any time during normal business hours for any proper purpose. Parent and Seller further agree that, to the extent such records have not otherwise been delivered to the Company or Buyer, Parent and Seller will not destroy or dispose of any material books, records or files relating to the investment portfolio existing as of the Closing Date without first offering to provide such books, records or files to Buyer and that, in any event, Buyer shall have the right to inspect and to make copies of the same at any time during normal business hours for any proper purpose, to the extent reasonably requested by Buyer.

9.2 First Quadrant Final Sale, Viking Sale and Constitution Re Sale. If the Company shall, after the Closing Date, receive any proceeds from the First Quadrant Final Sale, or any amount as purchase price adjustments from the Viking Sale or Constitution Re Sale, Buyer shall cause the Company to remit such amounts (net of any tax obligation of Buyer, the Company or any Subsidiary) to Seller as promptly as practicable.

9.3 Covenants Regarding the Securities. In connection with any sale, transfer or other disposition of all or any part of the Securities under an exemption from registration under the Securities Act, if requested by Buyer, Seller (or Parent, if such Securities are held by Parent) will deliver to Holdings an opinion of counsel (which may be the General Counsel of Parent or, if such Securities are held by Seller, of Seller), reasonably satisfactory in form and substance to Holdings, that such exemption is available; provided, however, that in case of any sale or other transfer of Securities to any

Person who is a qualified institutional buyer as defined in Rule 144A under the Securities Act, no opinion of counsel shall be required if Seller (or Parent, if such Securities are held by Parent) provides to Holdings an officer's certificate to the effect that such Person is a qualified institutional buyer as defined in Rule 144A under the Securities Act. Parent and Seller hereby agree and acknowledge that upon original issuance thereof, and until such time as the same is no longer required under the applicable requirements of the Securities Act, the Securities (and all securities issued in exchange therefor or substitution thereof) shall bear, until such restrictions are no longer applicable, the following legend:

"THE SECURITIES REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 ACT"). THEY MAY NOT BE SOLD OR TRANSFERRED EXCEPT IN COMPLIANCE WITH THE REGISTRATION PROVISIONS OF THE 1933 ACT AND ANY APPLICABLE STATE BLUE SKY LAWS OR SECURITY LAWS OR PURSUANT TO AN AVAILABLE EXEMPTION FROM SUCH PROVISIONS."

Parent and Seller further agree and acknowledge that any Holdings Common Stock acquired in accordance with Section 11.3 shall also bear (until such time as such restrictions are no longer applicable) the following legend:

"THE SECURITIES REPRESENTED BY THIS CERTIFICATE ARE SUBJECT TO A RIGHT OF FIRST REFUSAL AND CERTAIN OTHER RESTRICTIONS ON TRANSFER AS SET FORTH IN THAT CERTAIN STOCKHOLDERS AGREEMENT, BETWEEN NEW TALEGEN HOLDINGS CORPORATION AND XEROX FINANCIAL SERVICES, INC., A COPY OF WHICH MAY BE OBTAINED FROM THE SECRETARY OF NEW TALEGEN HOLDINGS CORPORATION."

9.4 Crostex/Camfex Purchase Money Notes. Seller and Parent shall indemnify, guaranty or otherwise post credit support pursuant to the covenant set forth in Section 6.16 from and after the Closing.

9.5 Certain Employee Benefit Matters. (a) Parent and its Affiliates (other than the Company, the Subsidiaries, TRG and its subsidiaries) shall retain all liabilities and obligations under the employee stock ownership plan ("ESOP") in which employees of the Company and the Subsidiaries participated prior to January 1, 1993. All awards made to such participants under the ESOP shall fully vest as of the Closing Date.

(b) Parent and its Affiliates (other than the Company, the Subsidiaries, TRG and its subsidiaries) shall retain all liabilities and obligations under the Long Term Incentive Program for the benefit of the participants listed on Schedule 9.5. All payments due to such participants under the Long Term Incentive Program shall be made at Closing.

9.6 Transfer Taxes. Seller shall pay, or cause to be paid, all stock transfer and other transfer taxes required to be paid in connection with the sale and delivery to Buyer of the Stock.

9.7 Dividends Received by TRG. To the extent that the TRG Dividend Replacement Amount exceeds the TRG Contributed Dividends as of Closing, Seller shall cause TRG to declare and pay at Closing a dividend to Seller in the form of a promissory note issued by TRG and in a principal amount equal to such excess, and immediately thereafter Seller shall contribute such note to the Company and assign to the Company all its rights thereunder. Such note shall be payable at such times as TRG shall have cash available (after the payment of its indebtedness and other corporate expenses). Interest shall accrue thereon at a rate per annum equal to the Overdue Rate (as defined in the Tax Agreement).

9.8 Ridge Re. On and after the Closing Date, Parent and Seller shall cause Ridge Re to refrain from (i) entering into any reinsurance or retrocession agreement or treaty and (ii) engaging in any business other than in connection with the Ridge Re Treaties, as amended by the applicable Ridge Re Endorsements, and the other treaties referenced in the first sentence of Section 4.9(c) as in effect on the date hereof, provided that the obligations contained in this Section 9.8 shall terminate upon consummation of the sale of Ridge Re to a Qualified Transferee.

9.9 Further Assurances. On and after the Closing Date, Parent, Seller, the Company, Holdings and Buyer will take all appropriate action and execute all documents, instruments or conveyances of any kind which may be reasonably necessary or advisable to carry out any of the provisions hereof, including without limitation, putting Buyer in possession and operating control of the business of the Company.

## ARTICLE X

## INDEMNIFICATION

10.1 Survival of Representations and Warranties. Holdings and Buyer have the right to rely fully upon the representations, warranties, covenants and agreements of Parent and Seller contained in this Agreement and the Ancillary Agreements. Parent and Seller have the right to rely fully upon the representations, warranties, covenants and agreements of Holdings and Buyer contained in this Agreement and the Ancillary Agreements. All such representations and warranties (including the Schedules hereto and the certificates delivered in accordance with Sections 7.1 and 8.1 hereof, insofar as the Schedules and such certificates relate to such representations and warranties) shall be deemed to be repeated at Closing for purposes of this Article X and, except as set forth in the last sentence of this Section, shall survive the execution and delivery hereof and the Closing, and thereafter (i) in the case of the representations and warranties contained in Sections 4.1, 4.2, 4.3, 4.4, 4.5, 4.6, 4.18, 5.1, 5.2, 5.4, 5.7 and 5.11 (other than clauses (iii), (iv) and (v) of Section 5.11(a)) hereof, such representations and warranties shall survive without limitation as to time, (ii) in the case of the representations and warranties contained in Sections 4.21, 4.24 and 4.28 hereof, such representations and warranties shall survive until 90 days after the expiration of the applicable statute of limitations with respect to the subject matter thereof and (iii) in the case of all other representations and warranties, such representations and warranties shall expire on the date two years following the Closing Date; provided, however, that any representation or warranty shall survive the time it would otherwise terminate pursuant to this Section to the extent that notice of a breach thereof giving rise to a right of indemnification shall have been given by a party hereto in accordance with Section 10.3 hereof prior to such time. All of the covenants and agreements of the parties contained in this Agreement and the Ancillary Agreements to be performed on or after the date of this Agreement shall survive the Closing without limitation as to time. Notwithstanding the foregoing, none of the following representations and warranties (including the Schedules hereto and the certificates delivered in accordance with Sections 7.1 and 8.1 hereof, insofar as the Schedules and such certificates relate to such representations and warranties) shall survive the Closing: (i) representations and warranties contained in Sections 4.16, 4.21(e), 4.21(h) and 5.10 and in clauses (iii), (iv) and (v) of Section 5.11(a); and (ii) representations and warranties contained in any Section of Article IV and which relate to Excluded Activities.

10.2 Indemnification. (a) Parent and Seller shall jointly and severally defend, indemnify and hold harmless Buyer, the Company and their Affiliates and each director and officer of such Persons against any loss, damage, claim, liability, judgment or settlement of any nature or kind, including all costs and expenses relating thereto, including without limitation, interest, penalties and reasonable attorneys' fees (collectively "Damages"), arising out of, resulting from or relating to:

(i) subject to Section 10.1, the breach of any representation or warranty of Parent or Seller contained in this Agreement (other than in Section 4.18), any Ancillary Agreement or any certificate delivered pursuant hereto or thereto; provided, however, that such Persons shall be entitled to indemnification hereunder only when and to the extent that the aggregate of all such Damages exceeds $10,000,000;

(ii) the breach of any covenant or agreement (whether to be performed prior to or after Closing) of Parent or Seller contained in this Agreement, any Ancillary Agreement or any certificate delivered pursuant hereto or thereto;

(iii) any facts, circumstances, conditions, events or actions existing or occurring at any time with respect to Constitution Re, First Quadrant and Viking and any subsidiary of any of the foregoing (other than liabilities related to the business represented by the First Quadrant Asset Sale) (collectively, the "Excluded Business");

(iv) any Action brought by a security holder or creditor of Seller or Parent in their capacity as such;

(v) long term incentive payments (including payments arising out of the sale of the Company or the Excluded Business) payable to the Persons listed on Schedule 10.2 including payments under the Long Term Incentive Program;

(vi) the breach of the representations and warranties contained in Section 4.18;

(vii) any facts, circumstances, conditions, events or actions existing or occurring after the Closing Date with respect to the Leesburg Training Facility; and

(viii) the breach, if any, by CFI or WSG of the respective Subsidiary Credit Agreement to which it is a party in connection with any of the reserving actions described in Section 6.14(a).

The foregoing provisions of this Section 10.2(a) shall not apply with respect to any Damages arising out of (and no indemnification hereunder shall be available with respect to) any (i) breach of any representation or warranty of Parent or Seller that is terminated as provided in Section 10.1 (subject, however, to the proviso contained in Section 10.1), (ii) breaches of the representations and warranties of Parent and Seller contained in this Agreement and the Ancillary Agreements which would result in the failure of any of the conditions in Section 8.1 to be satisfied if Holdings or Buyer had actual knowledge of such breaches (or received notice thereof pursuant to Section 6.6) prior to the Closing Date, (iii) breach of any representation or warranty contained in Section 4.21(h), (iv) breach of any representation or warranty to the extent it relates to Excluded Activities, (v) action that breaches Section 6.3(c) to the extent such action relates to Excluded Activities (except if such action is directed by Parent or Seller or, prior to or at the time taken, an officer listed on Schedule 1.1B knew that such action was to be taken), (vi) breach of any covenant to be performed prior to Closing to the extent it relates to Excluded Activities, other than a breach of Section 6.1, 6.3(a), 6.3(b), 6.10 or 6.14, (vii) action that breaches Section 6.2 or Section 6.9 (except in each case if such action is directed by Parent or Seller or, prior to or at the time taken, an officer listed on Schedule 1.1B knew that such action was to be taken) or (viii) underfunding of Company Plans (including fines and penalties assessed by governmental authorities relating thereto).

(b) Buyer shall defend, indemnify and hold harmless Seller, Parent and their Affiliates and each director or officer of such Persons against any Damages arising out of, resulting from or relating to:

(i) subject to Section 10.1, the breach of any representation or warranty of Holdings or Buyer contained in this Agreement (other than in Section 5.4), any Ancillary Agreement or any certificate delivered pursuant hereto or thereto; provided, however, that such Persons shall be entitled to indemnification hereunder only when and to the extent that the aggregate of all such Damages exceeds $10,000,000;

(ii) the breach of any covenant or agreement (whether to be performed prior to or after Closing) of Holdings or Buyer contained in this Agreement, any Ancillary Agreement or any certificate delivered pursuant hereto or thereto;

(iii) third party claims in connection with the sale of the Underwritten Notes, provided that (x) such Damages did not result from any act or omission by Parent, Seller or any Affiliate (other than the Company or any Subsidiary) or any director, officer, employee or agent thereof and (y) any Notice (as

defined in Section 10.3 below) related to an indemnification claim under this clause (iii) must be delivered prior to the third anniversary following the Closing Date and no Notice may be delivered thereafter; and

(iv) the breach of the representations and warranties contained in Section 5.4.

The foregoing provisions of this Section 10.2(b) shall not apply with respect to any Damages arising out of (and no indemnification hereunder shall be available with respect to) any (i) breach of any representation or warranty of Holdings or Buyer that is terminated (subject, however, to the proviso contained in Section 10.1), (ii) breaches of the representations and warranties of Holdings and Buyer contained in this Agreement and the Ancillary Agreements which would result in the failure of any of the conditions in Section 7.1 to be satisfied if Parent or Seller had actual knowledge of such breaches (or received notice thereof pursuant to Section 6.6) prior to the Closing Date or (iii) any breach of any representation or warranty contained in Section 5.10 or in clauses (iii), (iv) or (v) or Section 5.11(a).

(c) For purposes of clause (i) of Section 10.2(a), (X) a "Material Adverse Effect" (as such term is used in any representation or warranty contained in Article IV other than the representations and warranties contained in Section 4.7(a)) shall be deemed to have occurred if the aggregate of all Damages related to any such representation or warranty shall exceed $100,000 and (Y) the representations and warranties contained in Sections 4.7, 4.13 and 4.15(b) shall be read as if such representations and warranties do not include the words "Knowledge of Seller".

(d) The term "Damages" as used in this Article X is not limited to matters asserted by third parties against any Person entitled to be indemnified under this Article X, but includes Damages incurred or sustained by any such Person in the absence of third party claims.

(e) No claim for Damages under this Article X may be asserted or pursued by any former Subsidiary against Parent or Seller, unless, prior to the date that such former Subsidiary shall have ceased to be a "Subsidiary", such former Subsidiary shall have delivered a Notice to Parent or Seller relating to such claim.

10.3 Indemnification Procedures. (a) In the event that any Person shall incur or suffer any Damages in respect of which indemnification may be sought hereunder, such Person (the "Indemnitee") may assert a claim for indemnification by written notice (the "Notice") to the party from whom indemnification is being sought (the "Indemnitor"), stating the amount of Damages, if known, and the nature and basis of such claim. In the case of Damages arising or which may arise by reason of any third-party claim, promptly after receipt by an Indemnitee of written notice of the assertion or the commencement of any Action with respect to any matter in respect of which indemnification may be sought hereunder, the Indemnitee shall give Notice to the Indemnitor and shall thereafter keep the Indemnitor reasonably informed with respect thereto, provided that failure of the Indemnitee to give the Indemnitor prompt notice as provided herein shall not relieve the Indemnitor of any of its obligations hereunder, except to the extent that the Indemnitor is materially prejudiced by such failure. In case any such Action is brought against any Indemnitee, the Indemnitor shall be entitled to assume the defense thereof, by written notice of its intention to do so to the Indemnitee within 30 days after receipt of the Notice. If the Indemnitor shall assume the defense of such Action, it shall not settle such Action without the prior written consent of the Indemnitee, which consent shall not be unreasonably withheld, provided that an Indemnitee shall not be required to consent to any settlement that (i) does not include as an unconditional term thereof the giving by the claimant or the plaintiff of a release of the Indemnitee from all liability with respect to such Action or (ii) involves the imposition of equitable remedies or the imposition of any material obligations on such Indemnitee other than financial obligations for which such Indemnitee will be indemnified hereunder. As long as the Indemnitor is contesting any such Action in good faith and on a timely basis, the Indemnitee shall not pay or settle any claims brought under such Action. Notwithstanding the assumption

by the Indemnitor of the defense of any Action as provided in this Section, the Indemnitee shall be permitted to participate in the defense of such Action and to employ counsel at its own expense; provided, however, that if the defendants in any Action shall include both an Indemnitor and any Indemnitee and such Indemnitee shall have reasonably concluded that counsel selected by Indemnitor has a conflict of interest because of the availability of different or additional defenses to such Indemnitee, such Indemnitee shall have the right to select separate counsel to participate in the defense of such Action on its behalf, at the expense of the Indemnitor; provided that the Indemnitor shall not be obligated to pay the expenses of more than one separate counsel for all Indemnitees, taken together.

(b) If the Indemnitor shall fail to notify the Indemnitee of its desire to assume the defense of any such Action within the prescribed period of time, or shall notify the Indemnitee that it will not assume the defense of any such Action, then the Indemnitee may assume the defense of any such Action, in which event it may do so acting in good faith in such manner as it may deem appropriate, and the Indemnitor shall be bound by any determination made in such Action, provided, however, that the Indemnitee shall not be permitted to settle such action without the consent of the Indemnitor. No such determination or settlement shall affect the right of the Indemnitor to dispute the Indemnitee's claim for indemnification. The Indemnitor shall be permitted to join in the defense of such Action and to employ counsel at its own expense.

(c) Amounts payable by the Indemnitor to the Indemnitee in respect of any Damages for which such party is entitled to indemnification hereunder shall be payable by the Indemnitor as incurred by the Indemnitee.

(d) In the event of any dispute between the parties regarding the applicability of the indemnification provisions of this Agreement, the prevailing party shall be entitled to recover all Damages incurred by such party arising out of, resulting from or relating to such dispute.

10.4 Insurance Proceeds and Tax Limitations. The amount of any Damages or other liability for which indemnification is provided under this Agreement shall be net of any amounts recovered or recoverable by the Indemnitee under insurance policies with respect to such Damages or other liability and shall be (i) increased to take account of any Tax cost incurred (grossed up for such increase) by the Indemnitee arising from the receipt of indemnity payments hereunder (unless such indemnity payment is treated as an adjustment to the purchase price hereunder for tax purposes) and (ii) reduced to take account of any Tax benefit realized by the Indemnitee arising from the incurrence or payment of any such Damages or other liability. Such Tax cost or Tax benefit, as the case may be, shall be computed for any year using the Indemnitee's actual tax liability with and without (i) the incurrence or payment of any Damages or other liability for which indemnification is provided under this Agreement or (ii) the payment of any indemnification payments made pursuant to this Agreement in such year. In the event that the Indemnitee will actually realize a Tax cost or Tax benefit for a year(s) subsequent to the year in which the indemnity payment is made, a payment in respect of such Tax cost or Tax benefit shall be made in such subsequent year(s). Any indemnity payment made pursuant to this Agreement will be treated as an adjustment to the purchase price hereunder for Tax purposes, unless a determination (as defined in Section 1313 of the Code) with respect to the Indemnitee causes any such payment not to constitute an adjustment to the purchase price for United States Federal income tax purposes.

10.5 Tax Indemnification. Notwithstanding anything to the contrary in this Agreement, the rights and obligations of the parties with respect to indemnification for any and all Tax matters (other than with respect to any representations and warranties contained herein relating to Tax matters, except to the extent Buyer or Holdings is indemnified under the provisions of the Tax Agreement) shall be governed by the Tax Agreement and shall not be subject to this Article X, including any calculation pursuant to clause (i) of Section 10.2(a).

EXHIBIT XI

## MISCELLANEOUS

11.1 Termination. This Agreement may be terminated and the transactions contemplated hereby abandoned:

(a) by mutual consent of the parties; or

(b) by Parent and Seller, on the one hand, or Holdings and Buyer, on the other hand, on June 17, 1996 if it can be reasonably anticipated that the approvals referred to in Section 4.11(i) cannot be obtained without the applicable regulatory authorities imposing an additional material economic burden on Parent or Seller, on the one hand, or Holdings, Buyer, the Company and the Subsidiaries, taken as a whole, on the other hand; or

(c) by Parent and Seller, on the one hand, or Holdings and Buyer, on the other hand, if the conditions to such parties' obligations set forth in Articles VII and VIII, as the case may be, have not been satisfied (or waived by the party entitled to the benefit thereof) on or before August 17, 1996; provided that if the approvals referred to in Section 4.11(i) have not been obtained by August 17, 1996, this Agreement shall not be terminated prior to October 17, 1996 if it can be reasonably anticipated that such approvals can be obtained by October 17, 1996; or

(d) by Parent and Seller, on the one hand, or Holdings and Buyer, on the other hand, if the TRG Agreement is terminated in accordance with its terms.

Upon termination of this Agreement pursuant to this Section 11.1, this Agreement shall be void and of no further force and effect (except as provided in the last sentence of this paragraph) and no party shall have any liability to any other party under this Agreement unless such party has (a) willfully failed to have performed its obligations hereunder or (b) knowingly made a misrepresentation of any matter set forth herein. For purposes of the immediately preceding sentence, with respect to obligations of the Company or any Subsidiary to take or refrain from taking any action under this Agreement or obligations of Parent or Seller to cause the Company or any Subsidiary to take or refrain from taking any action under this Agreement, neither Parent nor Seller shall be deemed to have "willfully failed" unless, in each case, such action or failure to act is directed by Parent or Seller or occurs with knowledge of an officer listed on Schedule 1.1B or 1.1C; provided that if such action or failure is (X) not directed by Parent or Seller, (Y) occurs with the knowledge of an officer listed on Schedule 1.1C and (Z) occurs without the knowledge of an officer listed on Schedule 1.1B, Buyer shall recover only its Third Party Expenses and Seller and Parent shall have no further liability under this Agreement. For purposes of the second preceding sentence, neither Parent nor Seller shall be deemed to have "knowingly" made a misrepresentation unless an officer listed on Schedule 1.1B or 1.1C knows such representation is untrue when made; provided that if a representation is known to be untrue when this Agreement is executed by the parties hereto by an officer listed on Schedule 1.1C but not by an officer listed on Schedule 1.1B, Buyer shall recover only its Third Party Expenses and Seller and Parent shall have no further liability under this Agreement. Notwithstanding a termination of this Agreement, the provisions of Sections 11.2(b) and 11.11, the last sentences of Sections 4.18 and 5.4 and the confidentiality provision of the proviso to Section 6.4 hereof shall continue in full force and effect.

11.2 Confidentiality. (a) Parent and Seller shall assign to the Company at or prior to, and with effect from and after the Closing, all of their respective rights under the Confidentiality Agreement and under any other confidentiality agreements with third Persons relating to the business of the Company or any of the Subsidiaries.

(b) Except as otherwise required by law (including if required by any stock exchange on which any of the securities of any party or their respective Affiliates are listed or by any securities commission or similar regulatory authority having jurisdiction over any such party or any of its Affiliates), Buyer, Holdings, Seller and Parent shall keep confidential all aspects of the

transactions contemplated hereby, including the fact that this Agreement has been executed. Notwithstanding the foregoing or the terms of the Confidentiality Agreement, Buyer, Holdings and their respective Affiliates and Seller, Parent and their respective Affiliates may disclose information concerning the transactions contemplated hereby in connection with the financing of such transactions by Holdings and Buyer, to potential equity investors in Holdings or any of its Affiliates, as necessary to obtain any consents referenced in Section 8.2 and, in the case of Parent, as it, in its sole discretion, deems appropriate in light of its status as a Person with public stockholders. The parties will use their reasonable efforts to make the release to be issued announcing the Closing a mutually acceptable joint release. Before issuing any other press release with respect to the transactions contemplated by this Agreement, the parties will use reasonable efforts to provide each other with a reasonable opportunity to review and comment on any such announcement.

11.3 Parent Option. (a) Parent and/or Seller shall have the right to purchase up to an aggregate of 19.9% of the Holdings Common Stock immediately prior to the Closing for a per share purchase price equal to the per share purchase price paid or payable by other stockholders of Holdings on or prior to the Closing Date, provided that if investment partnerships affiliated with KKR shall have invested, as of the Closing Date, in a corporation which wholly-owns Holdings (rather than investing directly in Holdings), references to "Holdings Common Stock" in this Section 11.3, Sections 5.3, 5.7(b) and 9.3 and clause (b) of the definition of "Securities" contained in Section 1.1 shall be deemed to be references to the common stock of such corporation and references to "Holdings" and "New Talegen Holdings Corporation" in Section 9.3 shall be deemed to be references to such corporation. Parent and/or Seller shall pay the aggregate purchase price for any shares to be purchased pursuant to this Section in cash, payable by wire transfer in immediately available funds to an account which Buyer shall designate in writing to Parent no less than two business days prior to the Closing Date. To exercise such right, Parent and/or Seller must deliver irrevocable written notice to Buyer within 45 days from the date hereof which indicates the percentage interest (after giving effect to its purchase) of Holdings Common Stock that Parent and/or Seller desire to purchase hereunder, but not to exceed an aggregate of 19.9% (which irrevocable notice shall bind Parent, subject to the last sentence of this Section, to make such purchase on the Closing Date). No such notice shall be effective unless Parent and/or Seller concurrently delivers a notice under Section 11.3 of the TRG Agreement which indicates Parent's and/or Seller's election to purchase the same aggregate percentage interest in the securities covered by the election thereunder that Parent and/or Seller elect to purchase hereunder. Notwithstanding the foregoing, if this Agreement is terminated pursuant to Section 11.1, Parent and Seller shall cease to have the right to purchase Holdings Common Stock hereunder, whether or not their rights had been previously exercised, and any notice which shall have been delivered pursuant to this Section shall be void and of no effect.

(b) Any Holdings Common Stock purchased by Parent and/or Seller pursuant to paragraph (a) above shall be subject to the terms and conditions set forth in Exhibit M.

11.4 Assignment. Neither this Agreement nor any of the rights or obligations hereunder may be assigned by Parent or Seller without the prior written consent of Holdings or Buyer, or by Holdings or Buyer without the prior written consent of Parent or Seller. Subject to the foregoing, this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns, and no other Person shall have any right, benefit or obligation hereunder.

11.5 Notices. Unless otherwise provided herein, any notice, request, instruction or other document to be given hereunder by any party to the others shall be in writing and delivered in Person or by courier or facsimile transmission or mailed by certified mail, postage prepaid, return receipt requested (such mailed notice to be effective on the date such receipt is acknowledged), as follows:

If to Parent or Seller:

Xerox Financial Services, Inc.
100 First Stamford Place
Stamford, Connecticut 06904-2347
Attn: Stuart B. Ross
Chairman & Chief Executive
Officer
Fax: (203) 325-6822

and

Xerox Corporation
800 Long Ridge Road
Stamford, Connecticut 06904
Attn: Richard Paul, Esq.
General Counsel
Fax: (203) 968-3446

With a copy to:

Skadden, Arps, Slate, Meagher & Flom
919 Third Avenue
New York, New York 10022
Attn: Lou R. Kling, Esq. and
Peter Allan Atkins, Esq.
Fax: (212) 735-2000

If to Holdings or Buyer:

New Talegen Holdings Corporation
c/o Kohlberg Kravis Roberts & Co.
2800 Sand Hill Road, Suite 200
Menlo Park, California 94025
Attn: Saul A. Fox
Fax: (415) 233-6594

With copies to:

Joseph W. Brown
Talegen Holdings, Inc.
Waterfront Center One
1011 Western Avenue, Suite 1000
Seattle, Washington 98101
Fax: (206) 654-2633

Gary I. Horowitz, Esq.
Simpson Thacher & Bartlett
425 Lexington Avenue
New York, New York 10017
Fax: (212) 455-2502

or to such other place and with such other copies as either party may designate as to itself by written notice to the others.

11.6 Choice of Law. This Agreement shall be construed, interpreted and the rights of the parties determined in accordance with the internal laws of the State of New York, without regard to the conflict of law principles thereof.

11.7 Entire Agreement; Amendments and Waivers. This Agreement, together with the Ancillary Agreements and the Confidentiality Agreement (except to the extent superseded hereby), constitutes the entire agreement among the parties pertaining to the subject matter hereof and supersedes all prior agreements, understandings, negotiations and discussions, whether oral or written, of the parties. No supplement, modification or waiver of this Agreement (including, without limitation, any Schedule hereto) shall be binding unless executed in writing by all parties. No waiver of any of the provisions of this Agreement shall be deemed or shall constitute a waiver of any other provision hereof (whether or not similar), nor shall such waiver constitute a continuing waiver

unless otherwise expressly provided. With respect to breaches of any representation, warranty or covenant contained herein, unless this Agreement shall have been terminated pursuant to Section 11.1, the sole remedy of the parties against each other shall be the indemnification rights set forth in Section 10.2.

11.8 Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

11.9 Invalidity. In the event that any one or more of the provisions contained in this Agreement or in any other instrument referred to herein, shall, for any reason, be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision of this Agreement or any other such instrument.

11.10 Headings. The headings of the Articles and Sections herein are inserted for convenience of reference only and are not intended to be a part of or to affect the meaning or interpretation of this Agreement.

11.11 Expenses. Subject to Section 11.1, Seller and Buyer will each be liable for its own costs and expenses incurred in connection with the negotiation, preparation, execution or performance of this Agreement.

11.12 [Intentionally Omitted].

11.13 Joint and Several. (a) All covenants, representations and warranties made by Parent or Seller in this Agreement shall be deemed to be joint and several covenants, representations and warranties of Parent and Seller.

(b) All covenants, representations and warranties made by Holdings or Buyer in this Agreement shall be deemed to be joint and several covenants, representations and warranties of Holdings and Buyer.

11.14 No Third Party Beneficiaries. This Agreement shall inure exclusively to the benefit of and be binding upon the parties hereto and their respective successors, assigns, executors and legal representatives. Except as expressly provided in Section 10.2, nothing in this Agreement, express or implied, is intended to confer on any Person other than the parties hereto or their respective successors and assigns, any rights, remedies, obligations or liabilities under or by reason of this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement, or have caused this Agreement to be duly executed on their respective behalf by their respective officers thereunto duly authorized, as of the day and year first above written.

XEROX CORPORATION

/s/ Stuart B. Ross
Name: Stuart B. Ross
Title: Executive Vice President

XEROX FINANCIAL SERVICES, INC.

/s/ Stuart B. Ross
Name: Stuart B. Ross
Title: Chairman, President and Chief Executive Officer

NEW TALEGEN HOLDINGS CORPORATION

/s/ Saul A. Fox
Name: Saul A. Fox

Title: President and Chief Executive Officer

TALEGEN ACQUISITION CORPORATION

/s/ Saul A. Fox
Name: Saul A. Fox
Title: President and Chief Executive Officer

Exhibit 10(p)

# STOCK PURCHASE AGREEMENT

dated as of January 17, 1996

among

XEROX CORPORATION

XEROX FINANCIAL SERVICES, INC.

and

TRG ACQUISITION CORPORATION

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# STOCK PURCHASE AGREEMENT

STOCK PURCHASE AGREEMENT dated as of January 17, 1996 among Xerox Corporation, a New York corporation ("Parent"), Xerox Financial Services, Inc., a Delaware corporation and a wholly-owned subsidiary of Parent ("Seller"), and TRG Acquisition Corporation, a Delaware corporation ("Buyer").

## RECITALS

Seller is the beneficial and record owner of 1,000 shares of common stock, par value $1.00 per share, of The Resolution Group, Inc., a Delaware corporation (the "Company"), constituting all of the issued and outstanding capital stock (the "Stock") of the Company.

Buyer desires to purchase from Seller, and Seller desires to sell to Buyer, all of the Stock subject to the terms and conditions of this Agreement.

Parent is the sole stockholder of Seller and desires that Seller sell to Buyer all of the Stock, subject to the terms and conditions of this Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements contained herein and for other good and valuable consideration the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

## ARTICLE I

## DEFINITIONS

1.1 Defined Terms. As used herein, the terms below shall have the following meanings:

"Affiliate" shall mean a Person that directly or indirectly through one or more intermediaries controls, is controlled by or is under common control with the Person specified. For purposes of this definition and the definition of "Subsidiary" set forth below, the term "control" (including the terms "controlling," "controlled by" and "under common control with") of a Person means the possession, direct or indirect, of the power to (i) vote 50% or more of the voting securities of such Person or (ii) direct or cause the direction of the management and policies of such Person, whether by contract or otherwise.

"Agreement" shall mean this Stock Purchase Agreement (together with all schedules and exhibits referenced herein), as amended, modified or supplemented from time to time.

"Ancillary Agreements" shall mean, collectively, the Guarantees and the Tax Agreement.

"Balance Sheet Date" shall mean June 30, 1995.

"Cash Equivalents" shall mean (a) securities with maturities of one year or less from the date of acquisition issued or fully guaranteed or insured by the United States Government or any agency thereof, (b) certificates of deposit and eurodollar time deposits with maturities of one year or less from the date of acquisition and overnight bank deposits of any commercial bank having capital and surplus in excess of $500,000,000, (c) repurchase obligations of any commercial bank satisfying the requirements of clause (b) of this definition, having a term of not more than 30 days with respect to securities issued or fully guaranteed or insured by the United States government, (d) commercial paper of a domestic issuer rated at least A-2 by S&P or P-2 by Moody's, (e) securities with maturities of one year or less from the date of acquisition issued or fully guaranteed by any state, commonwealth or territory of the United States, by any political subdivision or taxing authority of any such state, commonwealth or territory or by any foreign government, the securities of which state, commonwealth, territory, political subdivision,

taxing authority or foreign government (as the case may be) are rated at least A by S&P or A by Moody's, (f) securities with maturities of one year or less from the date of acquisition backed by standby letters of credit issued by any commercial bank satisfying the requirements of clause (b) of this definition or (g) shares of money market mutual or similar funds which invest exclusively in assets satisfying the requirements of clauses (a) through (f) of this definition.

"Class 1 Stock" shall mean the Class 1 Stock having the terms set forth in the Restated Certificate of Incorporation.

"Class 2 Stock" shall mean the Class 2 Stock having the terms set forth in the Restated Certificate of Incorporation.

"Closing Date" shall mean the date on which the Closing occurs.

"Code" shall have the meaning ascribed in the Tax Agreement.

"Company GAAP Financial Statements" shall mean the audited Consolidated Balance Sheets of the Company (or its predecessors) as of December 31, 1994 and 1993 and the Consolidated Statements of Operations, Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of the Company (or its predecessors) for each of the three fiscal years included in the three-year period ended December 31, 1994, prepared in accordance with GAAP, together with the notes thereon and the related reports of KPMG Peat Marwick LLP.

"Company Interim Financial Statements" shall mean the unaudited Consolidated Balance Sheets and the unaudited Consolidated Statements of Operations, Consolidated Statements of Shareholder's Equity and Consolidated Statements of Cash Flows of the Company for the nine-month periods ended September 30, 1994 and 1995, together with the notes thereon.

"Contracts" shall mean all agreements, contracts, commitments and undertakings (other than contracts of insurance or reinsurance or retrocession agreements) to which the Company or any of the Subsidiaries is a party, an obligor or a beneficiary and (i) the performance or non-performance of which is individually or, with respect to any related series of agreements, in the aggregate, material to the Company and the Subsidiaries, taken as a whole, or (ii) which provide for an aggregate purchase price or payments of more than $1,000,000 under any agreement during any two-year period (or $1,000,000 in the aggregate, during any two-year period, in the case of any related series of agreements).

"Convention Statements" shall mean (i) the annual convention statements and the quarterly statement of each Insurance Subsidiary as filed with the insurance regulatory authorities in its jurisdiction of domicile for the years ended December 31, 1992, 1993 and 1994 and for the quarterly period ended September 30, 1995, and (ii) the annual convention statements of Ridge Re as filed with the insurance regulatory authorities in Bermuda for the period from December 14, 1992 to December 31, 1993 and for the year ended December 31, 1994.

"Crostex/Camfex Contracts" shall mean all contracts, agreements or arrangements of the Company or any Subsidiary relating to the real property and improvements located at (i) 255 California Street, San Francisco, California, (ii) 5724 W. Los Positos Blvd., Pleasonton, California, (iii) 299 Madison Avenue, Morris Township, New Jersey, (iv) 305 Madison Avenue, Morris Township, New Jersey and (v) 4040 North Central Expressway, Dallas, Texas, including, without limitation, any notes held by the Company or any Subsidiary (the "Crostex/Camfex Purchase Money Notes").

"Encumbrances" shall mean any claim, lien (statutory or other), pledge, option, charge, easement, security interest, right-of-way, encroachment, encumbrance, mortgage, or other rights of third parties.

"Environmental Laws" shall mean any and all applicable Federal, state or local laws or regulations relating to the protection of the environment or of human

health as it may be affected by the environment.

"Environmental Permit" shall mean any license, permit, order, consent, approval, registration, authorization, qualification or filing required under any Environmental Law.
"Environmental Report" shall mean any report, study, assessment, audit, or other similar document that addresses any issue of actual or potential noncompliance with, or actual or potential liability under, any Environmental Law that may in any way affect the Company or any Subsidiary other than to the extent such document addresses any issue of actual or potential noncompliance with, or actual or potential liability under, any Environmental Law by reason of any policy of insurance, reinsurance, indemnity, guaranty or assumption of liability of any party entered into by the Company or any Insurance Subsidiary.

"Excluded Activities" shall mean, with respect to the Company and the Subsidiaries, activities relating to insurance reserves, claims under, related to or in respect of insurance policies or any disputes related thereto, loss adjustments and loss adjustment expenses and reinsurance receivables, provided, however, that "Excluded Activities" shall not be deemed to include any (i) of the matters covered by the representations contained in Section 4.6, 4.9(c), 4.12 (to the extent it applies to Ridge Re) or 4.26 or other representations regarding Ridge Re or the Ridge Re Treaty or (ii) actions, suits, proceedings or claims pending by any governmental or regulatory authority to the extent based upon a violation of any law, statute, ordinance, rule or regulation.

"GAAP" shall mean generally accepted accounting principles in the United States of America in effect from time to time.

"Guarantees" shall mean the guarantees referred to in Section 8.15.

"HSR Act" shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

shall mean International Insurance Company, an Illinois corporation.

"Information Returns" shall have the meaning ascribed in the Tax Agreement.

"Insurance Subsidiaries" shall mean the Subsidiaries listed on Schedule 1.1A.

"Investment Policy" shall mean, with respect to certain Subsidiaries, the policy for each such Subsidiary set forth on Exhibit A.

"KKR" shall mean Kohlberg Kravis Roberts & Co.

"Knowledge of Seller" shall mean (i) with respect to matters relating to Parent or Seller, actual knowledge of any officer of Parent, Seller or Ridge Re set forth in Schedule 1.1B, and (ii) with respect to any matters relating to the Company or any Subsidiary, actual knowledge of any such officer of Parent or Seller, or the actual knowledge of the persons set forth in Schedule 1.1C.

"Material Adverse Effect" with respect to any Person shall mean a material adverse effect on the business, financial condition, assets or operations of such Person, but shall exclude any effect resulting from general economic conditions.

"Materials of Environmental Concern" shall mean any waste, pollutant, or contaminant or substance (including, without limitation, petroleum or petroleum products, asbestos or asbestos-containing materials, urea-formaldehyde insulation, polychlorinated biphenyls, odors, radioactivity, and electro-magnetic fields) regulated by or under, or which may otherwise give rise to liability under, any Environmental Law.

"Moody's" shall mean Moody's Investors Service, Inc.

Restructuring" shall mean the restructuring of Talegen and its subsidiaries

(including, without limitation, the Company and IIC) pursuant to the Restructuring Agreement dated as of September 3, 1993 among Seller, Ridge Re, Talegen and certain of its subsidiaries.

"Permits" shall mean all licenses, permits, orders, consents, approvals, registrations, authorizations, qualifications and filings with and under all Federal, state, local or foreign laws and governmental or regulatory bodies and all industry or other non-governmental self-regulatory organizations (including, without limitation, Environmental Permits).

"Person" shall mean an individual, a partnership, a joint venture, a corporation, a business trust, a limited liability company, a trust, an unincorporated organization, a government or any department or agency thereof or any other entity.

"Qualified Transferee" shall mean a corporation (or the wholly-owned direct or indirect subsidiary thereof) which, as of the date of the consummation of a sale pursuant to Section 9.6, is an insurance company engaged in the business of reinsurance and has at least $2 billion in assets and a rating of "A+" or better by A.M. Best & Co.

"Restated Certificate of Incorporation" shall mean the restated certificate of incorporation of Buyer in the form of Exhibit B, with such additional ministerial changes as do not adversely affect the holders of Class 2 Stock.

"Ridge Re" shall mean Ridge Reinsurance Limited, a Bermuda corporation and a wholly-owned subsidiary of Seller.

"Ridge Re GAAP Financial Statements" shall mean the audited Consolidated Balance Sheets of Ridge Re as of December 31, 1994 and 1993 and the related Statements of Operations and Retained Earnings and Cash Flows for the year ended December 31, 1994 and the period from December 14, 1992 to December 31, 1993, prepared in accordance with GAAP, together with the notes thereon and the related reports of KPMG Peat Marwick LLP.

"Ridge Re Interim Financial Statements" shall mean the unaudited Consolidated Balance Sheet of Ridge Re as of September 30, 1995, and the related Statements of Operations and Retained Earnings for the nine-month periods ended September 30, 1994 and September 30, 1995.

"Ridge Re Treaty" shall mean the agreement, as amended by Endorsement No. 1 thereto, contained in Schedule 1.1D.

shall mean Standard and Poor's Rating Group.

"Securities" shall mean (a) the Class 2 Stock and (b) any shares of Class 1 Stock purchased by Seller in accordance with Section 11.3.

"Statutory Accounting Principles" shall mean, as applied to any Subsidiary, the statutory accounting practices prescribed or permitted by the jurisdiction of domicile of such Subsidiary.

"Subsidiaries" shall mean all corporations, partnerships, joint ventures or other entities which the Company controls, directly or indirectly through one or more intermediaries. See definition of "Affiliate" in this Section 1.1 for the meaning of "control."

"Talegen" shall mean Talegen Holdings, Inc., a Delaware corporation.

"Talegen Acquisition" shall mean Talegen Acquisition Corporation, a Delaware corporation.

"Talegen Agreement" shall mean the Stock Purchase Agreement dated as of the date hereof among Parent, Seller, New Talegen Holdings Corporation, a Delaware corporation, and Talegen Acquisition as amended, modified or supplemented from time to time, which contemplates that Talegen Acquisition will purchase all of the outstanding capital stock of Talegen from Seller, subject to the terms and conditions thereof.

"Tax Agreement" shall mean the Tax Allocation and Indemnification Agreement dated as of the date hereof among Parent, Seller, the Company and Buyer.

"Tax Returns" shall have the meaning ascribed in the Tax Agreement.

"Taxes" shall have the meaning ascribed in the Tax Agreement.

"Third Party Amount" shall mean any amount paid by the transferee (which may be Seller or any of its Affiliates (other than the Company or any Subsidiary)) to the Company or the Subsidiaries of all or a portion of the Seller Notes or Leesburg Training Facility, as the case may be, pursuant to Sections 6.12 or 6.13.

"Third Party Expenses" shall mean all expenses paid or payable by Buyer to other Persons in connection with the transactions contemplated by this Agreement, the Ancillary Agreements and the Financing Documents other than expenses contingent upon a payment to Buyer or which are not payable unless there has been a breach of this Agreement by Parent, Seller, the Company or any Subsidiary, but shall in no event include any amount payable to KKR or its Affiliates (other than to Am-Re Consultants, Inc. in connection with reserve analyses) or any officer, director or employee of the Company or the Subsidiaries.

"Transaction Expenses" shall mean (i) a $5 million transaction fee payable by Buyer to an Affiliate of KKR, (ii) all fees and expenses of third party advisors to Buyer and of Buyer's financing sources in connection with the transactions contemplated by this Agreement, the Ancillary Agreements and the Financing Documents and (iii) all fees and expenses incurred by Buyer in connection with satisfying the conditions precedent in Article VIII, certified in good faith by Buyer to Seller.

1.2 Other Defined Terms. The following terms shall have the meanings defined for such terms in the Sections set forth below:

| Term | Section |
|---|---|
| "Actions" | 4.13 |
| "Assets" | 4.18 |
| "Closing" | 3.1 |
| "Company Plans" | 4.21 |
| "Confidentiality Agreement" | 6.4 |
| "Crostex/Camfex Purchase Money Notes" | 1.1 |
| "Damages" | 10.2 |
| "ERISA" | 4.21 |
| "ESOP" | 9.4 |
| "Exchange Act" | 4.11 |
| "Financing" | 5.3 |
| "Financing Documents" | 5.3 |
| "Indemnitor" | 10.3 |
| "Intellectual Property" | 4.20 |
| "Leesburg Training Facility Amount" | 6.13 |
| "Leesburg Training Facility" | 6.13 |
| "Liabilities" | 4.14 |
| "Long Term Incentive Program" | 9.4 |
| "Notice" | 10.3 |
| "Personnel" | 4.13 |
| "Section 4.5 Subsidiaries" | 4.5 |
| "Securities Act" | 4.3 |
| "Seller Notes" | 4.23 |
| "TRG Incentive Plans" | 9.4 |

1.3 Other Definitional Provisions. (a) The words "hereof", "herein" and "hereunder" and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement, and Section, Schedule and Exhibit references are to this Agreement unless otherwise specified.

(b) The meanings given to terms defined herein shall be equally applicable to both the singular and plural forms of such terms.

## ARTICLE II

## PURCHASE AND SALE OF STOCK AND CLASS 2 STOCK

2.1 Transfer of Stock. Upon the terms and subject to the conditions contained herein, Seller will sell, convey, transfer, assign and deliver to Buyer, and Buyer will acquire from Seller on the Closing Date, all of the Stock for the consideration set forth in Section 2.2.

2.2 Consideration for Stock. Upon the terms and subject to the conditions contained herein, as consideration for the purchase of the Stock, on the Closing Date Buyer will (i) pay to Seller cash in an amount equal to $150,000,000, payable by wire transfer in immediately available funds to an account which Seller will designate in writing to Buyer no less than two business days prior to the Closing Date, subject to adjustment as described in Section 2.3, and (ii) issue and deliver to Seller Class 2 Stock with an aggregate liquidation value of $462,000,000.

2.3 Adjustments. The amount of cash payable by Buyer pursuant to Section 2.2 will be reduced by an amount equal to the Transaction Expenses.

## ARTICLE III

## CLOSING

3.1 Closing. The closing of the transactions contemplated herein (the "Closing") shall take place as soon as practicable but in no event later than five business days after satisfaction or waiver of the conditions set forth in Articles VII and VIII, and shall be held at 9:00 a.m. local time on the Closing Date at the offices of Simpson Thacher & Bartlett, 425 Lexington Avenue, New York, New York 10017, unless the parties hereto otherwise agree. The parties agree that the effective time of the Closing for Federal income tax purposes shall be at the close of business on the Closing Date.

3.2 Documents to be Delivered. To effect the transfer referred to in Section 2.1 and the delivery of the consideration described in Section 2.2 hereof, Seller and Buyer shall, on the Closing Date, deliver the following:

(a) Seller shall deliver to Buyer certificate(s) evidencing the Stock, free and clear of any Encumbrances of any nature whatsoever (except Encumbrances arising as a result of any action taken by Buyer or any of its Affiliates), duly endorsed in blank for transfer or accompanied by stock powers duly executed in blank.

(b) Buyer shall deliver to Seller immediately available funds as provided in Section 2.2.

(c) Buyer shall deliver to Seller certificate(s) evidencing Class 2 Stock as provided in Section 2.2, free and clear of any Encumbrances of any nature whatsoever (except Encumbrances arising as a result of any action taken by Seller or any of its Affiliates) in the form of one or more certificates in the name of Seller or its designee as Seller may require.

(d) Seller and Buyer shall each deliver all documents required to be delivered pursuant to Articles VII and VIII.

(e) All instruments and documents executed and delivered to Buyer pursuant hereto shall be in form and substance, and shall be executed in a manner, reasonably satisfactory to Buyer. All instruments and documents executed and delivered to Seller pursuant hereto shall be in form and substance, and shall be executed in a manner, reasonably satisfactory to Seller.

## ARTICLE IV

## REPRESENTATIONS AND WARRANTIES OF PARENT AND SELLER

Parent and Seller hereby represent and warrant to Buyer as follows:

4.1 Organization of Seller and Parent. Seller is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business as it is presently being conducted and to own the Stock. Parent is duly organized, validly existing and in good standing under the laws of the State of New York and has full corporate power and authority to conduct its business as it is presently being conducted.

4.2 Organization of the Company. The Company is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business as it is presently being conducted and to own, lease and operate its properties and assets. The Company is duly qualified or otherwise authorized as a foreign corporation to conduct the business conducted by it and is in good standing in each jurisdiction in which such qualification or authorization is necessary under the applicable law and where the failure to be so qualified or otherwise authorized, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Seller has provided to Buyer a complete and correct copy of the certificate of incorporation, bylaws and other organizational documents of the Company and the minute books of the Company. The Company's minute books include copies of minutes of all meetings of the directors or shareholders of the Company held on or after January 1, 1993 and complete and accurate copies of all resolutions passed by the directors or actions by written consent of the shareholders on or after January 1, 1993.

4.3 Capital Stock. The Company has authorized 1,000 shares of common stock, $1.00 par value, 1,000 shares of which are issued and outstanding, and no shares of any other class or series of capital stock are authorized, issued or outstanding. All of the shares of the Stock have been duly and validly authorized and issued, and are fully paid and nonassessable. Seller owns of record and beneficially all of the Stock free and clear of all Encumbrances, including without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to the Stock; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such Stock without registration or qualification under, or in compliance with, applicable Federal or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act of 1933, as amended (the "Securities Act")) or without compliance with applicable insurance laws. There are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding for the purchase of, nor any securities convertible or exchangeable for, any equity interests of the Company. There are no restrictions upon the voting or transfer of any shares of the Stock pursuant to the Company's Certificate of Incorporation or Bylaws or any agreement or other instrument to which the Company, Talegen or Seller is a party or by which the Company, Talegen or Seller is bound. Upon consummation of the transactions contemplated by this Agreement, Buyer will acquire from Seller good and marketable title to such Stock, free and clear of all Encumbrances, except Encumbrances arising as a result of any action taken by Buyer or any of its Affiliates; provided that Parent and Seller make no representation regarding the ability of any Person other than Seller to transfer or otherwise dispose of such Stock without registration or qualification under, or in compliance with, applicable Federal securities or state securities or insurance laws.

4.4 Authorization. Each of Parent and Seller has all necessary corporate power and authority to enter into this Agreement and the Ancillary Agreements to which it is or will be a party, and has taken all corporate action necessary to consummate the transactions contemplated hereby and thereby and to perform its obligations hereunder and thereunder. This Agreement and the Tax Agreement have each been duly executed and delivered by each of Seller and

Parent. Assuming the due execution of this Agreement and the Tax Agreement by Buyer, each of this Agreement and the Tax Agreement is a legal, valid and binding obligation of each of Seller and Parent enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing. Subject to the occurrence of the Closing, the Guarantees will be duly executed and delivered by Parent and Seller, as applicable, on the Closing Date. Upon execution and delivery by Parent or Seller, as the case may be, each Guarantee will be a legal, valid and binding obligation of such Person enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

4.5 Subsidiaries. Schedule 4.5 sets forth a complete and accurate list of all of the Subsidiaries, other than Subsidiaries which are not Insurance Subsidiaries and which do not hold any assets (including capital stock) with a fair market value in excess of $1,000 or insurance licenses (the "Section 4.5 Subsidiaries"). Schedule 4.5 also contains the jurisdiction of incorporation or formation of each of the Section 4.5 Subsidiaries, each jurisdiction in which such Subsidiary is licensed, qualified or otherwise authorized to conduct insurance business, the number of shares of capital stock of any Section 4.5 Subsidiary which is a corporation issued and outstanding and the percentage ownership interest of the Company in each such Subsidiary. All outstanding shares of capital stock of such Subsidiaries have been duly and validly authorized and are fully paid and nonassessable. All such outstanding shares are owned by the Company and/or one or more of its Subsidiaries free and clear of any Encumbrances, including, without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to such shares; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such shares without registration or qualification under, or in compliance with, applicable Federal securities or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 under the Securities Act) or without compliance with applicable insurance laws. There are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding for the purchase of, nor any securities convertible or exchangeable for, any equity interests of any of the Section 4.5 Subsidiaries. Schedule 4.5 contains true and complete copies of all agreements and other instruments pursuant to which the Company or any Section 4.5 Subsidiary is obligated or required, under any circumstance, to make contributions to the capital of any Subsidiary. Each of the Insurance Subsidiaries is a corporation duly licensed, organized, validly existing and in good standing under the jurisdiction of its organization and each of the other Subsidiaries is a corporation duly organized, validly existing and in good standing under the jurisdiction of its organization, in each case, with corporate power to own its properties and conduct its business as now being conducted and is duly licensed (in the case of the Insurance Subsidiaries), qualified and in good standing to transact business in each jurisdiction (as listed in Schedule 4.5) where, by virtue of its business carried on or properties owned, it is required to be so licensed (in the case of the Insurance Subsidiaries) or qualified and where the failure to be so licensed (in the case of the Insurance Subsidiaries) or qualified, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. To the extent requested of Seller by Buyer, Seller has made available to Buyer a complete and correct copy of the certificates of incorporation, bylaws and other organizational documents of each Section 4.5 Subsidiary and the minute books of each such Subsidiary. The minute books include copies of minutes of all meetings of the directors or shareholders of each such Subsidiary held on or after January 1, 1993 and complete and accurate copies of all resolutions passed by the directors or actions by written consent of the shareholders on or after January 1, 1993.

4.6 Ridge Re. (a) Ridge Re is duly organized, validly existing and in good

standing under the laws of Bermuda and has full corporate power and authority to conduct its business as it is presently being conducted and to own, lease and operate its properties and assets. Ridge Re is duly licensed, qualified or otherwise authorized as an alien corporation to conduct the reinsurance business conducted by it and is in good standing in each jurisdiction in which such license, qualification or authorization is necessary under the applicable law and where the failure to be so licensed, qualified or otherwise authorized, individually or in the aggregate, would have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(b) Seller owns of record and beneficially all of the outstanding capital stock of Ridge Re free and clear of all Encumbrances, including without limitation, any agreement, understanding or restriction affecting the voting rights or other incidents of record or beneficial ownership pertaining to such shares; provided that Parent and Seller make no representation in this sentence regarding the ability of Seller to transfer or otherwise dispose of such shares without registration or qualification under, or in compliance with, applicable Federal or state securities laws to a Person who is not an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act) or without compliance with applicable insurance laws. There are no subscriptions, options, warrants, calls, commitments, preemptive rights or other rights of any kind outstanding to which Parent, Seller, Ridge Re or any of their respective Affiliates is a party for the purchase of, nor any securities convertible or exchangeable for, any equity interests of Ridge Re, except as set forth in Schedule 4.6. Schedule 4.6 contains a true and complete list of all agreements and other instruments pursuant to which Parent, Seller or any Affiliate is obligated or required, under any circumstance, to make contributions to the capital of Ridge Re.

(c) The Ridge Re Treaty is a legal, valid and binding obligation of Ridge Re, enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

4.7 Absence of Certain Changes or Events. To the Knowledge of Seller, except as expressly contemplated by this Agreement or as described on Schedule 4.7 or reflected in the Company Interim Financial Statements, since June 30, 1995, there has not been any:

(a) change in the business, condition (financial or otherwise), Permits, assets, Liabilities, working capital, earnings or operations of the Company or any Subsidiary, except for changes which have not, individually or in the aggregate, had or are not reasonably likely to have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole;

(b) acquisition of material assets or properties or of securities or business of any other Person by the Company or any Subsidiary (in each case, other than acquisitions in the ordinary course of business consistent with past practice) or any merger, consolidation or amalgamation involving the Company or any Subsidiary, except the acquisition of Cash Equivalents as part of the process of converting substantially all of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents prior to the date of this Agreement and the reinvestment thereof in accordance with the Investment Policy after the date of this Agreement;

(c) sale, assignment, lease or transfer of (i) the Crostex/Camfex Contracts, the Seller Notes (except transfers in accordance with, and to the extent Parent and Seller comply with, Section 6.12) or any interest in the Leesburg Training Facility (except transfers in accordance with, and to the extent Parent and Seller comply with, Section 6.13) or (ii) any other material assets (including any portion of the investment portfolio) of the Company or any Subsidiary, other than in the case of (ii) (W) in the ordinary course of business consistent with past practices and (X) converting substantially all of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents prior to the date of this Agreement and dispositions of securities in accordance with the Investment Policy after the date of this Agreement;

(d) incurrence by the Company or any Subsidiary of any indebtedness for borrowed money or incurrence, assumption or guarantee of, or any other act to become responsible for, any obligations of any other Person, or making of loans or advances by the Company or any Subsidiary to any Person (including, without limitation, any broker or agent), except (i) loans to employees made in the ordinary course of business consistent with past practice for relocation expenses and (ii) the issuance of insurance policies in the ordinary course of business consistent with past practice;

(e) cancellation of any indebtedness or waiver or compromise of any rights (including agent balances) having a value to the Company or any Subsidiary of $500,000 or more, including the Seller Notes and the Crostex/Camfex Purchase Money Notes, whether or not in the ordinary course of business (other than settlements in the ordinary course of business of claims and salvage and subrogation arising under contracts of insurance underwritten, assumed or ceded by the Company or any Subsidiary which settlements have not had nor would be reasonably likely to have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole and the terminations, modifications and commutations permitted by clause (j) below);

(f) failure of the Company or any Subsidiary to pay any creditor any amount owed to such creditor (in excess of $1,000,000 in the aggregate for all such creditors) when due (after the expiration of any applicable grace periods) except for failures to pay in the ordinary course of business or if the Company or any Subsidiary is disputing the amount due in good faith;

(g) payment by the Company or any Subsidiary of any material Liability before the same became due in accordance with its terms other than in the ordinary course of business consistent with past practice;

(h) material change in the reinsurance, claim processing and payment, financial or accounting practices or policies of the Company or any Subsidiary, except as required by law, generally accepted accounting principles or Statutory Accounting Principles;

(i) except to the extent required under employee and director benefit plans or policies, agreements or arrangements as in effect on the Balance Sheet Date, (1) increase in the compensation or fringe benefits of any of the directors, officers or employees of the Company or any Subsidiary (except for increases in salary or wages of employees of the Company or any Subsidiary who are not officers of the Company in the ordinary course of business in accordance with past practice), (2) grant of any severance or termination pay or entrance into any employment, consulting or severance agreement or arrangement with any present or former director, officer or employee of the Company or any Subsidiary or amendment of any such arrangement or agreement or (3) establishment, adoption, entrance into, amendment of or termination of any (X) collective bargaining agreement or (Y) plan or agreement to provide bonuses, profit sharing, stock options, restricted stock, pensions, retirement benefits, deferred compensation, employment or benefits upon termination for the benefit of any directors, officers or any group of other employees of the Company or any Subsidiary;

(j) (i) entry into or modification of any reinsurance or retrocession agreement by the Company or any Subsidiary other than in the ordinary course of business consistent with past practice, except for those which have not had nor are reasonably likely to have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole or (ii) termination or commutation of any reinsurance or retrocession agreement legally carried on the books of the Subsidiaries at the time of such termination or commutation at $5,000,000 or more;

(k) entry into, termination or modification by the Company or any Subsidiary of any Contract, agreement, commitment, transaction, or instrument (including, without limitation, relating to any borrowing, lending, capital expenditure, capital contribution or capital financing), except entering into, terminating or modifying contracts, agreements, commitments, transactions, or instruments

(i) in the ordinary course of business and (ii) as permitted by clauses (i) and (j) above; provided that except as disclosed on Schedule 4.7, no modifications shall have been made to the Crostex/Camfex Contracts or the Ridge Re Treaty;

(l) entry into a material joint venture, partnership or similar arrangement by the Company or any Subsidiary with any Person;

(m) any capital expenditure or execution of any lease or commitment for the foregoing by the Company or any Subsidiary involving annual payments in excess of $100,000;

(n) lapse or termination or failure to renew any Permit of the Company or any Subsidiary, in each case other than with respect to Permits the failure of which to be in effect would not have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole;

(o) (i) declaration, setting aside or payment of any dividends or distributions (whether in cash, stock or property) in respect of any capital stock of the Company or (ii) any redemption, purchase or other acquisition of any of the capital stock of the Company or any Subsidiary (other than a wholly owned Subsidiary), except for payments permitted under the Tax Agreement;

(p) issuance by the Company or any Subsidiary of, or commitment of the Company or any Subsidiary to issue, any shares of capital stock or obligations or securities convertible into or exchangeable for shares of capital stock except for issuances or commitments by any Subsidiary to issue any such securities to the Company or any wholly owned Subsidiary;

(q) amendment of the certificate of incorporation or bylaws of the Company or any Subsidiary; or

(r) agreement by the Company or any Subsidiary to do any of the foregoing.

4.8 Title to Assets, Etc. The Company and the Subsidiaries have good title to or valid and subsisting leasehold interests in all real and material personal property and other material assets on their books and reflected on the balance sheets included in the Company Interim Financial Statements or acquired in the ordinary course of business since September 30, 1995 which would have been required to be reflected on such balance sheets if acquired on or prior to September 30, 1995, other than (i) assets which have been disposed of in the ordinary course of business and (ii) assets which were disposed in connection with the conversion of the Company and the Subsidiaries' investment portfolio into cash and Cash Equivalents (the "Assets"). None of the Assets is subject to any Encumbrance, except for Encumbrances reflected in the financial statements contained in Schedule 4.12, as applicable, or which in the aggregate are not substantial in amount and do not materially detract from the value of the property or assets subject thereto or interfere with the present use.

4.9 Contracts and Commitments. (a) None of the Company or any Subsidiary is a party to any written or oral:

(i) Contracts not otherwise listed in Schedule 4.9;

(ii) except as listed on Schedule 4.9, treaties and agreements with, and undertakings or commitments to, any governmental or regulatory authority materially affecting the business of the Company and the Subsidiaries taken as a whole and not made in the ordinary course of business;

(iii) except as described in Schedule 4.9, contracts or agreements containing covenants limiting the freedom of the Company or any Subsidiary to engage in any line of business in any geographic area or to compete with any Person or to incur indebtedness for borrowed money;

(iv) except as described in Schedule 4.9 and for reinsurance and retrocession agreements, contracts or agreements containing "change in control" or similar provisions;

(v) except as listed on Schedule 4.9, employment contracts or agreements, including without limitation contracts to employ executive officers and other contracts with officers or directors of the Company or any Subsidiary which cannot be terminated by the Company or the Subsidiary upon notice of sixty days or less without penalty or premium and involve annual compensation in excess of $100,000 individually; or

(vi) contracts or agreements providing for the indemnification by the Company or any Subsidiary of any Person except for contracts entered into in the ordinary course of business consistent with past practice.

(b) None of the Company or any Subsidiary is (and, to the Knowledge of the Seller, no other party is) (i) in material breach of or materially in default under, any of the Contracts (or with or without notice or lapse of time or both, would be in material breach of or materially in default under any of the Contracts) or (ii) in breach or default under any of the Contracts (with or without notice or lapse of time or both) if such breach or default would permit a party other than the Company or a Subsidiary to terminate such Contract. None of Parent, Seller, the Company or any Subsidiary has delivered or received notice of termination or written notice of an intention to terminate to or from any other party to any Contract except as described on Schedule 4.9.

(c) Other than the Ridge Re Treaty and the other treaties referenced in the first sentence of Section 4.9(c) of the Talegen Agreement, Ridge Re is not a party to any reinsurance or retrocession agreement or treaty, and, except in connection with such treaties, does not engage in any business. Set forth in Schedule 4.9 is the amount of cover as of the date of this Agreement available under the Ridge Re Treaty. A true and complete copy of the Ridge Re Treaty is contained in Schedule 1.1D. The Ridge Re Treaty is in full force and effect and constitutes a legal, valid and binding obligation of the parties thereto, enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing. None of Parent, Seller, Talegen, the Company or any Subsidiary has received any notice from Ridge Re or any governmental or regulatory authority (i) that the Ridge Re Treaty is not enforceable against any party thereto or (ii) regarding the availability or enforceability of the cover under the Ridge Re Treaty. No party to the Ridge Re Treaty has received notice of termination of, or written notice of an intention to terminate, the Ridge Re Treaty. No party to the Ridge Re Treaty is in breach of or violation of or default under the Ridge Re Treaty (or with or without notice or lapse of time or both, would be in breach of or violation of or default under the Ridge Re Treaty), except for breaches, violations or defaults by IIC which would not permit Ridge Re to terminate the Ridge Re Treaty or which would not provide Ridge Re with a defense to any payment obligation of Ridge Re thereunder.

4.10 No Conflict or Violation. Except as set forth in Schedule 4.10, neither the execution, delivery and performance of this Agreement or any of the Ancillary Agreements nor the consummation of the transactions contemplated hereby or thereby will result in (a) a violation of or a conflict with any provision of the certificate of incorporation or bylaws of Parent, Seller, Talegen, Ridge Re, the Company or any Section 4.5 Subsidiary, (b) a breach of, or a default under, any term or provision of any contract, agreement, indebtedness, lease, Encumbrance, commitment, license, franchise, Permit, authorization or concession to which (i) Parent, Seller, Talegen or Ridge Re is a party or is subject or by which any assets (including investments) of any of them are bound or (ii) the Company or any Subsidiary is a party or is subject or by which any assets (including investments) of any of them are bound, which breach or default in the case of clause (ii) would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or in the case of clauses (i) and (ii) would interfere in any material way with the ability of Parent or Seller to consummate the transactions contemplated by this Agreement or any of the Ancillary Agreements or the Ridge Re Treaty, (c) subject to obtaining the

approvals referred to in Section 4.11, a violation by Parent, Seller, Talegen, Ridge Re, the Company or any Subsidiary of any statute, rule, regulation, ordinance, code, order, judgment, writ, injunction, decree or award, which violation would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or interfere in any material way with the ability of Parent, Seller or Ridge Re to consummate the transactions contemplated by this Agreement or any of the Ancillary Agreements, (d) the imposition of any Encumbrance, restriction or charge on the business of the Company or any Subsidiary or on any material assets of the Company or the Subsidiaries, (e) the creation or exercisability of any right of termination, cancellation or acceleration under any Contract or (f) result in the breach of any of the terms or conditions of, constitute a default under, or otherwise cause any impairment of, any Permit, which breach, default or impairment would result, individually or in the aggregate, in a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.11 Consents and Approvals. Except for (i) the approval of this Agreement, the Ancillary Agreements and the transactions contemplated hereby and thereby (including, without limitation, the Financing), and the new intercompany tax agreements among the Company and the Subsidiaries which shall be effective as of the Closing, by each of the governmental and regulatory authorities listed on Schedule 4.11, (ii) the approval of this Agreement, the Ancillary Agreements and the transactions contemplated hereby and thereby (including, without limitation, the Financing), and the new intercompany tax agreements among the Company and the Subsidiaries which shall be effective as of the Closing, by any other governmental or regulatory authorities, the failure of which to obtain would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, (iii) filings in respect of the transactions contemplated hereby required to be made for compliance with the applicable provisions of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the rules and regulations promulgated thereunder, (iv) the filing of premerger notification reports under the HSR Act and (v) consents, approvals, authorizations, declarations, filings and registrations required (x) by the nature of the business or ownership of Buyer or (y) solely by reason of the Financing (excluding any consents, approvals, authorizations, declarations, filings or registrations otherwise required in connection with this Agreement, the Ancillary Agreements or the transactions contemplated hereby or thereby), no consent, approval or authorization of, or declaration, filing or registration with, any governmental or regulatory authority, or any other Person, is required to be made or obtained by Parent, Seller, Talegen, Ridge Re, the Company, any Subsidiary or Buyer on or prior to the Closing Date in connection with the execution or delivery of this Agreement or any of the Ancillary Agreements, the performance of this Agreement, the Guarantees, the Tax Agreement, or the Ridge Re Treaty or the consummation of the transactions contemplated hereby and thereby.

4.12 Financial Statements. (a) Seller has heretofore delivered to Buyer the Company GAAP Financial Statements, the Ridge Re GAAP Financial Statements, the Company Interim Financial Statements, the Ridge Re Interim Financial Statements and the Convention Statements. A copy of each of the foregoing financial statements is included in Schedule 4.12.

(b) Except as otherwise set forth therein, (i) the Company GAAP Financial Statements are based on the books and records of the Company and its Subsidiaries, fairly present in all material respects the financial condition and consolidated results of operations of the Company and its Subsidiaries, as of the dates and for the periods indicated therein, have been prepared in accordance with GAAP (as in effect at the time of the respective financial statements) consistently applied, and have been audited by KPMG Peat Marwick LLP and (ii) the Ridge Re GAAP Financial Statements are based on the books and records of Ridge Re, fairly present in all material respects the financial condition and results of operation of Ridge Re, as of the dates and for the periods indicated therein, have been prepared in accordance with GAAP (as in effect at the time of the respective financial statements) consistently applied, and have been audited by KPMG Peat Marwick LLP.

(c) The Company Interim Financial Statements and the Ridge Re Interim

Financial Statements were prepared in the ordinary course of business and have been prepared on a consistent basis through the periods indicated and in a manner consistent with that employed in the Company GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be. The Company Interim Financial Statements and the Ridge Re Interim Financial Statements do not contain full footnote disclosures in accordance with United States generally accepted accounting principles and are subject to normal recurring year-end adjustments, but otherwise fairly present in all material respects the financial condition and results of operations of the Company and Ridge Re, as the case may be, as of the dates and for the periods indicated therein except as otherwise set forth therein.

(d) Except as otherwise set forth therein, the Convention Statements and the statutory balance sheets and income statements included in such Convention Statements fairly present in all material respects the statutory financial condition and results of operations of the respective Insurance Subsidiaries and Ridge Re, as the case may be, as of the dates and for the periods indicated therein and have been prepared in accordance with Statutory Accounting Principles (as in effect at the time of the respective financial statements) consistently applied throughout the periods indicated, except as expressly set forth therein. The statutory balance sheets and income statements included in the Convention Statements for the years ended December 31, 1993 and 1994 have been audited by KPMG Peat Marwick LLP.

4.13 Litigation. To the Knowledge of Seller, except as set forth on Schedule 4.13, there is no action, order, writ, injunction, judgment, fine or decree outstanding or suit, litigation, proceeding, labor dispute (other than routine grievance procedures or routine, uncontested claims for benefits under any benefit plans for any officers, employees or agents of the Company or any Subsidiary (collectively, "Personnel")), arbitral action, investigation or reported claim, in each case including, without limitation, those involving any governmental or regulatory authority and excluding those relating to insurance and reinsurance policies (collectively, "Actions") pending or threatened by or against or relating to (i) the Company or any Subsidiary, (ii) any benefit plan for Personnel or any fiduciary or administrator thereof or (iii) the transactions contemplated by this Agreement and the Ancillary Agreements. None of the Company or any Subsidiary is in default with respect to any order, writ, injunction, judgment, fine or decree of any court or governmental or regulatory agency, and there are no unsatisfied judgments against the Company or any Subsidiary which would have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.14 Liabilities. Except as set forth in Schedule 4.14, the Company and the Subsidiaries do not have any direct or indirect indebtedness, liability, claim, loss, damage, deficiency, obligation or responsibility, fixed or unfixed, choate or inchoate, liquidated or unliquidated, secured or unsecured, accrued, absolute, contingent or otherwise ("Liabilities"), other than (i) Liabilities fully and adequately reflected (including by reducing any numerical amount set forth) in one or more line items on, reserved on, or disclosed in the footnotes to, the balance sheets included in the Company Interim Financial Statements, or disclosed in the footnotes to the Company GAAP Financial Statements, (ii) Liabilities incurred in the ordinary course of business, consistent with past practice and the provisions of this Agreement and the Ancillary Agreements, (iii) Liabilities relating to future benefits, losses, claims and expenses arising under insurance and reinsurance policies of the Insurance Subsidiaries, (iv) Liabilities disclosed in response to any other representation, (v) Liabilities of a type that are subject to any other representation (without regard to any specific exclusions from such representation, including any specific exclusions from the definitions used therein) and (vi) Liabilities which have, or are reasonably likely to have a net ultimate cost of $25,000 or less, on an individual basis or in the aggregate to the extent such Liabilities arise out of a related series of events.

4.15 Investments. (a) As of the date of this Agreement, at least 83% of the investment portfolio for the Company and the Subsidiaries consists of cash and Cash Equivalents and at least 87% of the investment portfolio (excluding cash

and Cash Equivalents) for the Company and the Subsidiaries consists of fixed income securities rated at least AA by Moody's or by S&P. As of the date hereof, at least 87% of the fixed income portfolio (excluding cash and Cash Equivalents) has a maturity of one year or less.

(b) To the Knowledge of Seller, as of the Closing Date, the Company and the Subsidiaries have good and marketable title to the investments in their investment portfolios, provided that no representation is made as to the transferability thereof.

4.16 Reserves. Seller has delivered to Buyer true and complete copies of all actuarial reports or actuarial certificates in the possession or control of Parent, Seller, Talegen, the Company or any of the Subsidiaries relating to the adequacy of the claims reserves of any of the Subsidiaries for any period ended on or after December 31, 1993. Notwithstanding the foregoing representations contained in this Section or anything contained in Section 4.12, 4.14 or 6.2, Buyer acknowledges that Parent and Seller are not making any representations, express or implied in or pursuant to this Agreement, concerning the loss reserves or loss adjustment expense reserves of the Company or any of the Subsidiaries including, without limitation, (i) whether such reserves are adequate or sufficient, or (ii) whether such reserves were determined in accordance with any actuarial, statutory or other standard, or concerning any other "line item" or asset, liability or equity amount which would be affected thereby.

4.17 Compliance with Law; Permits; Regulatory. (a) Except as set forth on Schedule 4.17, the Company and the Subsidiaries are in compliance with all applicable laws, statutes, ordinances and regulations, whether Federal, foreign, state or local, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Since January 1, 1993, none of the Company or any Subsidiary has received any written notice to the effect that, or otherwise been advised that, it is not in compliance with any such statute, regulation, order, ordinance or other law where the failure to comply would, prior to June 30, 1998, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(b) Except as set forth on Schedule 4.17, the Company and the Subsidiaries hold all Permits necessary for the ownership and conduct of the respective businesses of the Company and the Subsidiaries in each of the jurisdictions in which the Company and the Subsidiaries conduct or operate their respective businesses in the manner now conducted, and such Permits are in full force and effect except where the failure to hold any Permit or the failure of any Permit to be in full force and effect would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. The consummation of the transactions contemplated by this Agreement will not result in any revocation, cancellation or suspension of any such Permit except as a result of the status of Buyer and its Affiliates, and, there are no pending or threatened suits, proceedings or investigations with respect to revocation, cancellation, suspension or nonrenewal thereof, and, there has occurred no event which (whether with notice or lapse of time or both) will result in such a revocation, cancellation, suspension or nonrenewal thereof, in any such case except where such a revocation, cancellation, suspension or non-renewal would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

(c) All insurance policies issued by the Insurance Subsidiaries, as now in force are, to the extent required under applicable law, are in a form acceptable to applicable regulatory authorities or have been filed and not objected to (or such objection has been withdrawn or resolved) by such authorities within the period provided for objection, except where such failure or objection would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Neither the Company nor any Subsidiary which is not an Insurance Subsidiary has issued any insurance policies. Except as set forth on Schedule 4.17, (i) all material reports, statements, documents, registrations, filings and submissions to state insurance regulatory authorities complied in all material respects with applicable law in effect when filed and (ii) no material

deficiencies have been asserted by any such regulatory authority with respect to such reports, statements, documents, registrations, filings or submissions that have not been satisfied or that would, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. Except as set forth on Schedule 4.17, all premium rates established by the Insurance Subsidiaries that are required to be filed with or approved by insurance regulatory authorities have been so filed or approved, the premiums charged conform to the premiums so filed or approved and comply (or complied at the relevant time) with the insurance laws applicable thereto except where such failures to comply, individually or in the aggregate, would not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.18 No Brokers. Except as previously disclosed in writing to Buyer, neither Parent, Seller, Talegen nor the Company has employed, or is subject to any valid claim of, any broker, finder, consultant or other intermediary in connection with the transactions contemplated by this Agreement who will be entitled to a fee or commission in connection with such transactions. Parent is solely responsible for any such payment, fee or commission that may be due to any Person so previously disclosed to Buyer in connection with the transactions contemplated hereby.

4.19 No Other Agreements to Sell the Assets or the. Except as set forth in Schedule 4.19, none of Parent, Seller, Talegen, the Company or any Subsidiary has any agreement, absolute or contingent, with any other Person to sell the capital stock, assets (other than sales of assets that would not be prohibited under Section 4.7(c)) or business of the Company or any Subsidiary or to effect any merger, consolidation or other reorganization of the Company or any Subsidiary or to enter into any agreement with respect thereto.

4.20 Proprietary Rights. (a) Except as set forth in Schedule 4.20, Parent, Seller and their Affiliates (other than the Company and the Subsidiaries) have no right or title to or interest in the trademarks, service marks, copyrights, trade names and the applications and registrations therefor and the trade secrets, software and other proprietary rights used in and material to the business of the Company or any of its Subsidiaries (collectively, "Intellectual Property").

(b) Schedule 4.20 sets forth a complete and correct list and brief description of all Intellectual Property that is material to the Company or any Subsidiary. With respect to intellectual property owned by the Company or a Subsidiary, such entity has the sole and exclusive right to use and is the sole and exclusive registered owner of all right, title and interest in and to the Intellectual Property. The Intellectual Property which is not owned by the Company or a Subsidiary is being used by the Company or a Subsidiary only with the consent of or license from the rightful owner thereof, and all such licenses are in full force and effect.

(c) To the Knowledge of Seller no activity in which the Company or a Subsidiary is engaged or any product which the Company or a Subsidiary sells, or any advertising that they employ, or the use of any of the Intellectual Property, breaches, violates, infringes or interferes with any rights of any third party or, except for the payment of computer software licensing fees, requires payment for the use of any patent, trade-name, trade secret, trade-mark, copyright or other intellectual property right or technology of another.

4.21 Employee Benefit Plans. (a) Schedule 4.21 contains a true and complete list of each "employee benefit plan" (within the meaning of section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), including, without limitation, multiemployer plans within the meaning of ERISA section 3(37)), stock purchase, stock option, severance, employment, change-in-control, fringe benefit, collective bargaining, bonus, incentive, deferred compensation and all other employee benefit plans, agreements, programs, policies or other arrangements, whether or not subject to ERISA (including any funding mechanism therefor now in effect or required in the future as a result of the transactions contemplated by this Agreement or otherwise), whether formal or informal, oral or written, legally binding or not, under which any employee or former employee of the Company or any Subsidiary has any present or future right to benefits or under which the Company or any Subsidiary has

any present or future liability. All such plans, agreements, programs, policies and arrangements shall be collectively referred to as the "Company Plans".

(b) With respect to each Company Plan, the Company has delivered to the Buyer a current, accurate and complete copy (or, to the extent no such copy exists, an accurate description) thereof and, to the extent applicable, (i) any related trust agreement, annuity contract or other funding instrument; (ii) the most recent determination letter; (iii) any summary plan description and other written communications (or a description of any oral communications) by the Company or any Subsidiary to their employees concerning the extent of the benefits provided under a Company Plan; and (iv) for the three most recent years (A) the Form 5500 and attached schedules; (B) audited financial statements; (C) actuarial valuation reports; and (D) attorney's response to an auditor's request for information.

(c) (i) Each Company Plan, in all material respects, has been established and administered in accordance with its terms and in compliance with the applicable provisions of ERISA, the Code and other applicable laws, rules and regulations; (ii) each Company Plan which is intended to be qualified within the meaning of Code section 401(a) is so qualified and has received a favorable determination letter as to its qualification and nothing has occurred, whether by action or failure to act, which would cause the loss of such qualification; (iii) except as listed on Schedule 4.21, with respect to any Company Plan, no actions, suits or claims (other than routine claims for benefits in the ordinary course) are pending or threatened, no facts or circumstances exist which could give rise to any such actions, suits or claims, and the Company will promptly notify Buyer in writing of any pending or threatened claims arising between the date hereof and the Closing Date; (iv) neither the Company, any Subsidiary nor any other party has engaged in a prohibited transaction, as such term is defined under Code section 4975 or ERISA section 406, which would subject the Company, any Subsidiary or the Buyer to any material taxes, penalties or other liabilities under Code section 4975 or ERISA sections 409 or 502(i); (v) no event has occurred and no condition exists that would subject the Company, either directly or by reason of its affiliation with any member of its "Controlled Group" (defined as any organization which is a member of a controlled group of organizations within the meaning of Code sections 414(b), (c), (m) or (o)), or any Subsidiary to any material tax, fine or penalty imposed by ERISA, the Code or other applicable laws, rules and regulations including, but not limited to the taxes imposed by Code sections 4971, 4972, 4977, 4979, 4980B, 4976(a) or the fine imposed by ERISA section 502(c); (vi) all insurance premiums required to be paid with respect to Company Plans as of the Closing Date have been or will be paid prior thereto and adequate reserves have been provided for on the Company's Interim Financial Statements as of September 30, 1995, to the extent required by GAAP, for any premiums (or portions thereof) attributable to service on or prior to the Closing Date; (vii) for each Company Plan with respect to which a Form 5500 has been filed, no material change has occurred with respect to the matters covered by the most recent Form since the date thereof; (viii) all contributions required to be made prior to the Closing Date under the terms of any Company Plan, the Code, ERISA or other applicable laws, rules and regulations have been or will be timely made and adequate reserves have been provided for on the Company's Interim Financial Statements as of September 30, 1995, to the extent required by GAAP, for all benefits attributable to service on or prior to the Closing Date; (ix) no Company Plan provides for an increase in benefits on or after the Closing Date; and (x) no Company Plan (excluding any agreement between the Company and individual employees) contains any contractual language which limits the Company's ability to amend or terminate such Company Plan without obligation or liability (other than those obligations and liabilities for which specific assets have been set aside in a trust or other funding vehicle or reserved for on the Company's Interim Financial Statements as of September 30, 1995).

(d) (i) No Company Plan has incurred any "accumulated funding deficiency" as such term is defined in ERISA section 302 and Code section 412 (whether or not waived); (ii) no event or condition exists which would be deemed a reportable event within the meaning of ERISA section 4043 which could result in a material liability to the Company, any member of its Controlled Group or any

Subsidiary, and no condition exists which could subject the Company, any member of its Controlled Group or any Subsidiary to a material fine under ERISA section 4071; (iii) as of the Closing Date, the Company, each member of its Controlled Group and each Subsidiary will have made all premium payments required to be made prior to the Closing Date to the PBGC; (iv) neither the Company, any member of its Controlled Group nor any Subsidiary is subject to any liability to the PBGC for any plan termination occurring on or prior to the Closing Date; (v) no amendment has occurred which has required or would require the Company, any member of its Controlled Group or any Subsidiary to provide security pursuant to Code section 401(a)(29); and (vi) neither the Company, any member of its Controlled Group nor any Subsidiary has engaged in a transaction which could subject it to material liability under ERISA section 4069

(e) With respect to each of the Company Plans which is not a multiemployer plan within the meaning of section 4001(a)(3) of ERISA but is subject to Title IV of ERISA, the funded status of each such Company Plan, as of January 1, 1995, is as reported in the actuarial valuation reports dated as of January 1, 1995. To the Knowledge of Seller, no material adverse change in the funded status of such Company Plans has occurred since January 1, 1995, and no material defects or omissions existed in the data provided to the preparers of the actuarial valuation reports discussed in the preceding sentence.

(f) There are no multiemployer plans (within the meaning of section 4001(a)(3) of ERISA) to which the Company, any member of its Controlled Group or any Subsidiary has or had any liability or contributes (or has at any time contributed or had an obligation to contribute).

(g) (i) Each Company Plan which is intended to meet the requirements for tax-favored treatment under Subchapter B of Chapter 1 of Subtitle A of the Code meets such requirements; and (ii) the Company and the Subsidiaries have no trusts intended to be qualified within the meaning of Code section 501(c)(9), and, except as listed on Schedule 4.21, had no such trusts in the past.

(h) Schedule 4.21 sets forth, on a plan-by-plan basis, the present value of any benefits payable presently or in the future to present or former employees of the Company or any Subsidiary under any Company Plan (excluding any agreements between the Company and individual employees which were not entered into as part of any plan or program) that is not fully funded and not subject to the reporting requirements of ERISA (if such amounts are not reflected in the financial statements included in Schedule 4.12) which present value is as reported in the most recent actuarial valuation or other reports done with respect to each such plan. To the Knowledge of Seller, no material adverse increase in the amount of such present values has occurred since the date of the most recent report, and no material defects or omissions existed in the reports, or, if applicable, in the data provided to the preparers of the reports.

(i) Except as set forth on Schedule 4.21 or referenced in Section 9.4, no Company Plan exists which could result in the payment to any Company employee or Subsidiary employee of any money or other property or accelerate or provide any other rights or benefits to any Company employee or Subsidiary employee as a result of the transactions contemplated by this Agreement, whether or not such payment would constitute a parachute payment within the meaning of Code section 280G. There is no cost to the Company and its Subsidiaries in the event that all Company Plans set forth in Schedule 4.21 are triggered.

(j) Neither the Company nor any Subsidiary is obligated or otherwise required to pay any bonuses (annual or otherwise) to Joseph W. Brown, Jr., or to any managing director of the Company on or after the date of the Closing.

(k) No Company Plan operates within or is subject to the jurisdiction of any foreign country, other than as described on Schedule 4.21.

(l) None of the amounts payable to any Company employee or any Subsidiary employee as a result of the transactions contemplated by this Agreement will be non-deductible under Section 280G of the Code.

4.22 Employment-Related Matters. Except as set forth in Schedule 4.22, (a) none of the Company or the Subsidiaries is a party to, or otherwise bound by, any consent decree with, or citation by, any government agency relating to employees or employment practices, (b) none of the Company or any of the Subsidiaries has closed any plant or facility, or effectuated any layoffs of employees within the past six months, nor have the Company or the Subsidiaries planned or announced any such action or programs for the future, and (c) the Company and the Subsidiaries are in compliance with their respective obligations pursuant to the Worker Adjustment and Retraining Notification Act of 1988 and any similar state notification law.

4.23 Transactions with Certain Persons. (a) To the Knowledge of Seller, neither any officer, director or employee of Parent, Seller, the Company or any Subsidiary nor any member of any such Person's immediate family is presently a party to any material transaction with the Company or any Subsidiary, including, without limitation, any Contract, or other binding arrangement (i) providing for the furnishing of material services (except in such Person's capacity as an officer, director, employee or consultant) by, (ii) providing for the rental of material real or personal property from, or (iii) otherwise requiring material payments to (other than for services as officers, directors or employees of Parent, Seller, the Company or any Subsidiary) any such Person.

(b) Schedule 4.23 sets forth all contracts, agreements and arrangements in effect on or after January 1, 1995, and all transactions (including, without limitation, the provision of any services or the sale of any goods) since January 1, 1994 between the Company or any Subsidiary, on the one hand, and Parent or any Affiliate of Parent (excluding the Company and the Subsidiaries, but including Talegen and its subsidiaries), on the other, excluding contracts, agreements and arrangements (i) relating to the use or purchase of products leased or sold by Parent in the ordinary course of Parent's document processing business, (ii) involving payments by or to the Company or any Subsidiary that do not exceed $100,000 in the aggregate or (iii) specifically referred to in the financial statements contained in Schedule 4.12. Certain Subsidiaries hold $25,000,000 aggregate principal amount of promissory notes issued by Seller and unconditionally guaranteed by Parent (such notes, collectively, the "Seller Notes"). Schedule 4.23 identifies the current holders of each of the Seller Notes.

(c) Except in the ordinary course of business consistent with past practice, since the Balance Sheet Date, Seller and the Company and/or any Subsidiary have not settled any intercompany trade receivables and payables.

4.24 Taxes. (a) Filing of Tax Returns. Seller and the Company (and any affiliated group of which the Company is now or has been a member) have timely filed with the appropriate taxing authorities all Federal, and to the Knowledge of Seller, state and local Tax Returns and Information Returns required to be filed through the date hereof. All such Federal, and to the Knowledge of Seller, state and local Tax Returns and Information Returns are complete and accurate in all material respects. The Company is a member of an affiliated group of corporations, within the meaning of Section 1504 of the Code, that includes Seller and Parent, and Parent is the common parent of the affiliated group.

(b) Payment of Taxes. All Taxes shown in the Tax Returns referred to in Section 4.24(a) above that are due and payable by the Company and its Subsidiaries before the date hereof have been paid.

(c) Liens for Taxes. There are no liens or other Encumbrances on any of the assets of the Company or any Subsidiary that arose in connection with any failure (or alleged failure) to pay any Tax.

(d) Audit History. Except as set forth in Schedule 4.24, there is no action, suit, proceeding, investigation, audit or claim now pending or, to the Knowledge of Seller, proposed against or with respect to the Company or any of its Subsidiaries or any affiliated group of which the Company and its Subsidiaries is or has been a member that relates to Tax liabilities attributable to items of income, gain, deduction, loss or credits of the

Company or any of its Subsidiaries.

(e) Prior Affiliated Groups. Except as set forth in Schedule 4.24 and except for the affiliated group of corporations of which the Company and the Subsidiaries is currently a member and of which Parent is the common parent, the Company and the Subsidiaries have never been members of an affiliated group of corporations, within the meaning of Section 1504 of the Code.

(f) Withholding. The Company and the Subsidiaries have withheld and paid all Federal, and to the Knowledge of Seller, state and local Taxes required to have been withheld and paid in connection with amounts paid or owing to any employee, independent contractor, creditor, stockholder or other third party.

(g) FIRPTA. Neither the Company nor any of the Subsidiaries have been a United States real property holding corporation within the meaning of Section 897(c)(2) of the Code during the five-year period ending on the date hereof.

(h) Material Adverse Effect. A representation with respect to Taxes contained in this Section 4.24 shall be deemed to be accurate unless an inaccuracy contained therein has a Material Adverse Effect on the Company and the Subsidiaries.

4.25 Reinsurance and Retrocessions. Schedule 4.25 contains a list as of the date of this Agreement of all treaty reinsurance or retrocession treaties and agreements in force to which any Subsidiary is a party (including any terminated or expired treaty or agreement under which there remains any outstanding liability with respect to paid or unpaid case reserves in excess of $500,000), any terminated or expired treaty or agreement under which there remains any outstanding liability from one reinsurer with respect to paid or unpaid case reserves in excess of $100,000 and any treaty or agreement with any Affiliate of such Subsidiary, the effective date of each such treaty or agreement, and the termination date of any treaty or agreement which has a definite termination date. To the Knowledge of Seller, no Subsidiary is in default in any respect as to any provision of any reinsurance or retrocession treaty or agreement or has failed to meet the underwriting standards required for any business reinsured thereunder except for defaults which, individually or in the aggregate, would not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

4.26 1992/93 Restructuring. All novations made pursuant to the 1992/93 Restructuring and any amendments to the Ridge Re Treaty made prior to the date hereof, were made in accordance with all applicable laws, rules and regulations at the time such novations or amendments were completed except where the failure to do so (i) would not, individually or in the aggregate, have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, or (ii) was a result of the failure by the Company or any Subsidiary to obtain the consent of any insured or policyholder to the novation or assumption of the relevant insurance policy. Notwithstanding the foregoing, Buyer acknowledges that Seller and Parent shall have no liability to Buyer for breach of this representation with respect to any novation or assumption, or any amendment to the Ridge Re Treaty, which results in any liability for the Company or any of its Subsidiaries, if there is a corresponding benefit realized (or any liability avoided) by the Company or any other Subsidiary or Talegen or any of its subsidiaries.

4.27 Capital Commitments. Schedule 4.27 contains a list of all capital commitments as of the date of this Agreement of the Company or any Subsidiary in excess of $100,000.

4.28 Environmental Laws. (a) Each of the Company and each Subsidiary complies and has complied with all applicable Environmental Laws, and possesses and complies with and has possessed and complied with all Environmental Permits required under such laws except where the failure to be in possession of or to comply with such Environmental Permits, or where the failure to be in compliance with any Environmental Law, would not have, individually or in the aggregate, a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole. There are no past, present, or anticipated future events, conditions, circumstances, practices, plans or

legal requirements that could reasonably be expected to prevent, or materially increase the burden on the Company or any Subsidiary of their complying with applicable Environmental Laws or of their obtaining, renewing, or complying with all Environmental Permits required under such laws. There are and have been no Materials of Environmental Concern or other conditions at any property owned, operated or otherwise used by the Company or any Subsidiary now or in the past, or at any other location, that could reasonably be expected to give rise to liability of the Company or any Subsidiary under any Environmental Law. Parent, Seller and the Company have provided to Buyer true and complete copies of all Environmental Reports prepared within the last five years in their possession or control.

(b) Notwithstanding the representations contained in this Section, Buyer acknowledges that Parent and Seller are not making any representations (express or implied in or pursuant to this Agreement) with respect to any violation of or noncompliance with Environmental Law or Environmental Permits, or failure to obtain Environmental Permits, in each case by reason of any policy of insurance, reinsurance, indemnity, guaranty or assumption of liability of any party, entered into by the Company or any Insurance Subsidiary.

4.29 Acquisition for Investment. Each of Seller and Parent acknowledges that the Securities have not been registered under the Securities Act, or under any state securities laws. Each of Seller and Parent (to the extent Parent acquires Securities pursuant to Section 11.3) is acquiring the Securities solely for its own account and not with a view to any distribution or other disposition of such Securities or any part thereof, or interest therein, except in accordance with the Securities Act. Each of Seller and Parent is an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act).

ARTICLE V

REPRESENTATIONS AND WARRANTIES OF BUYER

Buyer hereby represents and warrants to Seller and Parent as follows:

5.1 Organization of Buyer. Buyer is duly organized, validly existing and in good standing under the laws of the State of Delaware and has full corporate power and authority to conduct its business and to own and lease its properties.

5.2 Authorization. Buyer has all necessary corporate authority to enter into this Agreement the Tax Agreement and has taken all necessary corporate action to consummate the transactions contemplated hereby and to perform its obligations hereunder. This Agreement and the Tax Agreement have been duly executed and delivered by Buyer. Assuming the due execution of this Agreement by Parent and Seller, this Agreement is a legal, valid and binding obligation of Buyer enforceable against it in accordance with its terms, subject to the effects of bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and other similar laws relating to or affecting creditors' rights generally, general equitable principles (whether considered in a proceeding in equity or at law) and an implied covenant of good faith and fair dealing.

5.3 No Conflict or Violation. Neither the execution, delivery and performance of this Agreement or the Tax Agreement by Buyer nor the issuance of the Class 2 Stock by Buyer, nor the issuance, if issued, of Class 1 Stock by Buyer pursuant to the provisions of Section 11.3, nor the consummation by Buyer of the transactions contemplated hereby or thereby will result in (a) a violation of or a conflict with any provision of the certificate of incorporation or bylaws of Buyer, (b) a breach of, or a default under, any term or provision of any contract, agreement, indebtedness, lease, Encumbrance, commitment, license, franchise, Permit, authorization or concession (including any agreements, documents or instruments (the "Financing Documents") constituting part of the financing required to consummate the transactions contemplated by this Agreement (the "Financing")) to which Buyer is a party or is subject or by which any assets of Buyer are bound, which breach or default is in a Financing Document or would, individually or in the

aggregate, have a Material Adverse Effect on Buyer or interfere in any material way with the ability of Buyer to consummate the transactions contemplated by this Agreement and the Tax Agreement, or (c) subject to obtaining the approvals referred to in Section 4.11, a violation by Buyer of any statute, rule, regulation, ordinance, code, order, judgment, writ, injunction, decree or award, which violation would, individually or in the aggregate, have a Material Adverse Effect on Buyer or its ability to consummate the transactions contemplated by this Agreement and the Tax Agreement.

5.4 No Brokers. Except for the services of Merrill Lynch & Co., Buyer has not employed, and is not subject to the valid claim of, any broker, finder, consultant or other intermediary in connection with the transactions contemplated by this Agreement who will be entitled to a fee or commission in connection with such transactions. Buyer is solely responsible for any such payment, fee or commission that may be due to Merrill Lynch & Co. in connection with the transactions contemplated by this Agreement.

5.5 Acquisition for Investment. Buyer acknowledges that the Stock has not been registered under the Securities Act or under any state securities laws. Buyer is acquiring the Stock solely for its own account and not with a view to any distribution or other disposition of the Stock or any part thereof, or interest therein, except in accordance with the Securities Act. Buyer is an "accredited investor" (as defined in Rule 501 of Regulation D under the Securities Act).

5.6 Organizational Documents. Copies of the certificate of incorporation and bylaws of Buyer have heretofore been delivered to Seller and such copies are true, accurate and complete, without any amendment, modification or supplement, as of the date of this Agreement and, after giving effect to the filing of the Restated Certificate of Incorporation prior to Closing, the Closing Date (except such amendments, modifications or supplements which would not have a Material Adverse Effect on Seller or which change the amount of authorized capital stock).

5.7 Capitalization of Buyer. (a) As of the Closing Date, investment partnerships affiliated with KKR shall own, directly or indirectly, no less than 70% of the Class 1 Stock, which percentage shall be reduced to reflect any investment made by Parent and/or Seller pursuant to Section 11.3.

(b) In the event that Seller acquires any of the Class 1 Stock as provided in Section 11.3 hereof, such shares will be duly authorized, validly issued, fully paid and nonassessable, and free of preemptive rights.

(c) Upon consummation of the transactions contemplated by this Agreement, the Class 2 Stock to be issued by Buyer pursuant hereto, when delivered by Buyer for the consideration specified herein, will be duly and validly authorized and issued by Buyer, fully paid, nonassessable and free of preemptive rights and Seller will acquire good and marketable title thereto, free and clear of all Encumbrances, except Encumbrances arising as a result of any action taken by Seller or any of its Affiliates; provided that Buyer makes no representations regarding the ability of any Person other than Buyer to transfer or otherwise dispose of such Class 2 Stock without registration or qualification under, or in compliance with, applicable Federal securities or state securities or insurance laws.

5.8 Consents and Approvals. Except for (i) consents, approvals, authorizations, declarations, filings and registrations required by the nature of the business or ownership of Parent, Seller, the Company and the Subsidiaries, (ii) filings in respect of the transactions contemplated hereby required to be made for compliance with the applicable provisions of the Exchange Act and the rules and regulations promulgated thereunder and (iii) the filing of premerger notification reports under the HSR Act, no consents, approval or authorization of, or declaration, filing or registration with, any governmental or regulatory authority, or any other Person, is required to be made or obtained by Buyer or any of its Affiliates in connection with the execution, delivery and performance of this Agreement, the Ancillary Agreements and the consummation of the transactions contemplated hereby and

thereby.

5.9 Financial Obligations. Buyer has received and delivered copies to Seller of (i) a commitment letter from senior lenders regarding the transactions contemplated by this Agreement, (ii) a letter with respect to equity Financing (other than that to be provided by management of the Company), which letter is addressed to Seller and (iii) an agreement in principal between Buyer and management of the Company with respect to the investment by management referred to in Section 8.16.

5.10 Solvency. At the Closing (after and giving effect to the acquisition of the Stock and the Financing), neither Buyer nor the Company will (i) be insolvent (either because its financial condition is such that the sum of its debts is greater than the fair value of its assets or because the present fair saleable value of its assets will be less than the amount required to pay its probable liability on its debts as they become absolute and matured), (ii) has unreasonably small capital with which to engage in its business or (iii) has incurred or plan to incur debts beyond its ability to pay as they become absolute and matured.

ARTICLE VI

ACTIONS BY PARENT, SELLER AND BUYER PRIOR TO THE CLOSING

Parent, Seller and Buyer covenant as follows for the period from the date hereof to the Closing Date (except, in the case of Section 6.16, for the period specified in such Section):

6.1 Maintenance of Business and Preservation of Permits and Services. Except as expressly contemplated by this Agreement, Seller shall cause the Company and each Subsidiary to carry on its business, in the ordinary course consistent with past practice. Neither Parent nor Seller shall cause the Company or any Subsidiary to terminate an officer thereof or to diminish the duties or responsibilities of such officer.

6.2 Additional Financial Statements. As soon as reasonably practicable after the end of the applicable period, Seller shall furnish to Buyer (a) the quarterly convention statements of the Subsidiaries for all interim quarterly periods subsequent to September 30, 1995, which shall have been prepared on a basis consistent with the Convention Statements and, with respect to the financial statements included therein, in accordance with Statutory Accounting Principles, (b) the quarterly financial statements of the Company and Ridge Re for all quarterly periods subsequent to September 30, 1995, which shall have been prepared in accordance with generally accepted accounting principles and on a basis consistent with the Company GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be, subject to normal year-end adjustments and the absence of footnote disclosure, (c) the consolidated financial statements for the Company and Ridge Re for the year ended December 31, 1995, which shall have been prepared in accordance with generally accepted accounting principles and on a basis consistent with the Company GAAP Financial Statements and the Ridge Re GAAP Financial Statements, as the case may be, and (d) (to the extent ordinarily prepared) all monthly financial statements of the Company, the Subsidiaries and Ridge Re (for months subsequent to June 1995), which shall have been prepared in a manner consistent with past practice.

6.3 Certain Prohibited Transactions. Parent and Seller agree to cause the Company and each Subsidiary not to, without the prior written approval of Buyer or except as expressly contemplated by this Agreement:

(a) terminate, cancel or amend any insurance coverage maintained by the Company or any of its Subsidiaries with respect to any material assets of the Company or any Subsidiary which is not replaced by an adequate amount of insurance coverage or is not deemed unnecessary in the reasonable judgment of the Company;

(b) settle any pending or threatened Action relating to an insurance claim in an amount in excess of $5,000,000 above the policy limit relating to such

claim or settle any other pending or threatened Action in an amount in excess of $1,000,000; or

(c) take any action which causes any representation or warranty (other than Section 4.7(a)) of Parent or Seller in this Agreement to be or become untrue at Closing or results in a material breach of any covenant made by Parent or Seller in this Agreement.

6.4 Investigation by Buyer. Parent and Seller shall, and shall use their reasonable efforts to cause the Company and the Subsidiaries to, allow Buyer during regular business hours through Buyer's employees, agents and representatives, to make such investigation of the business, properties, books and records of the Company and the Subsidiaries, and to conduct such examination of the condition of the Company and the Subsidiaries, as Buyer reasonably deems necessary or advisable to familiarize itself with such business, properties, books, records, condition and other matters, and to verify the representations and warranties of Seller hereunder; provided, however, that any information obtained from Seller or the Company shall be deemed to be Evaluation Material for purposes of the Confidentiality Agreement dated August 3, 1995, between Seller and Kohlberg Kravis Roberts Co., L.P. (the "Confidentiality Agreement") and shall be subject to the Confidentiality Agreement.

6.5 Consents. (a) As soon as practicable after execution and delivery of this Agreement, Buyer and Seller shall make all filings required under the HSR Act. Buyer and Seller will each furnish all information as may be required by any other state regulatory agency properly asserting jurisdiction or by the Federal Trade Commission and the United States Department of Justice under the HSR Act in order that the requisite approvals for the purchase and sale of the Stock pursuant hereto, and the transactions contemplated hereby, be obtained or to cause any applicable waiting periods to expire.

(b) Buyer shall use its best efforts to file Form A change of control applications with the applicable state insurance regulators referred to in Schedule 4.11 within 45 days from the date hereof. Buyer will use its reasonable efforts to obtain insurance regulatory approvals as soon as possible following the Form A change of control filings. Parent and Seller shall cooperate with Buyer to obtain such approvals.

(c) Seller and Buyer will, as soon as practicable, commence to take all other action required to obtain as promptly as practicable all necessary consents, approvals, authorizations and agreements of, and to give all notices and make all other filings with, any third parties, including governmental authorities, necessary to authorize, approve or permit the consummation of the transactions contemplated hereby and by the Ancillary Agreements, including all consents, approvals and waivers referred to in Sections 7.4 and 8.2 hereof, and Buyer, Parent and Seller shall cooperate with each other with respect thereto.

(d) Notwithstanding the foregoing, however, none of Parent, Seller, Buyer, the Company or the Subsidiaries shall be required to agree to any limitations, requirements or conditions of, any third party including, but not limited to, any insurance regulatory body, or make any payment to any party including the Company or any Subsidiary in order to obtain consents referred to in Sections 7.4 and 8.2. Parent and Seller shall be entitled to have a representative or representatives present at all meetings that may be held by Buyer with insurance regulators.

6.6 Notification of Certain Matters. Parent and Seller, to the extent within the actual knowledge of an officer of Parent or Seller listed on Schedule 1.1B, shall give prompt notice to Buyer, and Buyer, to the extent within the knowledge of Buyer, shall give prompt notice to Seller, of (i) the occurrence, or failure to occur, of any event which occurrence or failure would be likely to cause any representation or warranty contained in this Agreement to be untrue or inaccurate in any material respect any time from the date hereof to the Closing Date, (ii) any material failure of Parent, Seller or Buyer, as the case may be, to comply with or satisfy any covenant, condition or agreement to be complied with or satisfied by it hereunder (and each party shall use all reasonable efforts to remedy such failure), (iii) any notice or other

communication from any Person alleging that the consent of such Person is or may be required in connection with the transactions contemplated by this Agreement and the Ancillary Agreements, (iv) any notice or other communication from any governmental or regulatory agency or authority in connection with the transactions contemplated by this Agreement and the Ancillary Agreements, (v) any Actions that, if pending or threatened on the date hereof, would have been required to have been disclosed pursuant to Section 4.13 and (vi) any Actions that relate to the consummation of the transactions contemplated by this Agreement and the Ancillary Agreements.

6.7 No Solicitations. (a) Parent, Seller and each of their respective Affiliates, including the Company and the Subsidiaries, will not, directly or indirectly, solicit any inquiries or proposals or enter into or continue any discussions, negotiations, understandings, arrangements or agreements relating to the sale or exchange of any Stock, the merger or amalgamation of the Company or any of its Subsidiaries with, or the direct or indirect disposition of a significant amount of the Company's assets or any Subsidiary's assets or business to any Person other than Buyer or its Affiliates or provide any assistance or any information to or otherwise cooperate with any Person in connection with any such inquiry, proposal or transaction (except that the Company may direct inquiries to Buyer, which shall not disclose confidential information about the Company or any of its Subsidiaries in connection with responding to such inquiries). In the event that Parent, Seller or any of their Affiliates, including the Company and the Subsidiaries receives a solicited or unsolicited inquiry, proposal or offer for such a transaction or obtains information that such an offer is likely to be made, Parent and Seller will provide Buyer with notice thereof as soon as practical after receipt thereof, including the identity of the prospective purchaser or soliciting party. Buyer agrees that to the extent it engages in any discussions regarding the Company or the Subsidiaries with potential purchasers of the capital stock or businesses thereof, Buyer shall not include officers or employees of the Company or the Subsidiaries in such discussions.

(b) The parties acknowledge that there may be no adequate remedy at law for a breach of Section 6.7(a) and that money damages may not be an adequate remedy for breach of such Section. Therefore, the parties agree that Buyer shall have the right, in addition to any other rights it may have, to injunctive relief and specific performance of Section 6.7(a) in the event of any breach of such Section. The remedy set forth in the preceding two sentences is cumulative and shall in no way limit any other remedy any party hereto has at law, in equity or pursuant hereto.

6.8 Cooperation; Accounting and Other Matters. Seller shall, and Seller shall use its reasonable efforts to cause the Company to, cooperate with Buyer in respect of any proposed public offering or private placement of securities, and arrangements of other financing by Buyer, the proceeds of which are to be used to finance a portion of the purchase of the Stock by Buyer (provided, however, that Seller shall not be obligated to participate in such financing or the marketing thereof and shall not be obligated to be a party to any underwriting, private placement or other agreement with respect thereto), and shall, without limitation of the foregoing, cause such Company financial statements to be prepared as may be required by the rules and regulations of the Securities and Exchange Commission promulgated under the Securities Act.

6.9 Investment Portfolio. (a) Parent and Seller shall cause the Company and the Subsidiaries to manage the investment portfolio for the Company and the Subsidiaries in accordance with the Investment Policy.

(b) Five days prior to the Closing Date, Parent and Seller shall cause the Company to deliver to Buyer a list of all Investments in the investment portfolio for the Company and the Subsidiaries as of such date.

6.10 Reinsurance Agreements. Seller shall cause the Company and each Subsidiary not to, without the prior written approval of Buyer (which approval shall not be unreasonably withheld), except in the ordinary course of business consistent with past practice (i) amend any reinsurance or retrocession agreement, (ii) enter into or commit to enter into any loss portfolio transfer or other similar transaction, agreement or arrangement or series of related

transactions, agreements or arrangements involving any ceded reinsurance of the Company or any Subsidiary, (iii) enter into or commit to enter into any reinsurance or retrocession contract or treaty except to replace, renew or extend existing reinsurance and retrocession agreements and treaties on terms which are not different in any material respect from the terms of the agreement or treaty being replaced, renewed or extended, as the case may be, or (iv) commute or terminate any contract of reinsurance, provided that Seller shall cause the Company and each Subsidiary not to commute or terminate any such contract which at the time of commutation or termination is legally carried on the books of the Company and the Subsidiaries in an amount of $5,000,000 or more. All reinsurance or retrocession agreements or treaties permitted by this Section shall not have a change of control or similar provision which would require the Company or any Subsidiary to obtain a consent to consummate the transactions contemplated hereby (unless such provisions shall have been waived prior to Closing).

6.11 Dividends. Seller and Parent shall cause the Company not to (i) declare, set aside or pay any dividends or distributions (whether in cash, stock or property) in respect of any capital stock of the Company, (ii) make any other payment or distribution to Parent, Seller or any Affiliate of Parent (excluding the Company and the Subsidiaries, but including Talegen and its subsidiaries), or (iii) redeem, purchase or otherwise acquire any of the capital stock of the Company or any Subsidiary, except for (A) payments permitted under the Tax Agreement, (B) payments under the contracts, agreements or arrangements referred to in Schedule 4.23 or described in clauses (i), (ii) or (iii) of Section 4.23(b) and (C) dividends from TRG in an amount not to exceed the TRG Dividend Replacement Amount (as defined in the Talegen Agreement).

6.12 Seller Notes. The Company and the Subsidiaries shall not dispose of the Seller Notes to a Person other than a Subsidiary, except that the Company and the Subsidiaries may dispose of all or a portion of the Seller Notes prior to Closing to a Person other than a Subsidiary if upon such disposition Seller shall pay to the Company the excess of (i) the aggregate principal amount of the Seller Notes so disposed plus accrued but unpaid interest through the date of such disposition over (ii) the Third Party Amount. To the extent not already disposed of, immediately prior to Closing, Seller shall repay the outstanding principal amounts and any accrued but unpaid interest thereon under the Seller Notes issued by it and held at that time by the Company or any Subsidiary.

6.13 Leesburg Training Facility. The Company and the Subsidiaries shall not dispose of any of their interests in the ground lease agreement among Parent and certain of the Subsidiaries or the lease agreement among Seller and such Subsidiaries, each dated as of December 1, 1985 and each relating to approximately six acres of land in Loudon County, Virginia and a training facility located thereon or their fee interests in such facility (the "Leesburg Training Facility"), to a Person other than a Subsidiary, except that the Company and the Subsidiaries may dispose of their interests (in whole or in part) in the Leesburg Training Facility prior to Closing to a Person other than a Subsidiary if upon such disposition Seller pays to the Company the excess of (i) the greater of $6,200,000 and the statutory carrying value of the Leesburg Training Facility as of December 31, 1995 over (ii) the Third Party Amount. If no Third Party Amount has been received by the Company or any Subsidiary prior to the Closing, immediately prior to Closing, Parent and Seller agree to cause an amount equal to the greater of (i) the statutory carrying value of the Leesburg Training Facility as of December 31, 1995 and (ii) $6,200,000, to be contributed to such Subsidiaries, allocated to such Subsidiaries in accordance with Schedule 6.13 (such contributed amount, the "Leesburg Training Facility Amount"). At Closing, the Company shall cause to be transferred to Seller or an Affiliate of Seller any remaining interests the Company or any of the Subsidiaries has in the Leesburg Training Facility. Upon any transfer of the Leesburg Training Facility in accordance with this Section 6.13, the Company and the Subsidiaries shall have no further rights or obligations relating to the Leesburg Training Facility.

6.14 Cessions to Ridge Re. The Insurance Subsidiaries shall make cessions to Ridge Re under the Ridge Re Treaty in the ordinary course of business, which

cessions shall be actuarially supported.

6.15 Restated Certificate of Incorporation. Prior to the Closing Date, Buyer shall file the Restated Certificate of Incorporation with the Secretary of State of the State of Delaware.

6.16 Certain Admitted Assets. Parent and Seller shall indemnify, guaranty or otherwise post credit support to the extent that as of the Closing Date the Insurance Subsidiaries shall not have received credit for statutory purposes for the Crostex/Camfex Purchase Money Notes in an amount equal to at least $35 million. Such indemnity, guaranty or credit support shall continue until final maturity of such notes but only in the amount provided in the preceding sentence.

6.17 Intercompany Accounts. (a) Except as provided in Sections 6.12 and 6.13, all intercompany accounts (other than those relating to Taxes and those under or relating to reinsurance contracts and arrangements) between the Company and any Subsidiary, on the one hand, and Parent and any of its Affiliates (other than the Company and its Subsidiaries), on the other hand, as of the Closing shall be settled at fair value (irrespective of the terms of payment of such intercompany accounts) in the manner provided in this Section. At least five business days prior to the Closing, Seller shall prepare and deliver to Buyer a statement setting out in reasonable detail the calculation of all such intercompany account balances based upon the latest available financial information as of such date and, to the extent reasonably requested by Buyer, provide Buyer with supporting documentation to verify the underlying intercompany charges and transactions. All such intercompany account balances shall be paid in full in cash prior to the Closing. All intercompany reinsurance agreements shall remain in effect and shall be settled in the ordinary course of business. All intercompany accounts relating to Taxes will be governed by the Tax Agreement.

(b) As promptly as practicable, but no later than 60 days after the Closing Date, Seller shall cause to be prepared and delivered to Buyer a statement setting out in reasonable detail the calculation of such intercompany account balances as of the Closing Date (giving effect to any settlement under subsection (a) and any other payments). Buyer and Seller shall cooperate in the preparation of any such calculation including the provision of supporting documentation to verify the underlying intercompany charges, transactions and payments. If Buyer disagrees with Seller's calculation of such intercompany balances Buyer may, within 30 days after delivery of such statement, deliver a notice to Seller disagreeing with such calculation and setting forth Buyer's calculation of such amount. If Buyer and Seller are unable to resolve such disagreement within 30 days thereafter, such disagreement shall be resolved by independent accountants of nationally recognized standing reasonably satisfactory to Buyer and Seller. The net amount of any such intercompany balance shall be paid in cash promptly thereafter, together with interest thereon from and including the Closing Date to but excluding the date of payment at a rate equal to 5% per annum. Such interest shall be payable at the same time as the payable to which it relates and shall be calculated daily on the basis of a year of 365 days and the actual number of days elapsed. All amounts owing to Buyer under this Section 6.17 shall be paid directly to the Company.

6.18 Financing. Buyer shall use its reasonable efforts to obtain financing that will satisfy the condition in Section 8.9 hereof.

6.19 Letter Agreement. The Letter Agreement substantially in the form of Exhibit C shall be executed and delivered at the Closing.

## ARTICLE VII

## CONDITIONS TO OBLIGATIONS OF PARENT AND SELLER

The obligations of Parent and Seller to consummate the transactions contemplated hereby on the Closing Date are subject, in the discretion of Parent and Seller, to the satisfaction or waiver, on or prior to the Closing Date, of each of the following conditions:

7.1  Representations, Warranties and Covenants.  All representations and warranties of Buyer contained in this Agreement and the Ancillary Documents to which Buyer is a party shall be true and correct in all material respects (except that such representations and warranties specifically qualified by materiality shall be read for purposes of this Section so as not to require an additional degree of materiality) as of the date of this Agreement and (except to the extent such representations and warranties speak as of an earlier date) as of the Closing Date as if such representations and warranties were made on and as of the Closing Date, any breaches of such representations and warranties as of the Closing Date (determined for purposes of this clause without regard to any materiality qualifications in such representations and warranties) taken together shall not have a Material Adverse Effect on Buyer, the Company and the Subsidiaries, taken as a whole (assuming that the Closing shall have occurred), or on Parent or Seller, and Buyer shall have performed in all material respects all agreements and covenants required hereby to be performed by it prior to or at the Closing Date.  There shall be delivered to Seller a certificate (signed by the President of Buyer) to the foregoing effect.

7.2  HSR Act.  The applicable waiting period, including any extension thereof, under the HSR Act shall have expired.

7.3  No Governmental or Other Proceeding; Illegality.  (a)  No Action shall be pending or threatened which seeks to enjoin, restrain or prohibit the consummation of the transactions contemplated by this Agreement (including, without limitation, the execution, delivery and performance of any Ancillary Agreement by the parties thereto) which either Parent or Seller reasonably believes presents a material risk that it or its Affiliates would suffer substantial monetary damage (whether or not indemnified under this Agreement).

(b)  There shall not be in effect any statute, rule, regulation or order of any court, governmental or regulatory body which prohibits or makes illegal the transactions contemplated hereby, including, without limitation, the execution or delivery of any of the Ancillary Agreements or the performance of any of the Guarantees, the Tax Agreement or the Ridge Re Treaty.

7.4  Consents.  All consents, approvals and waivers from governmental authorities and other parties necessary to permit Seller and Parent to consummate the transactions contemplated hereby shall have been obtained, unless the failure to obtain any such consent, approval or waiver would not have a Material Adverse Effect on Seller or Parent, as the case may be, provided, however, that no such consent, approval or waiver shall contain any limitations, requirements or conditions on Parent or Seller or require Parent or Seller to make any payment to any party including the Company or any Subsidiary.

7.5  Opinion of Counsel.  Buyer shall have delivered to Seller an opinion of Simpson Thacher & Bartlett, substantially in the form of Exhibit D-1, and an opinion of King & Spalding, special tax counsel to Buyer, substantially in the form of Exhibit D-2.

7.6  Certificates.  Buyer will furnish Seller with such certificates of its officers, directors and others to evidence compliance with the conditions set forth in this Article VII as may be reasonably requested by Seller.

7.7  Corporate Documents.  Seller shall have received from Buyer resolutions adopted by the Board of Directors of Buyer approving this Agreement and the Tax Agreement and the transactions contemplated hereby and thereby, certified by the corporate secretary or assistant secretary of Buyer.

7.8  Talegen Closing.  Talegen Acquisition shall have simultaneously purchased all of the outstanding shares of Talegen's capital stock pursuant to the Talegen Agreement.

7.9  Reated Certificate of Incorporation.  The Restated Certificate of Incorporation shall have been duly filed with the Secretary of State of the State of Delaware.

7.10 Solvency Matters. Buyer shall have provided to Seller, any solvency letters or similar opinions or certificates relating to the solvency and adequate capitalization of Buyer or the Company and/or the ability of Buyer or the Company to pay its debts that are given to any banks or other lenders in connection with the acquisition of the Stock at the same time as such letters, opinions or certificates are provided to such banks or other lenders.

7.11 Capitalization. Buyer shall have received no less than $50,000,000 in equity and the amount of indebtedness for borrowed money of Buyer shall be no more than $110,000,000.

7.12 Company Certificates. Seller shall have received (i) a certificate signed by each of the persons listed on Schedule 1.1C dated as of the date of this Agreement, and (ii) a certificate signed by each of such persons dated as of the Closing Date, in each case substantially in the form of Exhibit E.

7.13 Subsidiary Releases. All of the domestic U.S. Subsidiaries included in the consolidated federal income tax return of Parent which are Subsidiaries as of Closing shall have executed and delivered to Parent and Seller the releases of any and all obligations under existing tax sharing agreements substantially in the form of Exhibit F.

## ARTICLE VIII

## CONDITIONS TO OBLIGATIONS OF BUYER

The obligations of Buyer to consummate the transactions contemplated hereby are subject, in the discretion of Buyer, to the satisfaction or waiver, on or prior to the Closing Date, of each of the following conditions:

8.1 Representations, Warranties and Covenants. All representations and warranties of Parent and Seller contained in this Agreement and the Ancillary Agreements to which Parent or Seller is a party shall be true and correct in all material respects (except that such representations and warranties specifically qualified by materiality shall be read for purposes of this Section so as not to require an additional degree of materiality) as of the date of this Agreement and (except to the extent such representations and warranties speak as of an earlier date) as of the Closing Date as if such representations and warranties were made on and as of the Closing Date, any breaches of such representations and warranties as of the Closing Date (determined for purposes of this clause without regard to any materiality qualifications in such representations and warranties) taken together shall not have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, and Parent and Seller shall have performed in all material respects all agreements and covenants (other than those contained in Section 6.3(c) and clauses (i), (ii) and (v) of Section 6.6) required hereby to be performed by them, respectively, prior to or at the Closing Date. There shall be delivered to Buyer a certificate of each of Parent and Seller (signed by an Executive Vice President of Parent and the President of Seller) to the foregoing effect.

8.2 Consents. All consents, approvals and waivers (a) referred to in clauses (i) and (ii) of Section 4.11 or on Schedule 5.8, (b) referred to on Schedule 4.10, (c) under reinsurance and retrocession agreements for the accident year in which the Closing occurs that would be terminable as a result of consummation of the transactions contemplated by this Agreement and the Ancillary Agreements, (d) under all other reinsurance and retrocession agreements that would be terminable as a result of consummation of the transactions contemplated by this Agreement and the Ancillary Agreements and (e) under the reinsurance agreement described in clause (e) of Section 8.2 of the Talegen Agreement shall have been obtained in form and substance satisfactory to Buyer, acting reasonably, and shall be in full force and effect, except, in the case of consents, approvals and waivers referred to in clauses (b), (c) and (d), consents, approvals or waivers the failure of which to obtain would not, individually or in the aggregate, result in a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole, provided, however, that in the case of clauses (a), (b), (c), (d) and (e) no

such consent, approval or waiver shall contain any limitations, requirements or conditions on Buyer, the Company or a Subsidiary or require Buyer, the Company or a Subsidiary to make any payment to any party including in the case of Buyer, to the Company or, in the case of Buyer or the Company, to any Subsidiary, provided further, that the approval of any intercompany tax agreements referred to in either Section 4.11(i) or (ii) for a period after Closing shall not be a condition to the obligations of Buyer hereunder, and provided still further, that with respect to any intercompany tax agreement among the Company and the Subsidiaries for the period January 1, 1995 through Closing, the obligations of Buyer hereunder shall be conditioned only on the approval of an agreement that is reasonably consistent with those provisions of the Tax Agreement that provide for the amount and time for payments attributable to Taxes.

8.3 HSR Act. The applicable waiting period, including any extension thereof, under the HSR Act shall have expired.

8.4 No Governmental or Other Proceeding; Illegality. (a) No Action shall be pending or threatened which seeks to enjoin, restrain or prohibit the consummation of the transactions contemplated by this Agreement (including, without limitation, the execution, delivery and performance of any Ancillary Agreement by the parties thereto) or to impose limitations on the ability of Buyer to exercise full rights of ownership of the Stock or to require the divestiture by Buyer of the Stock or by the Company, Buyer or any of their Affiliates of any assets or businesses, which Buyer reasonably believes presents a material risk that it or its Affiliates (including the Company and the Subsidiaries after the Closing Date) would not realize substantially all of the benefits of the transactions contemplated by this Agreement or would suffer substantial monetary damages (whether or not indemnified under this Agreement).

(b) There shall not be in effect any statute, rule, regulation or order of any court, governmental or regulatory body which prohibits or makes illegal the transactions contemplated hereby, including, without limitation, the execution or delivery of any of the Ancillary Agreements or the performance of any of the Guarantees, the Tax Agreement or the Ridge Re Treaty.

8.5 Opinion of Counsel. Seller shall have delivered to Buyer an opinion of Skadden, Arps, Slate, Meagher & Flom, substantially in the form of Exhibit G-1, an opinion of Richard S. Paul, Senior Vice President and General Counsel of Seller, substantially in the form of Exhibit G-2, an opinion of Bruce Shulin, General Counsel of IIC, substantially in the form of Exhibit G-3, an opinion of Richard N. Frasch, General Counsel of the Company, substantially in the form of Exhibit G-4, and an opinion of LeBoeuf, Lamb, Greene & MacRae, special tax counsel to Parent and Seller, substantially in the form of Exhibit G-5.

8.6 Certificates. Parent and Seller shall furnish Buyer with such certificates of the respective officers of Parent and Seller and others to evidence compliance with the conditions set forth in this Article VIII as may be reasonably requested by Buyer.

8.7 Corporate Documents. Buyer shall have received from Parent and Seller resolutions adopted by the respective boards of directors of Parent and Seller approving this Agreement and the other Ancillary Agreements to which Parent or Seller is or will be a party and the transactions contemplated hereby and thereby, certified by the corporate secretary or assistant secretary of Parent and Seller, as applicable.

8.8 Talegen Closing. Talegen Acquisition shall have simultaneously purchased all of the outstanding shares of Talegen's capital stock pursuant to the Talegen Agreement.

8.9 Financing. Buyer shall have obtained proceeds from financing sources on terms and conditions consistent with the senior bank commitment letter provided by Buyer to Seller prior to the date hereof, and otherwise reasonably satisfactory to Buyer.

8.10 No Material Adverse Effect. Since June 30, 1995, there shall not have

occurred any event, change or development (including, without limitation, the suspension, revocation or other termination of any Permit) which individually or in the aggregate, has had or is reasonably likely to have a Material Adverse Effect on the Company and the Subsidiaries, taken as a whole.

8.11 Resignation of Officers and Directors. All Persons who are directors and/or officers of the Company and/or any of the Subsidiaries whose principal employment is as an officer and/or employee of Seller and/or Parent, shall have resigned such directorships and/or such offices.

8.12 Transfer Taxes. Seller shall have caused all appropriate stock transfer tax stamps to be affixed to the certificate or certificates representing the Stock.

8.13 Seller Notes. Seller shall have made the payments contemplated by Section 6.12 and repaid all amounts outstanding under any Seller Notes that are still held by the Company and any Subsidiary together with any accrued but unpaid interest thereon.

8.14 Leesburg Training Facility Amount. The Leesburg Training Facility Amount shall have been paid, as provided in Section 6.13.

8.15 Guarantees. Parent shall have executed and delivered to Buyer a guarantee for the benefit of IIC substantially in the form of Exhibit H and Parent and Seller shall have executed and delivered to Buyer a guarantee for the benefit of IIC substantially in the form of Exhibit I.

8.16 Management Investment. Members of the management of the Company and the Subsidiaries designated by Buyer shall have invested in the capital stock of Buyer on terms substantially consistent with the agreements in principle delivered to Seller prior to the date hereof or otherwise satisfactory to Buyer.

## ARTICLE IX

## ACTIONS BY PARENT, SELLER, AND BUYER AFTER THE CLOSING

9.1 Books and Records. Parent, Seller and Buyer agree that so long as any books, records and files relating to the business, properties, assets or operations of the Company or the Subsidiaries, to the extent that they pertain to the operations of the Company or the Subsidiaries prior to the Closing Date, remain in existence and available, each party (at its expense) shall have the right to inspect and to make copies of the same at any time during normal business hours for any proper purpose. Parent and Seller further agree that, to the extent such records have not otherwise been delivered to the Company or Buyer, Parent and Seller will not destroy or dispose of any material books, records or files relating to the investment portfolio existing as of the Closing Date without first offering to provide such books, records or files to Buyer and that, in any event, Buyer shall have the right to inspect and to make copies of the same at any time during normal business hours for any proper purpose, to the extent reasonably requested by Buyer.

9.2 Covenants Regarding the Securities. In connection with any sale, transfer or other disposition of all or any part of the Securities under an exemption from registration under the Securities Act, if requested by Buyer, Seller (or Parent, if such Securities are held by Parent) will deliver to Buyer an opinion of counsel (which may be the General Counsel of Parent or, if such Securities are held by Seller, of Seller), reasonably satisfactory in form and substance to Buyer, that such exemption is available; provided, however, that in case of any sale or other transfer of Securities to any Person who is a qualified institutional buyer as defined in Rule 144A under the Securities Act, no opinion of counsel shall be required if Seller (or Parent, if such Securities are held by Parent) provides to Buyer an officer's certificate to the effect that such Person is a qualified institutional buyer as defined in Rule 144A under the Securities Act. Parent and Seller hereby agree and acknowledge that upon original issuance thereof, and until such time as the same is no longer required under the applicable requirements of the Securities Act, the Securities (and all securities issued in exchange therefor

or substitution thereof) shall bear, until such restrictions are no longer applicable, the following legend:

"THE SECURITIES REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 ACT"). THEY MAY NOT BE SOLD OR TRANSFERRED EXCEPT IN COMPLIANCE WITH THE REGISTRATION PROVISIONS OF THE 1933 ACT AND ANY APPLICABLE STATE BLUE SKY LAWS OR SECURITY LAWS OR PURSUANT TO AN AVAILABLE EXEMPTION FROM SUCH PROVISIONS."

Parent and Seller further agree and acknowledge that any Class 1 Stock acquired in accordance with Section 11.3 shall also bear (until such time as such restrictions are no longer applicable) the following legend:

"THE SECURITIES REPRESENTED BY THIS CERTIFICATE ARE SUBJECT TO A RIGHT OF FIRST REFUSAL AND CERTAIN OTHER RESTRICTIONS ON TRANSFER AS SET FORTH IN THAT CERTAIN STOCKHOLDERS AGREEMENT, BETWEEN TRG ACQUISITION CORPORATION AND XEROX FINANCIAL SERVICES, INC., A COPY OF WHICH MAY BE OBTAINED FROM THE SECRETARY OF TRG ACQUISITION CORPORATION."

9.3 Crostex/Camfex Purchase Money Notes. Seller and Parent shall indemnify, guaranty or otherwise post credit support pursuant to the covenant set forth in Section 6.16 from and after the Closing.

9.4 Certain Employee Benefit Matters. (a) Parent and its Affiliates (other than the Company, the Subsidiaries, Talegen and its subsidiaries) shall retain all liabilities and obligations under the employee stock ownership plan ("ESOP") in which employees of the Company and the Subsidiaries participated prior to January 1, 1993. All awards made to such participants under the ESOP shall fully vest as of the Closing Date.

(b) Parent and its Affiliates (other than the Company, the Subsidiaries, Talegen and its subsidiaries) shall retain all liabilities and obligations under the Long Term Incentive Program attached as Attachment A and the Stock Option Agreement attached as Exhibit A to the Employment Agreement among Joseph W. Brown, Jr., Parent and the Company and the five related agreements with management of the Company or TRG (collectively, the "Long Term Incentive Program") for the benefit of the participants listed on Schedule 9.4. All payments due to such participants under the Long Term Incentive Program shall be made at Closing.

(c) All payments due, at or before the Closing, under the Senior Management Group Compensation Plan of the Company and IIC, any related agreements thereto, the Plan Termination Agreement and General Release for the Senior Management Group, the Plan Termination Agreement and General Release for Banded Associates, the TRG Senior Management Long Term Incentive Compensation Plan, the IIC Annual Compensation Plan for Banded Associates, the IIC Annual Compensation Plan for the Senior Management Group and any related termination agreements (collectively, the "TRG Incentive Plans") shall be made at or prior to the Closing. After the Closing, Parent and its Affiliates shall retain all remaining liabilities and obligations arising under the TRG Incentive Plans.

9.5 Transfer Taxes. Seller shall pay, or cause to be paid, all stock transfer and other transfer taxes required to be paid in connection with the sale and delivery to Buyer of the Stock.

9.6 Ridge Re. On and after the Closing Date, Parent and Seller shall cause Ridge Re to refrain from (i) entering into any reinsurance or retrocession agreement or treaty and (ii) engaging in any business other than in connection with the Ridge Re Treaty and the other treaties referenced in the first sentence of Section 4.9(c) of the Talegen Agreement as in effect on the date hereof, provided that the obligations contained in this Section 9.6 shall terminate upon consummation of the sale of Ridge Re to a Qualified Transferee.

9.7 Further Assurances. On and after the Closing Date, Parent, Seller, the Company and Buyer will take all appropriate action and execute all documents, instruments or conveyances of any kind which may be reasonably necessary or advisable to carry out any of the provisions hereof, including without limitation, putting Buyer in possession and operating control of the business

of the Company.

ARTICLE X

INDEMNIFICATION

10.1 Survival of Representations and Warranties. Buyer has the right to rely fully upon the representations, warranties, covenants and agreements of Parent and Seller contained in this Agreement and the Ancillary Agreements. Parent and Seller have the right to rely fully upon the representations, warranties, covenants and agreements of Buyer contained in this Agreement and the Ancillary Agreements. All such representations and warranties (including the Schedules hereto and the certificates delivered in accordance with Sections 7.1 and 8.1 hereof, insofar as the Schedules and such certificates relate to such representations and warranties) shall be deemed to be repeated at Closing for purposes of this Article X and, except as set forth in the last sentence of this Section, shall survive the execution and delivery hereof and the Closing, and thereafter (i) in the case of the representations and warranties contained in Sections 4.1, 4.2, 4.3, 4.4, 4.5, 4.6 and 4.18 hereof, such representations and warranties shall survive without limitation as to time, (ii) in the case of the representations and warranties contained in Sections 4.21, 4.24 and 4.28 hereof, such representations and warranties shall survive until 90 days after the expiration of the applicable statute of limitations with respect to the subject matter thereof and (iii) in the case of all other representations and warranties, such representations and warranties shall expire on the date two years following the Closing Date; provided, however, that any representation or warranty shall survive the time it would otherwise terminate pursuant to this Section to the extent that notice of a breach thereof giving rise to a right of indemnification shall have been given by a party hereto in accordance with Section 10.3 hereof prior to such time. All of the covenants and agreements of the parties contained in this Agreement and the Ancillary Agreements to be performed on or after the date of this Agreement shall survive the Closing without limitation as to time. Notwithstanding the foregoing, none of the following representations and warranties (including the Schedules hereto and the certificates delivered in accordance with Sections 7.1 and 8.1 hereof, insofar as the Schedules and such certificates relate to such representations and warranties) shall survive the Closing: (i) representations and warranties contained in Sections 4.16, 4.21(e), 4.21(h) and Article V; and (ii) representations and warranties contained in any Section of Article IV and which relate to Excluded Activities.

10.2 Indemnification. (a) Parent and Seller shall jointly and severally defend, indemnify and hold harmless Buyer, the Company and their Affiliates and each director and officer of such Persons against any loss, damage, claim, liability, judgment or settlement of any nature or kind, including all costs and expenses relating thereto, including without limitation, interest, penalties and reasonable attorneys' fees (collectively "Damages"), arising out of, resulting from or relating to:

(i) subject to Section 10.1, the breach of any representation or warranty of Parent or Seller contained in this Agreement (other than in Section 4.18), any Ancillary Agreement or any certificate delivered pursuant hereto or thereto; provided, however, that such Persons shall be entitled to indemnification hereunder only when the aggregate of all such Damages exceeds $10,000,000 (in which event such Persons shall be entitled to indemnification for all such Damages); provided, further, that Seller shall not be liable under this clause (i) for an amount of Damages in excess of (x) $150,000,000 less an amount equal to Transaction Expenses plus (y) amounts received in cash dividends on, and in respect of cash redemptions of, the Class 2 Stock;

(ii) the breach of any covenant or agreement (whether to be performed prior to or after Closing) of Parent or Seller contained in this Agreement, any Ancillary Agreement or any certificate delivered pursuant hereto or thereto;

(iii) any facts, circumstances, conditions, events or actions existing or occurring at any time with respect to Constitution Re, First Quadrant and Viking (as such terms are defined in the Talegen Agreement) and any subsidiary

of any of the foregoing (other than liabilities related to the business represented by the First Quadrant Asset Sale (as defined in the Talegen Agreement));

(iv) any Action brought by a security holder or creditor of Seller or Parent in their capacity as such;

(v) long term incentive payments (including payments arising out of the sale of the Company or the Excluded Business) payable to the Persons listed on Schedule 10.2;

(vi) the breach of the representations and warranties contained in Section 4.18; and

(vii) any facts, circumstances, conditions, events or actions existing or occurring after the Closing Date with respect to the Leesburg Training Facility.

The foregoing provisions of this Section 10.2(a) shall not apply with respect to any Damages arising out of (and no indemnification hereunder shall be available with respect to) any (i) breach of any representation or warranty of Parent or Seller that is terminated as provided in Section 10.1 (subject, however, to the proviso contained in Section 10.1), (ii) breaches of the representations and warranties of Parent and Seller contained in this Agreement and the Ancillary Agreements which would result in the failure of any of the conditions in Section 8.1 to be satisfied if Buyer had actual knowledge of such breaches (or received notice thereof pursuant to Section 6.6) prior to the Closing Date, (iii) breach of any representation or warranty contained in Section 4.21(h), (iv) breach of any representation or warranty to the extent it relates to Excluded Activities, (v) action that breaches Section 6.3(c) to the extent such action relates to Excluded Activities (except if such action is directed by Parent or Seller or, prior to or at the time taken, an officer listed on Schedule 1.1B knew that such action was to be taken), (vi) breach of any covenant to be performed prior to Closing to the extent it relates to Excluded Activities, other than a breach of Section 6.1, 6.3(a), 6.3(b), 6.10 or 6.14, (vii) action that breaches Section 6.2 or Section 6.9 (except in each case if such action is directed by Parent or Seller or, prior to or at the time taken, an officer listed on Schedule 1.1B knew that such action was to be taken) or (viii) underfunding of Company Plans (including fines and penalties assessed by governmental authorities relating thereto).

(b) For purposes of clause (i) of Section 10.2(a), (X) a "Material Adverse Effect" (as such term is used in any representation or warranty contained in Article IV other than the representations and warranties contained in Section 4.7(a)) shall be deemed to have occurred if the aggregate of all Damages related to any such representation or warranty shall exceed $1 and (Y) the representations and warranties contained in Sections 4.7, 4.13 and 4.15(b) shall be read as if such representations and warranties do not include the words "Knowledge of Seller".

(c) The term "Damages" as used in this Article X is not limited to matters asserted by third parties against any Person entitled to be indemnified under this Article X, but includes Damages incurred or sustained by any such Person in the absence of third party claims.

(d) No claim for Damages under this Article X may be asserted or pursued by any former Subsidiary against Parent or Seller, unless, prior to the date that such former Subsidiary shall have ceased to be a "Subsidiary", such former Subsidiary shall have delivered a Notice to Parent or Seller relating to such claim.

10.3 Indemnification Procedures. (a) In the event that any Person shall incur or suffer any Damages in respect of which indemnification may be sought hereunder, such Person (the "Indemnitee") may assert a claim for indemnification by written notice (the "Notice") to the party from whom indemnification is being sought (the "Indemnitor"), stating the amount of Damages, if known, and the nature and basis of such claim. In the case of Damages arising or which may arise by reason of any third-party claim,

promptly after receipt by an Indemnitee of written notice of the assertion or the commencement of any Action with respect to any matter in respect of which indemnification may be sought hereunder, the Indemnitee shall give Notice to the Indemnitor and shall thereafter keep the Indemnitor reasonably informed with respect thereto, provided that failure of the Indemnitee to give the Indemnitor prompt notice as provided herein shall not relieve the Indemnitor of any of its obligations hereunder, except to the extent that the Indemnitor is materially prejudiced by such failure. In case any such Action is brought against any Indemnitee, the Indemnitor shall be entitled to assume the defense thereof, by written notice of its intention to do so to the Indemnitee within 30 days after receipt of the Notice. If the Indemnitor shall assume the defense of such Action, it shall not settle such Action without the prior written consent of the Indemnitee, which consent shall not be unreasonably withheld, provided that an Indemnitee shall not be required to consent to any settlement that (i) does not include as an unconditional term thereof the giving by the claimant or the plaintiff of a release of the Indemnitee from all liability with respect to such Action or (ii) involves the imposition of equitable remedies or the imposition of any material obligations on such Indemnitee other than financial obligations for which such Indemnitee will be indemnified hereunder. As long as the Indemnitor is contesting any such Action in good faith and on a timely basis, the Indemnitee shall not pay or settle any claims brought under such Action. Notwithstanding the assumption by the Indemnitor of the defense of any Action as provided in this Section, the Indemnitee shall be permitted to participate in the defense of such Action and to employ counsel at its own expense; provided, however, that if the defendants in any Action shall include both an Indemnitor and any Indemnitee and such Indemnitee shall have reasonably concluded that counsel selected by Indemnitor has a conflict of interest because of the availability of different or additional defenses to such Indemnitee, such Indemnitee shall have the right to select separate counsel to participate in the defense of such Action on its behalf, at the expense of the Indemnitor; provided that the Indemnitor shall not be obligated to pay the expenses of more than one separate counsel for all Indemnitees, taken together.

(b) If the Indemnitor shall fail to notify the Indemnitee of its desire to assume the defense of any such Action within the prescribed period of time, or shall notify the Indemnitee that it will not assume the defense of any such Action, then the Indemnitee may assume the defense of any such Action, in which event it may do so acting in good faith in such manner as it may deem appropriate, and the Indemnitor shall be bound by any determination made in such Action, provided, however, that the Indemnitee shall not be permitted to settle such action without the consent of the Indemnitor. No such determination or settlement shall affect the right of the Indemnitor to dispute the Indemnitee's claim for indemnification. The Indemnitor shall be permitted to join in the defense of such Action and to employ counsel at its own expense.

(c) Amounts payable by the Indemnitor to the Indemnitee in respect of any Damages for which such party is entitled to indemnification hereunder shall be payable by the Indemnitor as incurred by the Indemnitee.

(d) In the event of any dispute between the parties regarding the applicability of the indemnification provisions of this Agreement, the prevailing party shall be entitled to recover all Damages incurred by such party arising out of, resulting from or relating to such dispute.

10.4 Insurance Proceeds and Tax Limitations. The amount of any Damages or other liability for which indemnification is provided under this Agreement shall be net of any amounts recovered or recoverable by the Indemnitee under insurance policies with respect to such Damages or other liability and shall be (i) increased to take account of any Tax cost incurred (grossed up for such increase) by the Indemnitee arising from the receipt of indemnity payments hereunder (unless such indemnity payment is treated as an adjustment to the purchase price hereunder for tax purposes) and (ii) reduced to take account of any Tax benefit realized by the Indemnitee arising from the incurrence or payment of any such Damages or other liability. Such Tax cost or Tax benefit, as the case may be, shall be computed for any year using the Indemnitee's actual tax liability with and without (i) the incurrence or payment of any

Damages or other liability for which indemnification is provided under this Agreement or (ii) the payment of any indemnification payments made pursuant to this Agreement in such year. In the event that the Indemnitee will actually realize a Tax cost or Tax benefit for a year(s) subsequent to the year in which the indemnity payment is made, a payment in respect of such Tax cost or Tax benefit shall be made in such subsequent year(s). Any indemnity payment made pursuant to this Agreement will be treated as an adjustment to the purchase price hereunder for Tax purposes, unless a determination (as defined in Section 1313 of the Code) with respect to the Indemnitee causes any such payment not to constitute an adjustment to the purchase price for United States Federal income tax purposes.

10.5 Tax Indemnification. Notwithstanding anything to the contrary in this Agreement, the rights and obligations of the parties with respect to indemnification for any and all Tax matters (other than with respect to any representations and warranties contained herein relating to Tax matters, except to the extent Buyer is indemnified under the provisions of the Tax Agreement) shall be governed by the Tax Agreement and shall not be subject to this Article X, including any calculation pursuant to clause (i) of Section 10.2(a).

## ARTICLE XI

## MISCELLANEOUS

11.1 Termination. This Agreement may be terminated and the transactions contemplated hereby abandoned:

(a) by mutual consent of the parties; or

(b) by Parent and Seller, on the one hand, or Buyer, on the other hand, on June 17, 1996 if it can be reasonably anticipated that the approvals referred to in Section 4.11(i) cannot be obtained without the applicable regulatory authorities imposing an additional material economic burden on Parent or Seller, on the one hand, or Buyer, the Company and the Subsidiaries, taken as a whole, on the other hand; or

(c) by Parent and Seller, on the one hand, or Buyer, on the other hand, if the conditions to such parties' obligations set forth in Articles VII and VIII, as the case may be, have not been satisfied (or waived by the party entitled to the benefit thereof) on or before August 17, 1996; provided that if the approvals referred to in Section 4.11(i) have not been obtained by August 17, 1996, this Agreement shall not be terminated prior to October 17, 1996 if it can be reasonably anticipated that such approvals can be obtained by October 17, 1996; or

(d) by Parent and Seller, on the one hand, or Buyer, on the other hand, if the Talegen Agreement is terminated in accordance with its terms.

Upon termination of this Agreement pursuant to this Section 11.1, this Agreement shall be void and of no further force and effect (except as provided in the last sentence of this paragraph) and no party shall have any liability to any other party under this Agreement unless such party has (a) willfully failed to have performed its obligations hereunder or (b) knowingly made a misrepresentation of any matter set forth herein. For purposes of the immediately preceding sentence, with respect to obligations of the Company or any Subsidiary to take or refrain from taking any action under this Agreement or obligations of Parent or Seller to cause the Company or any Subsidiary to take or refrain from taking any action under this Agreement, neither Parent nor Seller shall be deemed to have "willfully failed" unless, in each case, such action or failure to act is directed by Parent or Seller or occurs with knowledge of an officer listed on Schedule 1.1B or 1.1C; provided that if such action or failure is (X) not directed by Parent or Seller, (Y) occurs with the knowledge of an officer listed on Schedule 1.1C and (Z) occurs without the knowledge of an officer listed on Schedule 1.1B, Buyer shall recover only its Third Party Expenses and Seller and Parent shall have no further liability under this Agreement. For purposes of the second preceding sentence, neither Parent nor Seller shall be deemed to have "knowingly" made a misrepresentation

unless an officer listed on Schedule 1.1B or 1.1C knows such representation is untrue when made; provided that if a representation is known to be untrue when this Agreement is executed by the parties hereto by an officer listed on Schedule 1.1C but not by an officer listed on Schedule 1.1B, Buyer shall recover only its Third Party Expenses and Seller and Parent shall have no further liability under this Agreement. Notwithstanding a termination of this Agreement, the provisions of Sections 11.2(b) and 11.11, the last sentences of Sections 4.18 and 5.4 and the confidentiality provision of the proviso to Section 6.4 hereof shall continue in full force and effect.

11.2 Confidentiality. (a) Parent and Seller shall assign to the Company at or prior to, and with effect from and after the Closing, all of their respective rights under the Confidentiality Agreement and under any other confidentiality agreements with third Persons relating to the business of the Company or any of the Subsidiaries.

(b) Except as otherwise required by law (including if required by any stock exchange on which any of the securities of any party or their respective Affiliates are listed or by any securities commission or similar regulatory authority having jurisdiction over any such party or any of its Affiliates), Buyer, Seller and Parent shall keep confidential all aspects of the transactions contemplated hereby, including the fact that this Agreement has been executed. Notwithstanding the foregoing or the terms of the Confidentiality Agreement, Buyer and its Affiliates and Seller, Parent and their respective Affiliates may disclose information concerning the transactions contemplated hereby in connection with the financing of such transactions by Buyer, to potential equity investors in Buyer or any of its Affiliates, as necessary to obtain any consents referenced in Section 8.2 and, in the case of Parent, as it, in its sole discretion, deems appropriate in light of its status as a Person with public stockholders. The parties will use their reasonable efforts to make the release to be issued announcing the Closing a mutually acceptable joint release. Before issuing any other press release with respect to the transactions contemplated by this Agreement, the parties will use reasonable efforts to provide each other with a reasonable opportunity to review and comment on any such announcement.

11.3 Parent Option. (a) Parent and/or Seller shall have the right to purchase up to an aggregate of 19.9% of the Class 1 Stock immediately prior to the Closing for a per share purchase price equal to the per share purchase price paid or payable by other stockholders of Buyer on or prior to the Closing Date. Parent and/or Seller shall pay the aggregate purchase price for any shares to be purchased pursuant to this Section in cash, payable by wire transfer in immediately available funds to an account which Buyer shall designate in writing to Parent no less than two business days prior to the Closing Date. To exercise such right, Parent and/or Seller must deliver irrevocable written notice to Buyer within 45 days from the date hereof which indicates the percentage interest (after giving effect to its purchase) of Class 1 Stock that Parent and/or Seller desire to purchase hereunder, but not to exceed an aggregate of 19.9% (which irrevocable notice shall bind Parent, subject to the last sentence of this Section, to make such purchase on the Closing Date). No such notice shall be effective unless Parent and/or Seller concurrently delivers a notice under Section 11.3 of the Talegen Agreement which indicates Parent's and/or Seller's election to purchase the same aggregate percentage interest in the securities covered by the election thereunder that Parent and/or Seller elect to purchase hereunder. Notwithstanding the foregoing, if this Agreement is terminated pursuant to Section 11.1, Parent and Seller shall cease to have the right to purchase Class 1 Stock hereunder, whether or not their rights had been previously exercised, and any notice which shall have been delivered pursuant to this Section shall be void and of no effect.

(b) Any Class 1 Stock purchased by Parent and/or Seller pursuant to paragraph (a) above shall be subject to the terms and conditions set forth in Exhibit J.

11.4 Assignment. Neither this Agreement nor any of the rights or obligations hereunder may be assigned by Parent or Seller without the prior written consent of Buyer, or by Buyer without the prior written consent of Parent or Seller. Subject to the foregoing, this Agreement shall be binding upon and

inure to the benefit of the parties hereto and their respective successors and assigns, and no other Person shall have any right, benefit or obligation hereunder.

11.5 Notices. Unless otherwise provided herein, any notice, request, instruction or other document to be given hereunder by any party to the others shall be in writing and delivered in Person or by courier or facsimile transmission or mailed by certified mail, postage prepaid, return receipt requested (such mailed notice to be effective on the date such receipt is acknowledged), as follows:

If to Parent or Seller:

Xerox Financial Services, Inc.
First Stamford Place
Stamford, Connecticut 06904-2347
Attn: Stuart B. Ross
Chairman & Chief Executive Officer
Fax: (203) 325-6822

and

Xerox Corporation
Long Ridge Road
Stamford, Connecticut 06904
Attn: Richard Paul, Esq.
General Counsel
Fax: (203) 968-3446

With a copy to:

Skadden, Arps, Slate, Meagher & Flom
Third Avenue
New York, New York 10022
Attn: Lou R. Kling, Esq. and
Peter Allan Atkins, Esq.
Fax: (212) 735-2000

If to Buyer:

TRG Acquisition Corporation
c/o Kohlberg Kravis Roberts & Co.
Sand Hill Road, Suite 200
Menlo Park, California 94025
Attn: Saul A. Fox
Fax: (415) 233-6594

With copies to:

Joseph W. Brown
Talegen Holdings, Inc.
Waterfront Center One
Western Avenue, Suite 1000
Seattle, Washington 98101
Fax: (206) 654-2633

Gary I. Horowitz, Esq.
Simpson Thacher & Bartlett
Lexington Avenue
New York, New York 10017
Fax: (212) 455-2502

or to such other place and with such other copies as either party may designate as to itself by written notice to the others.

11.6 Choice of Law. This Agreement shall be construed, interpreted and the rights of the parties determined in accordance with the internal laws of the

State of New York, without regard to the conflict of law principles thereof.

11.7 Entire Agreement; Amendments and Waivers. This Agreement, together with the Ancillary Agreements and the Confidentiality Agreement (except to the extent superseded hereby), constitutes the entire agreement among the parties pertaining to the subject matter hereof and supersedes all prior agreements, understandings, negotiations and discussions, whether oral or written, of the parties. No supplement, modification or waiver of this Agreement (including, without limitation, any Schedule hereto) shall be binding unless executed in writing by all parties. No waiver of any of the provisions of this Agreement shall be deemed or shall constitute a waiver of any other provision hereof (whether or not similar), nor shall such waiver constitute a continuing waiver unless otherwise expressly provided. With respect to breaches of any representation, warranty or covenant contained herein, unless this Agreement shall have been terminated pursuant to Section 11.1, the sole remedy of the parties against each other shall be the indemnification rights set forth in Section 10.2.

11.8 Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

11.9 Invalidity. In the event that any one or more of the provisions contained in this Agreement or in any other instrument referred to herein, shall, for any reason, be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision of this Agreement or any other such instrument.

11.10 Headings. The headings of the Articles and Sections herein are inserted for convenience of reference only and are not intended to be a part of or to affect the meaning or interpretation of this Agreement.

11.11 Expenses. Subject to Section 11.1, Seller and Buyer will each be liable for its own costs and expenses incurred in connection with the negotiation, preparation, execution or performance of this Agreement.

11.12 [Intentionally Omitted].

11.13 Joint and Several. All covenants, representations and warranties made by Parent or Seller in this Agreement shall be deemed to be joint and several covenants, representations and warranties of Parent and Seller.

11.14 No Third Party Beneficiaries. This Agreement shall inure exclusively to the benefit of and be binding upon the parties hereto and their respective successors, assigns, executors and legal representatives. Except as expressly provided in Section 10.2, nothing in this Agreement, express or implied, is intended to confer on any Person other than the parties hereto or their respective successors and assigns, any rights, remedies, obligations or liabilities under or by reason of this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement, or have caused this Agreement to be duly executed on their respective behalf by their respective officers thereunto duly authorized, as of the day and year first above written.

XEROX CORPORATION

Stuart B. Ross
Name: Stuart B. Ross
Title: Executive Vice President

XEROX FINANCIAL SERVICES, INC.

Stuart B. Ross
Name: Stuart B. Ross

Title:  Chairman, President and Chief Executive Officer

TRG ACQUISITION CORPORATION

Saul A. Fox
Name:   Saul A. Fox
Title:  President and Chief Executive Officer

Computation of Net Income Per Common Share

(Dollars in millions, except per-share data; shares in thousands)

I. Primary Net Income (Loss) Per Common Share
- Income (loss) from continuing operations
- Accrued dividends on ESOP preferred stock, net
- Accrued dividends on redeemable preferred stock
- Call premium on redeemable preferred stock
- Adjusted income (loss) from continuing operations
- Discontinued operations
- Change in accounting principles
- Adjusted net income (loss)

- Average common shares outstanding during the period
- Common shares issuable with respect to common stock equivalents for stock options, incentive and exchangeable shares
- Adjusted average shares outstanding for the period

- Primary earnings (loss) per share:
  - Continuing operations
  - Discontinued operations
  - Change in accounting principles
- Primary earnings (loss) per share

II. Fully Diluted Net Income (Loss) Per Common Share
- Income (loss) from continuing operations
- Accrued dividends on ESOP preferred stock, net
- Accrued dividends on redeemable preferred stock
- Call premium on redeemable preferred stock
- ESOP expense adjustment, net of tax
- Interest on convertible debt, net of tax
- Adjusted income (loss) from continuing operations
- Discontinued operations
- Change in accounting principles
- Adjusted net income (loss)

- Average common shares outstanding during the period
- Common shares issuable with respect to:
  - Stock options, incentive and exchangeable shares
  - Convertible debt
  - ESOP preferred stock
- Adjusted average shares outstanding for the period

- Fully diluted earnings (loss) per share:
  - Continuing operations
  - Discontinued operations
  - Change in accounting principles
- Fully diluted earnings (loss) per share *

* Fully diluted discontinued operations net loss per share for the year ended December 31, 1995 is computed by dividing adjusted net loss of $(1,646) by the adjusted average shares outstanding for the period of 110,563 used in the computation of primary net income per common share. This computation is necessitated by the anti-dilutive nature of convertible debt and ESOP preferred stock which would otherwise decrease fully diluted net loss per share for this period.

EXHIBIT 11

| 1995 | 1994 | 1993 | 1992 | 1991 |
|---|---|---|---|---|
| $ 1,174 | $ 794 | $ (193) | $ 562 | $ 436 |
| (42) | (41) | (38) | (39) | (60) |

| | | | | |
|---|---|---|---|---|
| (3) | (12) | (23) | (23) | (23) |
| - | (11) | - | - | - |
| 1,129 | 730 | (254) | 500 | 353 |
| (1,646) | - | 67 | (818) | 18 |
| - | - | - | (764) | - |
| $ (517) | $ 730 | $ (187) | $ (1,082) | $ 371 |
| 107,362 | 105,425 | 100,047 | 94,424 | 92,447 |
| 3,201 | 3,001 | 1,354 | 1,484 | 2,479 |
| 110,563 | 108,426 | 101,401 | 95,908 | 94,926 |
| $ 10.20 | $ 6.73 | $ (2.50) | $ 5.21 | $ 3.72 |
| (14.89) | - | .66 | (8.53) | .19 |
| - | - | - | (7.97) | - |
| $ (4.69) | $ 6.73 | $ (1.84) | $ (11.29) | $ 3.91 |
| $ 1,174 | $ 794 | $ (193) | $ 562 | $ 436 |
| - | - | (38) | (39) | - |
| (3) | (12) | (23) | (23) | (23) |
| - | (11) | - | - | - |
| (9) | (7) | - | - | (25) |
| 4 | 3 | - | - | 1 |
| 1,166 | 767 | (254) | 500 | 389 |
| (1,646) | - | 67 | (818) | 18 |
| - | - | - | (764) | - |
| $ (480) | $ 767 | $ (187) | $ (1,082) | $ 407 |
| 107,362 | 105,425 | 100,047 | 94,424 | 92,447 |
| 3,229 | 3,001 | 1,354 | 1,484 | 2,791 |
| 881 | 881 | - | - | 217 |
| 9,554 | 9,770 | - | - | 10,007 |
| 121,026 | 119,077 | 101,401 | 95,908 | 105,462 |
| $ 9.63 | $ 6.44 | $ (2.50) | $ 5.21 | $ 3.69 |
| (14.89) | - | .66 | (8.53) | .17 |
| - | - | - | (7.97) | - |
| $ (5.26) | $ 6.44 | $ (1.84) | $ (11.29) | $ 3.86 |

EXHIBIT 12

Computation of Ratio of Earnings to Fixed Charges

| Year ended December 31 (in millions) | 1995 | 1994 | 1993* | 1992 | 1991 |
|---|---|---|---|---|---|
| Fixed Charges: | | | | | |
| Interest expense | $ 591 | $ 520 | $ 540 | $ 627 | $ 596 |
| Rental expense | 142 | 170 | 180 | 187 | 178 |
| Total fixed charges before capitalized interest | 733 | 690 | 720 | 814 | 774 |
| Capitalized interest | - | 2 | 5 | 17 | 3 |
| Total fixed charges | $ 733 | $ 692 | $ 725 | $ 831 | $ 777 |
| Earnings available for fixed charges: | | | | | |
| Earnings** | $1,979 | $1,602 | $ (193) | $1,183 | $1,035 |
| Less undistributed income in minority owned companies | (90) | (54) | (51) | (52) | (70) |
| Add fixed charges before capitalized interest | 733 | 690 | 720 | 814 | 774 |
| Total earnings available for fixed charges | $2,622 | $2,238 | $ 476 | $1,945 | $1,739 |
| Ratio of earnings to fixed charges (1)(2) | 3.58 | 3.23 | 0.66 | 2.34 | 2.24 |

(1) The ratio of earnings to fixed charges has been computed based on the Company's continuing operations by dividing total earnings available for fixed charges, excluding capitalized interest, by total fixed charges. Fixed charges consist of interest, including capitalized interest, and one-third of rent expense as representative of the interest portion of rentals. Debt has been assigned to discontinued operations based on historical levels assigned to the businesses when they were continuing operations adjusted for subsequent paydowns. The discontinued operations consist of the Company's Insurance and Other Financial Services businesses and its real-estate development and third-party financing businesses.

(2) The Company's ratio of earnings to fixed charges includes the effect of the Company's finance subsidiaries, which primarily finance Xerox equipment. Financing businesses are more highly leveraged and, therefore, tend to operate at lower earnings to fixed charges ratio levels than do non-financial businesses.

* 1993 earnings were inadequate to cover fixed charges. The coverage deficiency was $249 million.

** Sum of "Income (Loss) before Income Taxes, Equity Income and Minorities' Interests" and "Equity in Net Income of Unconsolidated Affiliates."

Consolidated Statements of Income

| Year ended December 31 (in millions, except per-share data) | 1995 | 1994 | 1993 |
|---|---|---|---|
| REVENUES | | | |
| Sales | $ 8,799 | $ 7,853 | $ 7,211 |
| Service and rentals | 6,804 | 6,229 | 5,954 |
| Finance income | 1,008 | 1,006 | 1,064 |
| Total Revenues | 16,611 | 15,088 | 14,229 |
| COSTS AND EXPENSES | | | |
| Cost of sales | 4,962 | 4,653 | 4,098 |
| Cost of service and rentals | 3,437 | 3,016 | 2,986 |
| Equipment financing interest | 509 | 502 | 537 |
| Research and development expenses | 951 | 895 | 883 |
| Selling, administrative and general expenses | 4,770 | 4,394 | 4,477 |
| Special charges, net | - | - | 1,373 |
| Other, net | 135 | 114 | 155 |
| Total Costs and Expenses | 14,764 | 13,574 | 14,509 |
| INCOME (LOSS) BEFORE INCOME TAXES, EQUITY INCOME AND MINORITIES' INTERESTS | 1,847 | 1,514 | (280) |
| Income Taxes (Benefits) | 615 | 595 | (78) |
| Equity in Net Income of Unconsolidated Affiliates | 132 | 88 | 87 |
| Minorities' Interests in Earnings of Subsidiaries | 190 | 213 | 78 |
| INCOME (LOSS) FROM CONTINUING OPERATIONS | 1,174 | 794 | (193) |
| Discontinued Operations | (1,646) | - | 67 |
| NET INCOME (LOSS) | $ (472) | $ 794 | $ (126) |
| PRIMARY EARNINGS (LOSS) PER SHARE | | | |
| Continuing Operations | $ 10.20 | $ 6.73 | $ (2.50) |
| Discontinued Operations | (14.89) | - | .66 |
| PRIMARY EARNINGS PER SHARE | $ (4.69) | $ 6.73 | $ (1.84) |
| FULLY DILUTED EARNINGS (LOSS) PER SHARE | | | |
| Continuing Operations | $ 9.63 | $ 6.44 | $ (2.50) |
| Discontinued Operations | (14.89) | - | .66 |
| FULLY DILUTED EARNINGS PER SHARE | $ (5.26) | $ 6.44 | $ (1.84) |

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

[PHOTO]

Chuck Wessendorf
Clark Robson
Investor Relations



FINANCIAL REVIEW

## Our Results of Operations and Financial Condition

### SUMMARY OF TOTAL COMPANY RESULTS

In January 1996, we announced agreements to sell our remaining property and casualty insurance units to investor groups led by Kohlberg Kravis Roberts & Co. and existing management for consideration totaling $2.7 billion. We expect the transactions will close in the middle of this year. As a result, results from insurance operations are now accounted for as discontinued operations and all prior periods have been restated. Therefore the Document Processing business is the only component of Continuing Operations.

Document Processing revenues increased 10 percent to $16.6 billion in

1995, following an increase in revenues to $15.1 billion in 1994 from $14.2 billion in 1993.

The following table summarizes net income:

| (In millions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| Document Processing before Special Items | $ 1,076 | $ 794 | $ 580 |
| Tax Benefits | 98 | - | 40 |
| Special Charges | - | - | (813) |
| Continuing Operations | 1,174 | 794 | (193) |
| Discontinued Operations | (1,646) | - | 67 |
| Net Income (Loss) | $ (472) | $ 794 | $(126) |

Document Processing income in 1995 increased 36 percent to $1,076 million before a $98 million gain from a reduction in the Brazilian tax rate, from $794 million in 1994. Income increased 37 percent in 1994 from $580 million in 1993 before special items. The 1993 special items included charges of $813 million after taxes to provide for the costs of restructuring the Document Processing business and lawsuit settlements, and $40 million in one-time tax benefits. After special items, Document Processing reported a $193 million loss in 1993.

Fully diluted earnings per share for Continuing Operations, which now include only the Document Processing business, increased 37 percent to $8.83 in 1995, before the Brazilian tax gain, from $6.44 in 1994 which was a 33 percent increase from $4.86 in

[PHOTO]
Pictured here is Charlene Stephens, Public Relations, and a graphic depicting Continuing Operations Fully Diluted Earnings per Share before special items of $8.83 for 1995, $6.44 for 1994 and $4.86 for 1993.

1993, before special items. The 1993 Continuing Operations earnings per share reflect the impact of the additional 8.1 million shares issued through an equity offering in June 1993.

Discontinued Operations had a loss of $1.646 billion in 1995 compared with break-even results in 1994 and income of $67 million in 1993. The 1995 results reflect fourth quarter after-tax charges of $1.546 billion as a result of the insurance disengagement. These charges consist of a non-cash loss on the sales of $978 million and $568 million primarily to cover additional insurance loss reserves and all estimated future expenses associated with excess of loss reinsurance coverage. Prior to the fourth quarter charges, insurance operations had a $100 million loss in the 1995 full year. The 1993 results included a $62 million after-tax gain on the sale of The Van Kampen Merritt Companies, Inc. (VKM).



The fully diluted loss per share for Discontinued Operations was $14.89, compared with break-even in 1994, and income of $.66 in 1993.

The net loss in 1995 of $472 million compares with net income of $794 million in 1994, and a net loss of $126 million in 1993. The fully diluted loss per share of $5.26 in 1995 compares with earnings of $6.44 in 1994 and a net loss of $1.84 per share in 1993.

DOCUMENT PROCESSING

UNDERLYING GROWTH

To understand the trends in the business, we believe that it is helpful to adjust revenue and expense growth (except for ratios) to exclude the impact of the changes in the translation of foreign currencies into U.S. dollars and special items that distort the trends. We refer to this adjusted growth as "underlying growth." The items that have been excluded from the discussion of underlying growth are the 1993 charges for the Document Processing restructuring program and the lawsuit settlements.

When compared with the major European currencies, the U.S. dollar was approximately 10 percent weaker in 1995, 2 percent stronger in 1994 and 11 percent stronger in 1993. As a result, foreign currency translation had a favorable impact of 3 percentage points on revenues in 1995, and unfavorable impacts of 1 percentage point in 1994 and 4 percentage points in 1993. We do not hedge foreign-currency denominated revenues to the extent they do not represent cross-border cash flows.

REVENUES

The estimated components of underlying growth were as follows:

| | Underlying Growth | | |
|---|---|---|---|
| | 1995 | 1994 | 1993 |
| Total Revenues | 7% | 7% | 3% |
| Equipment Sales* | 6 | 10 | (1) |
| Non-equipment revenues | 7 | 5 | 6 |
| Supplies | 9 | 11 | 11 |
| Paper | 39 | 4 | (4) |
| Service | 2 | 4 | 6 |
| Rentals | 1 | (1) | (6) |
| Document Outsourcing/Other | 32 | 20 | 5 |
| Finance Income | (4) | (4) | 4 |

* Only includes equipment sales to end-users

The decline in the growth in equipment sales, across most major product lines, in 1995 principally reflects disruption in the U.S. sales force primarily caused by the realignment of the field sales organization and

[PHOTO]
Pictured here is a graphic depicting Equipment Sales Growth of 6% in 1995, 10% in 1994 and -1% in 1993; Non-Equipment Revenue Growth of 7% in 1995, 5% in 1994 and 6% in 1993; and Total Revenue Growth of 7% in 1995, 7% in 1994 and 3% in 1993.



changes in sales compensation plans. Modifications have been made to these plans, sales force turnover has declined and we believe that the disruption will have a declining impact going forward.

The growth in 1994 reflected good growth in black-and-white copiers, excellent growth in the DocuTech family of digital publishers and a near doubling of color copier and printer equipment sales.

Non-equipment revenues from supplies, paper, service, rentals, document outsourcing and other revenues, and income from customer financing represented 67 percent of total revenues in 1995, 65 percent of total revenues in 1994 and 63 percent in 1993. These revenues are less volatile than equipment sales revenues, and therefore provide significant stability to overall revenues. Growth in these revenues is primarily a function of the growth in our installed population of equipment, usage and pricing.

- - Supplies sales: The strong growth over the last several years is principally due to cartridge sales for personal and convenience copiers and to new OEM customers.

- - Paper sales: The significant improvement in the growth rate in 1995 is primarily due to higher prices, commencing in late 1994, after several years of declining wholesale prices. Our strategy is to charge a spread over mill wholesale prices.

- - Service revenues: The declining growth reflects the diversionary trend to document outsourcing, rental plans and competitive pricing pressures.

- - Rental revenues: After a number of years of decline, reflecting a customer preference for outright purchase of equipment, the rate of decline was arrested by an increasing, but still relatively small, trend principally in the U.S. toward cost-per-copy rental plans.

- - Document outsourcing, copy centers and other revenues: The growth in 1995 and 1994 reflected the trend of customers to focus on their core businesses and outsource their document processing require-ments to Xerox. This trend, which diverts revenue from equipment sales, service and finance income, can reduce current period total revenues but increase revenues in future periods.

- - Finance income: The continuing decline in 1995 reflects lower interest rates on financing contracts, the increasing customer preference for document out-sourcing rather than purchase and finance and a stabilization in the percent of customers who finance purchases through Xerox at approximately 80 percent of equipment sales in the U.S. and 70 percent in Western Europe. Our strategy is to charge a spread over our cost of borrowing.

Geographically, the underlying revenue growth rates were estimated as follows:

| | UNDERLYING GROWTH | | |
|---|---|---|---|
| | 1995 | 1994 | 1993 |
| Total Revenues | 7% | 7% | 3% |
| United States | 3 | 7 | 4 |
| Rank Xerox | 8 | 7 | 2 |
| Other Areas | 16 | 7 | 4 |

United States revenues were 49 percent of total revenues. Revenues of Rank Xerox Limited and related companies (Rank Xerox), which manufacture and market our products in eastern hemisphere countries, were 33 percent of total revenues. Revenues of Other Areas, which includes operations principally in Latin America and Canada, were 18 percent of total revenues.

[PHOTO AND CAPTION]

Pictured here are Vicente Jose Felice, Adelia Maria Branco Cerqueira, Jorge Pereira da Silva, and Sergio Nicola, Xerox of Brazil, with the caption "Itau Bank, Sao Paulo, found a more productive way to produce checkbooks when it adopted a Xerox solution based on a 4635MX printer connected in-line to a checkbook maker. The automatic process saved the bank the costs of manual production."



[PHOTO]

VIMAL GADHIA
Rank Xerox
Corporate Communications

The decline in U.S. revenue growth in 1995 principally reflects the disruption in the sales force. The improving revenue growth in Rank Xerox and the Other Areas in 1995 reflected good growth in black-and-white copiers and excellent growth in enterprise printing products, attributable, in part, to improving sales productivity and a strong economic environment in Brazil. In Mexico, revenues declined significantly in 1995 due to currency and the continuing economic disruption following devaluation of the Mexican peso in December 1994. In 1995, revenues were approximately $1.4 billion in Brazil and $200 million in Mexico compared with 1994 revenues of approximately $1 billion and $300 million, respectively. The improved revenue growth in all areas in 1994 reflected good growth in black-and-white copiers, excellent growth in the DocuTech family of digital publishers and a near doubling of color copier and printer revenues, attributable, in part, to improved sales productivity and economic environments.

For the major product categories, the underlying revenue growth rates were estimated as follows:

| | Underlying Growth | | |
|---|---|---|---|
| | 1995 | 1994 | 1993 |
| Total Revenue | 7% | 7% | 3% |
| Enterprise Printing | 17 | 20 | 18 |
| Black and White Copiers | 2 | 4 | - |
| Paper and Other Products | 14 | 3 | (5) |

Revenues from enterprise printing, comprised of production publishing, color copying and printing, data center printing and network printing, represented 25 percent of total document processing revenues in 1995, 22 percent in 1994 and 19 percent in 1993. Revenues from black-and-white copying represented 59 percent of total document processing revenues in 1995, 63 percent in 1994 and 65 percent in 1993. The revenues from paper and other products were 16 percent of total document processing revenues in 1995, 15 percent in 1994 and 16 percent in 1993.

Total revenues from the DocuTech family of production publishing products reflected excellent growth to $1.4 billion in 1995 and $1.1 billion in 1994. Revenues from color products grew 45 percent to approximately $600 million in 1995 from approximately $400 million in 1994, which in turn had almost doubled over 1993 levels. Revenues from network and data center printing products had good growth in both 1995 and 1994. We believe that the declining growth in enterprise printing revenues during 1995 was the result of the U.S. sales force disruption and weak economic environments in Canada and some European countries.

During the fourth quarter of 1995, we introduced the first two products in the Document Centre Systems family, a new enterprise printing category. These networked office products print, scan, fax and copy documents for work groups, with all operations managed over the network from each user's personal computer or on a walk-up basis.

The decline in black-and-white copying revenue growth in 1995 reflects the slowdown in revenue growth in the U.S. Black-and-white copying revenues had good growth in international markets. The other revenue growth in 1995 and 1994 and the decline in 1993 were principally due to paper pricing.

PRODUCTIVITY INITIATIVES

In 1993, we announced a restructuring program to significantly reduce the cost base and to improve productivity. Our objectives were to reduce our



worldwide work force by more than 10,000 employees and to close or consolidate a number of facilities.

To date, the activities associated with the 1993 restructuring program have reduced employment by 12,000 and achieved pre-tax cost savings of approximately $650 million in 1995 and $350 million in 1994. However, we have reinvested a portion of these savings to re-engineer business processes, support the expansion in growth markets, and mitigate anticipated continued pricing pressures.

Employment declined by 2,400 from year-end 1994 to 85,200 employees at the end of 1995; 4,400 reductions were due to restructuring program initiatives, partially offset by the addition of 2,000 employees, principally to support the document outsourcing business.

We are on track towards achieving our restructuring program objectives.

During 1994, we awarded a 10-year, $3.2 billion contract to Electronic Data Systems Corp. (EDS) to operate our worldwide computer and telecommunications network. Information management strategy and architecture and the development of systems for re-engineered business processes were not outsourced.

Also in 1994, we signed a labor agreement with the principal union that represents U.S. manufacturing employees. We believe that the contract has enabled productivity, competitive advantages and progress towards achieving benchmark unit manufacturing costs.

COSTS AND EXPENSES

The gross margins by revenue stream were as follows:

| | Gross Margins | | |
|---|---|---|---|
| | 1995 | 1994 | 1993 |
| Total | 46.4% | 45.8% | 46.4% |
| Sales | 43.6 | 40.7 | 43.2 |
| Service and Rentals | 49.5 | 51.6 | 49.9 |
| Finance Income | 49.5 | 50.1 | 49.5 |

The 1995 improvement in sales gross margins was principally due to cost

reductions, favorable product and geographic mix, principally Brazil, partially offset by pricing pressures. The declines in sales gross margins during 1994 were principally due to adverse currency, competitive pricing, unfavorable product and channel mix and inventory adjustments partially offset by improved productivity. In 1995, the

[PHOTO]
Pictured here is a graphic depicting Selling, Administrative and General Expenses (Percent of Revenues) of 28.7% in 1995, 29.1% in 1994 and 31.5% in 1993.

erosion in service and rentals gross margins was largely due to pricing pressures and economics, partially offset by productivity improvements. The service and rentals gross margin improvement during 1994 was principally due to improved productivity and price increases partially offset by economic cost increases and adverse currency.

Research and development (R&D) expense increased 6 percent in 1995 and 1 percent in 1994. We expect to increase our investment in technological development in 1996 and over the longer term to maintain our premier position in the rapidly changing document processing market. We strategically coordinate R&D with Fuji Xerox. The R&D investment by Fuji Xerox was approximately $600 million in 1995, bringing the total to approximately $1.5 billion.



Selling, administrative and general expenses (SAG) increased 6 percent in 1995 on an underlying basis, declined 1 percent in 1994, and were essentially unchanged in 1993. SAG as a percent of revenues was 28.7 percent in 1995 compared with 29.1 percent in 1994 and 31.5 percent in 1993. The improvement in the ratios is primarily due to improved productivity, partially offset by investments in systems and in support of high-growth markets, principally document outsourcing and our operations in Brazil, where the rate of inflation exceeded pricing.

Other expenses, net, were $135 million in 1995, $114 million in 1994, and $155 million in 1993. The increase in Other expenses, net of $21 million in 1995 reflects higher interest expense and goodwill amortization, principally resulting from our increased financial interest in Rank Xerox, and the non-recurrence of one-time gains in 1994, partially offset by lower foreign currency losses from balance sheet translation in our Brazilian operations. The decrease in Other expenses, net of $41 million in 1994 primarily reflects lower foreign currency losses in Brazil.

Our South American operations in general, and Brazil in particular, are subject to hyperinflation, government-imposed price controls and currency devaluation. By historical standards Brazilian exchange rates have been relatively stable since the implementation of a new economic plan in mid-1994. There can be no assurance this relative stability will continue.

INCOME TAXES, EQUITY IN NET INCOME OF UNCONSOLIDATED AFFILIATES, AND MINORITIES' INTERESTS IN EARNINGS OF SUBSIDIARIES BEFORE SPECIAL ITEMS

Income before special items and income taxes was $1,847 million in 1995 compared with $1,514 million in 1994 and $1,093 million in 1993.

Excluding a $98 million gain from a reduction in the Brazilian statutory tax rate in 1995, gains from statutory rate changes in 1993 and $813 million of special charges in 1993, the effective tax rate was 39 percent in 1995 and 1994, and 41 percent in 1993. The higher tax rate in 1993 was due to mix of oper-

Pictured here is a graphic depicting Document Processing Return on Assets of 18.5% in 1995, 16.1% in 1994 and 12.6% in 1993 before special items.

ations. We estimate that the impact of the lower Brazilian statutory tax rate will result in a two percentage point decline in the effective tax rate in the future.

Equity in Net Income of Unconsolidated Affiliates increased 50 percent to $132 million in 1995 after remaining essentially unchanged at $88 million in 1994. The equity in the income of Fuji Xerox, the principal unconsolidated affiliate, increased 41 percent in 1995 due to revenue growth in the Japanese domestic market and the strengthening of the Japanese yen against the U.S. dollar. The equity in the income of Fuji Xerox in 1994 reflected improved operating results offset by a provision for an early retirement program.

Minorities' Interests in Earnings of Subsidiaries were $190 million in 1995 compared with $213 million in 1994 and $152 million, before the effect of special items, in 1993. The 1995 decrease was due to our increased financial interest in Rank Xerox, partially offset by excellent growth in Rank Xerox income, reflecting good revenue growth and benefits from productivity. The 1994 increase was due to excellent growth in Rank Xerox income, reflecting strong revenue growth as well as benefits from productivity.

INCOME

In 1995, Document Processing income of $1,076 million, before the Brazilian tax gain, grew 36 percent compared with $794 million in 1994. 1994 income of $794 million grew 37 percent from $580 million before 1993 special items.



RETURN ON ASSETS

Improving Return on Assets (ROA) is an important focus throughout all levels of the Document Processing organization, combining a focus on both asset turnover and margin improvement. Excluding special items, the 1995 ROA was 18.5 percent compared with 16.1 percent in 1994 and 12.6 percent in 1993.

The internal measurement for ROA is defined as Document Processing before-tax profits plus equity in the net income of unconsolidated affiliates divided by average ROA assets. These assets are Document Processing assets less investments in affiliates and Xerox equipment financing debt.

SPECIAL ITEMS

In the fourth quarter of 1993, $813 million after income taxes and minorities' interests in earnings of subsidiaries was provided for the costs of a restructuring program and lawsuit settlements.

In January 1994, we reached agreement to settle a 1992 antitrust class action lawsuit involving selling spare parts for high-volume copiers and printers to independent service organizations, and a lawsuit involving the termination of a contract to purchase laptop computers. Under the antitrust settlement, $225 million of discount certificates were provided to members of the plaintiff class for use as partial payment on future purchases of Xerox products, and we agreed to sell service parts to independent service organizations in the U.S., similar to the existing policy in Europe.

The discount certificates are available for use over a three-year period that commenced in September 1994 and may be applied against the payment of future purchases, excluding service, by our customers. Through 1995, $119 million of discount certificates were applied against purchases.

In 1995, we recognized a $98 million benefit from the favorable revaluation of the deferred tax liability due to a change in the Brazilian statutory income tax rate from 45 percent to 30 percent. In 1993, we benefited from a total of $40 million of favorable revaluations of deferred tax provisions due to changes in the U.S. and Brazilian statutory income tax rates.

Quarterly Analytical Earnings Per Share

We believe that the 1995 Continuing Operations results, before the gain from a reduction in the Brazilian tax rate, are an appropriate basis for comparison

with future financial results. The following schedule summarizes the 1995 Continuing Operations revenues, income and Earnings Per Share computations, before the gain from a reduction in the Brazilian tax rate, on a quarterly basis.

| (In millions, except per-share data, unaudited) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|---|---|---|---|---|---|
| Revenues | $3,770 | $4,054 | $4,027 | $4,760 | $16,611 |
| Income | $ 187 | $ 254 | $ 256 | $ 477 | $ 1,174 |
| Gain from Brazilian tax rate reduction | - | - | - | 98 | 98 |
| Income before gain from tax rate reduction | $ 187 | $ 254 | $ 256 | $ 379 | $ 1,076 |
| Primary Earnings per Share | | | | | |
| Preferred dividends net of tax benefit | $ (12) | $ (11) | $ (11) | $ (11) | $ (45) |
| Income available for common shareholders | 175 | 243 | 245 | 368 | 1,031 |
| Adjusted average shares outstanding | 109.2 | 110.2 | 110.8 | 111.4 | 110.6 |
| Primary Earnings per Share | $ 1.60 | $ 2.21 | $ 2.21 | $ 3.30 | $ 9.32 |
| Fully Diluted Earnings per Share | | | | | |
| Preferred dividends net of tax benefit | $ (3) | $ (2) | $ (1) | $ (2) | $ (8) |
| Income available for common shareholders | 184 | 252 | 255 | 377 | 1,068 |
| Adjusted average shares outstanding | 119.9 | 120.7 | 121.5 | 121.8 | 121.0 |
| Fully Diluted Earnings per Share | $ 1.54 | $ 2.09 | $ 2.09 | $ 3.11 | $ 8.83 |



ADDITIONAL FINANCIAL INTEREST IN RANK XEROX

On February 28, 1995, we paid The Rank Organisation Plc (RO) (Pounds)620 million, or $972 million, for a 40 percent share of RO's financial interest in Rank Xerox. The transaction increased our financial interest in Rank Xerox to about 80 percent from 67 percent. The transaction resulted in goodwill of $574 million and a decline in minorities' interests in equity of subsidiaries of approximately $400 million.

The transaction increased earnings per share and cash flow in 1995, and we estimate that it will have a positive impact on earnings per share and cash flow going forward. Minorities' interests in earnings of subsidiaries declined by approximately 40 percent as a result of the transaction, which was partially offset by an increase in interest expense related to the funding of the transaction. The goodwill is amortized over 40 years, resulting in an annual impact of $14 million, before and after taxes.

RANK XEROX AND LATIN AMERICAN FISCAL-YEAR CHANGE IN 1995

Effective January 1, 1995, we changed Rank Xerox and Latin American operations to calendar-year financial reporting. The 1994 fiscal year ended on October 31 for Rank Xerox and on November 30 for Latin American operations. The results of these non-U.S. operations that occurred between the 1994 and 1995 fiscal years (the stub period) were accounted for as a direct charge to equity. A loss of $21 million was charged to equity in the stub period, primarily due to the currency devaluation and related economic dislocations in Mexico. Excluding the Mexican devaluation and related economic dislocations, income during the stub period was $4 million.

[PHOTO]
Pictured here are Josue Freitas and Miguel Brandtner, Xerox of Brazil, with the caption "Pelotas University, Rio Grande do Sul, Brazil, dramatically increased its production with the DocuTech Production Publisher, going from 4 to 40 books a year."



CONSOLIDATED BALANCE SHEETS

| December 31 (in millions) | 1995 | 1994 |
|---|---|---|

| | | |
|---|---|---|
| ASSETS | | |
| Cash | $ 130 | $ 35 |
| Accounts Receivable, net | 1,894 | 1,811 |
| Finance Receivables, net | 4,069 | 3,910 |
| Inventories | 2,646 | 2,294 |
| Deferred Taxes and Other Current Assets | 1,094 | 1,199 |
| Total Current Assets | 9,833 | 9,249 |
| Finance Receivables Due after One Year, net | 6,406 | 6,038 |
| Land, Buildings and Equipment, net | 2,092 | 2,108 |
| Investments in Affiliates, at Equity | 1,328 | 1,278 |
| Goodwill | 627 | 66 |
| Other Assets | 873 | 635 |
| Investment in Discontinued Operations | 4,810 | 7,904 |
| TOTAL ASSETS | $25,969 | $27,278 |
| LIABILITIES AND EQUITY | | |
| Short-Term Debt and Current Portion of Long-Term Debt | $ 3,265 | $ 3,159 |
| Accounts Payable | 563 | 562 |
| Accrued Compensation and Benefit Costs | 731 | 709 |
| Unearned Income | 228 | 298 |
| Other Current Liabilities | 2,212 | 2,110 |
| Total Current Liabilities | 6,999 | 6,838 |
| Long-Term Debt | 7,867 | 7,074 |
| Postretirement Medical Benefits | 1,018 | 1,006 |
| Deferred Taxes and Other Liabilities | 2,436 | 2,732 |
| Discontinued Operations Liabilities - Policyholders' Deposits and Other | 2,810 | 4,194 |
| Deferred ESOP Benefits | (547) | (596) |
| Minorities' Interests in Equity of Subsidiaries | 745 | 1,021 |
| Preferred Stock | 763 | 832 |
| Common Shareholders' Equity | 3,878 | 4,177 |
| TOTAL LIABILITIES AND EQUITY | $25,969 | $27,278 |

Shares of common stock issued and outstanding at December 31, 1995 and 1994 were (in thousands) 108,343 and 105,993, respectively.

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

[PHOTO]

SUE ANDERSON
Investor Services



CAPITAL RESOURCES AND LIQUIDITY

CAPITAL RESOURCES

Total debt, including ESOP and Discontinued Operations debt not shown separately in our consolidated balance sheets, increased to $11,785 million at December 31, 1995, from $10,939 million in 1994 and $10,084 million in 1993.

On a consolidated basis, the debt-to-capital ratio at December 31, 1995 was 71 percent compared with 67 percent in 1994 and 66 percent in 1993. The increase over 1994 was primarily due to the $972 million paid for our increased financial interest in Rank Xerox and growth in the financing of equipment sales.

For purposes of capital ratio analysis, total equity includes common equity, preferred stock and minorities' interests in the equity of subsidiaries.

The following table summarizes the changes in total equity during 1995 and 1994:

| (In millions) | Total Equity 1995 | Total Equity 1994 |
|---|---|---|
| Balance as of January 1 | $ 6,030 | $5,882 |
| Income from Continuing Operations | 1,174 | 794 |
| Loss from Discontinued Operations | (1,646) | - |
| Change in Unrealized Gains (Losses) on Investment Securities | 432 | (439) |
| Shareholder Dividends Paid | (389) | (395) |
| Change in Minorities' Interests | (276) | 177 |
| Exercise of Stock Options | 137 | 92 |
| All Other, net | (76) | (81) |
| Balance as of December 31 | $ 5,386 | $6,030 |

We manage the capital structure of our non-financing operations separately from that of our more highly leveraged activities. The following table summarizes the ratios of earnings to fixed charges and interest expense; and debt, equity and total capital for our non-financing and financing activities for the three-year period ended December 31, 1995:

| (Dollars in millions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| NON-FINANCING: | | | |
| Ratio of Earnings to Fixed Charges | 3.87x | 3.59x | 2.58x |
| Ratio of Earnings to Interest Expense | 5.35x | 5.75x | 4.10x |
| Debt | $ 3,003 | $2,651 | $2,446 |
| Equity | 4,035 | 4,730 | 4,679 |
| Total Capital | $ 7,038 | $7,381 | $7,125 |
| Debt-to-Capital Ratio | 42.7%* | 35.9% | 34.3% |
| FINANCING: | | | |
| Debt | $ 8,782 | $8,288 | $7,638 |
| Equity | 1,351 | 1,300 | 1,203 |
| Total Capital | $10,133 | $9,588 | $8,841 |
| Debt-to-Equity Ratio | 6.5x | 6.4x | 6.4x |
| Ratio of Earnings to Fixed Charges | 1.71x | 1.81x | 1.78x |
| Ratio of Earnings to Interest Expense | 1.71x | 1.81x | 1.78x |

/*/ 31.2 percent, on a pro forma basis, adjusted for anticipated receipt of net proceeds from the announced sale of Talegen's remaining operating groups.

The 1995 debt-to-capital ratio for non-financing operations, including ESOP debt and Discontinued Operations debt, increased as Document Processing cash generation, net of shareholder dividends, and the proceeds from the sales of Constitution Re Corporation, Viking Insurance Holdings, Inc. and the Xerox Financial Services Life Insurance Company and related companies were more than offset by the

[PHOTO]

Pictured here is David Cloyd, XSoft, with the caption "The new publishing system incorporating XSoft's InConcert enables TV Guide to produce several dozen editions simultaneously, managing the production process for the magazine's features, program listings and advertisements. TV Guide needed a workflow solution that could automate the processing of editorial tasks, as well as provide quality control capabilities. InConcert's centralized management and monitoring features prevent errors and allow system operators to track the editorial assembly and compilation process - a cycle that encompasses more than 10,000 tasks per week - across the company network. TV Guide has the nation's largest magazine readership with a circulation of more than 13 million readers."



[PHOTO]

JANAE TUCKER-TAYLOR (IN-FRONT)
ANGELA TUCKER-TAYLOR
Investor Relations

purchase of the increased financial interest in Rank Xerox and non-cash charges in connection with the sales of the remaining Talegen units. The 1994 ratio of 35.9 percent increased from 34.3 percent at year-end 1993 as strong net cash flow from Document Processing was more than offset by the impact of Talegen business unit borrowings, unrealized insurance investment portfolio losses and the redemption of preferred stock.

With respect to our financing activities, we match fund by arranging fixed-rate liabilities with maturities similar to the underlying customer financing assets. Our guideline debt-to-equity ratio for the financing activities is 6.5 to 1.

The following table summarizes the principal causes for changes in consolidated indebtedness for the three-year period ended December 31, 1995:

| (In millions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| Total Debt/*/ as of January 1 | $10,939 | $10,084 | $10,638 |
| NON-FINANCING BUSINESSES: | | | |
| Document Processing Operations | (543) | (989) | (496) |
| Increased financial interest in Rank Xerox | 972 | - | - |
| Yen/$ Financing repayment | - | 116 | - |
| ESOP | (49) | (45) | (40) |
| Discontinued businesses | (399) | 605 | (15) |

| | | | |
|---|---|---|---|
| Non-Financing | (19) | (313) | (551) |
| FINANCING BUSINESSES, NET | 494 | 650 | 210 |
| Total Operations | 475 | 337 | (341) |
| Shareholder dividends | 389 | 395 | 389 |
| Equity issuance (redemption) and other changes | (18) | 123 | (602) |
| Total Debt* as of December 31 | $11,785 | $10,939 | $10,084 |

/*/ Including Discontinued Operations

NON-FINANCING OPERATIONS

The following table summarizes 1995 and 1994, Document Processing non-financing operations cash generation and borrowing:

| (In millions) | Cash Generated/(Borrowed) 1995 | 1994 |
|---|---|---|
| DOCUMENT PROCESSING NON-FINANCING: | | |
| Income | $ 970 | $ 565 |
| Depreciation and Amortization | 660 | 649 |
| Restructuring Payments | (331) | (423) |
| Capital Expenditures | (438) | (389) |
| Assets Sold | 90 | 220 |
| Working Capital/Other | (408) | 367 |
| | $ 543 | $ 989 |

1995 cash generation of $543 million was $446 million below the 1994 level as higher income and lower restructuring payments were more than offset by lower sales of fixed assets (primarily related to the information management outsourcing), higher capital spending, inventory growth including equipment on operating lease, and 1994 profit sharing paid in 1995.

Discontinued businesses generated $399 million of cash in 1995 resulting from proceeds from the sales of Constitution Re Corporation, Viking Insurance Holdings, Inc. and the Xerox Financial Services Life Insurance Company and related companies, partially offset by premium and interest payments to Ridge Re and debt service requirements. This contrasts with $605 million of net borrowing in 1994 resulting from higher debt service requirements and borrowing by Talegen business units to retire intercompany debt and fund investment activities. Net cash generation of $15 million in 1993 was mainly due to cash proceeds from the 1993 sales of VKM and Furman Selz Holding Corporation, partially offset by Talegen restructuring requirements.



FINANCING BUSINESSES

Financing business debt grew by $494 million in 1995 or $156 million less

than in 1994 due to lower growth in equipment sales revenue and the effects of translating foreign currencies into U.S. dollars. Financing debt growth of $650 million in 1994 was $440 million more than in 1993 due to accelerated growth in equipment sales revenue and currency translation effects.

Debt related to discontinued third-party financing activities, which is included in Financing Business debt, totaled $231 million in 1995 and 1994, and $424 million in 1993. Portfolio run-off in 1995 was offset by timing differences related to tax payments while the 1994 debt reduction reflects both asset sales and run-off.

FUNDING PLANS FOR 1996

Non-financing debt levels will be significantly affected by proceeds from the expected sales in 1996 of the remaining Talegen Holdings, Inc. (Talegen) insurance operating groups for a total of $2.7 billion, including $1.4 billion in cash partially offset by $0.6 billion of cash usage related to the funding of intercompany accounts and transaction costs, and borrowing activity resulting from the recently announced plan to repurchase up to $1 billion of our common stock. Customer financing-related debt is planned to increase in line with 1996 sales activity.

We believe that we have adequate short-term credit facilities available to fund day-to-day operations and have readily available access to the capital markets to meet any longer-term financing requirements. Our domestic operations have a $5.0 billion revolving credit agreement with a group of banks, which expires in 2000. This facility is unused and available to provide back-up to our commercial paper borrowings, which amounted to $2.8 billion and $2.4 billion at December 31, 1995 and 1994, respectively. In addition, our foreign subsidiaries have unused committed long-term lines of credit aggregating $1.7 billion, in various currencies at prevailing interest rates, that are used to provide back-up to short-term indebtedness.

At December 31, 1995, Xerox and XCC had domestic shelf capacity of $865 million and $1 billion, respectively. A $1 billion Euro-debt facility is available to both Xerox and XCC of which $547 million remained unused at December 31, 1995. In 1996, we intend to increase the size of the Euro facility by $1 billion to further enhance our capital markets flexibility.

Decisions in 1996 regarding the size and timing of any new term debt financing will be made based on cash flows, match funding needs, refinancing requirements and capital market conditions.

[PHOTO]

Pictured here is a Xerox 5614 convenience copier with the caption "The Xerox 5614 convenience copier is a "green machine" that lets the user exercise environmental responsibility without paying a cost penalty. It features customer-settable Power Saver, low noise, reduced ozone emissions, returnable copy and toner cartridges, recyclable packaging and design suitable for remanufacturing. Customers can return both their used copy and toner cartridges, which will then recycle, reuse or remanufacture to new-product standards.

This Xerox cartridge remanufacturing and reuse initiative reduced the amount of material entering the waste stream in 1995 by more than 1,100 tons. Customers have shown their strong acceptance of the program, returning nearly 60 percent of all cartridges in 1995."



HEDGING INSTRUMENTS

We have entered into certain financial instruments to manage interest rate and foreign currency exposures. These instruments are held solely for hedging purposes and include interest rate swap agreements, forward foreign exchange contracts and foreign currency swap agreements. We have long-standing policies prescribing that derivative instruments are only to be used to achieve a set of

very limited objectives: to lock in the value of cross-border cash flows and to reduce the impact of currency and interest rate volatility on costs, assets and liabilities. We do not enter into derivative instrument transactions for trading purposes.

Currency derivatives are primarily arranged in conjunction with underlying transactions that give rise to foreign currency-denominated payables and receivables: for example, an option to buy foreign currency to settle the importation of goods from suppliers, or a forward foreign-exchange contract to fix the rate at which a dividend will be paid by a foreign subsidiary. In addition, when cost-effective, currency derivatives are also used to hedge balance sheet exposures in hyperinflationary economies.

We do not hedge foreign currency-denominated revenues of our foreign subsidiaries since these do not represent cross-border cash flows.

With regard to interest rate hedging, virtually all customer financing assets earn fixed rates of interest and, therefore, we "lock in" an interest rate spread by arranging fixed-rate liabilities with similar maturities as the underlying assets. Additionally, customer financing assets in one currency are consistently funded with liabilities in the same currency. We refer to the effect of these conservative practices as "match funding" customer financing assets. This practice effectively eliminates the risk of a major decline in interest margins resulting from adverse changes in the interest rate environment. Conversely, this practice does effectively eliminate the opportunity to materially increase margins when interest rates are declining.

More specifically, pay fixed-rate and receive variable-rate swaps are typically used in place of more expensive fixed-rate debt. Pay variable-rate and receive variable-rate swaps are used to transform variable-rate medium-term debt into commercial paper or local currency LIBOR obligations. Additionally, pay variable-rate and receive fixed-rate swaps are used from time to time to transform longer-term fixed-rate debt into commercial paper-based rate obligations. The transactions performed within each of these three categories enable the cost effective management of interest rate exposures. The potential

[PHOTO]

Pictured here is Mel Peel, Xerox Business Services, UK, with the caption "A Dun & Bradstreet unit in the U.S. develops market intelligence reports for European customers on Monday and Tuesday and transmits them electronically on Thursday to the Document Technology Centre at Rank Xerox Mitcheldean. Personalized reports are printed on Friday and mailed to 16 countries. Documents Direct, our network document service, eliminates shipping costs and gets the reports on customers' desks at least three days earlier than previously."



CONSOLIDATED STATEMENTS OF CASH FLOWS

| Year ended December 31 (in millions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | |
| Income (Loss) from Continuing Operations | $1,174 | $ 794 | $ (193) |
| Adjustments required to reconcile income (loss) to cash flows from operating activities: | | | |
| Depreciation and amortization | 660 | 649 | 629 |
| Provision for special charges | - | - | 1,373 |
| Provisions for doubtful accounts | 308 | 252 | 250 |
| Provision for postretirement medical benefits | 40 | 54 | 70 |
| Charges against 1993 restructuring reserve | (331) | (423) | - |
| Minorities' interests in earnings of subsidiaries | 190 | 213 | 78 |
| Undistributed equity in income of affiliated companies | (90) | (54) | (51) |
| Increase in inventory | (604) | (472) | (228) |
| Increase in finance receivables | (774) | (937) | (993) |
| (Increase) decrease in accounts receivable | (173) | (266) | 134 |
| Increase (decrease) in accounts payable and accrued | | | |

| | | | |
|---|---|---|---|
| compensation and benefit costs | 179 | 205 | (65) |
| Net change in current and deferred income taxes | 263 | 258 | (359) |
| Other, net | (243) | 204 | (32) |
| Total | 599 | 477 | 613 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | |
| Cost of additions to land, buildings and equipment | (438) | (389) | (470) |
| Proceeds from sales of land, buildings and equipment | 90 | 220 | 41 |
| Proceeds from sale of Constitution Re and Viking | 526 | - | - |
| Purchase of additional interest in Rank Xerox | (972) | - | - |
| Total | (794) | (169) | (429) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Net change in debt | 766 | 550 | 215 |
| Yen financing repayment | - | (116) | - |
| Dividends on common and preferred stock | (389) | (395) | (389) |
| Proceeds from sale of common stock | 139 | 90 | 665 |
| Redemption of preferred stock | (69) | (245) | (6) |
| Dividends to minority shareholders | (86) | (97) | (105) |
| Proceeds received from (returned to) minority shareholders | 20 | (32) | 12 |
| Total | 381 | (245) | 392 |
| EFFECT OF EXCHANGE RATE CHANGES ON CASH | (5) | (78) | (34) |
| CASH PROVIDED (USED) BY CONTINUING OPERATIONS | 181 | (15) | 542 |
| CASH USED BY DISCONTINUED OPERATIONS | (86) | (18) | (476) |
| INCREASE (DECREASE) IN CASH | 95 | (33) | 66 |
| CASH AT BEGINNING OF YEAR | 35 | 68 | 2 |
| CASH AT END OF YEAR | $ 130 | $ 35 | $ 68 |

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



risk attendant to this strategy is the performance of the swap counterparty. We address this risk by arranging swaps exclusively with a diverse group of strong-credit counterparties, regularly monitoring their credit ratings, and determining the replacement cost, if any, of existing transactions.

On an overall worldwide basis, and including the impact of our hedging activities, weighted average interest rates for 1995, 1994 and 1993 approximated 6.5 percent, 7.2 percent and 8.3 percent, respectively.

Our currency and interest rate hedging are typically unaffected by changes in market conditions as forward contracts, options and swaps are normally held to maturity consistent with our objective to lock in currency rates and interest rate spreads on the underlying transactions.

[PHOTO]

Pictured here is Gabor Gagyor, Rank Xerox, Hungary, with the caption "Hungarian mobile telephone customers get their bills much faster since Westel 900 switched to the Xerox DocuPrint to print its high volume of personalized invoices. The payoff for Westel? A very measurable impact on cash flow."

## LIQUIDITY

Our primary sources of liquidity are cash generated from operations and borrowings. The consolidated statements of cash flows detailing changes in our cash balances are on Page 46.

Operating activities, including growth in finance receivables, and after $331 million of restructuring payments in 1995 and $423 in 1994, generated positive cash flows of $599 million, $477 million and $613 million in 1995, 1994 and 1993, respectively.

Investing activities, including proceeds from the sales of Constitution Re Corporation and Viking Insurance Holdings, Inc. and a $972 million payment to

The Rank Organisation Plc, which increased our financial interest in Rank Xerox from 67 percent to 80 percent, resulted in net cash usage of $794 million in 1995 compared with $169 million and $429 million in 1994 and 1993, respectively. The lower level of investing usage in 1994 versus the prior year was primarily due to higher fixed asset sales in 1994 resulting from the information management outsourcing initiative.

Financing activities generated $381 million of pos- itive cash flow in 1995 compared with $245 million of cash usage in 1994 and $392 million of generation in 1993. Financing cash flows include $766 million, $550 million and $215 million of net borrowing in 1995, 1994 and 1993, respectively, excluding foreign currency translation effects and other adjustments. Financing usage in 1994 included repayment of a 1984 yen-denominated financing for $116 million and $184 million used to redeem 8.25 percent preferred stock. Financing generation in 1993 included net proceeds of $580 million from a public offering of common stock.

Overall, Continuing Operations generated net cash of $181 million in 1995, used $15 million in 1994, and generated $542 million in 1993.

Discontinued Operations used $86 million in 1995, $18 million in 1994, and $476 million in 1993.

The combined cash flows of Continuing and Discontinued Operations resulted in a $95 million increase in cash balances in 1995, a $33 million decrease in 1994, and a $66 million increase in 1993.



Insurance and Other Financial Services

In January 1993, we announced our decision to concentrate on the core Document Processing business and our intent to sell or otherwise disengage from the Insurance and Other Financial Services (IOFS) businesses, which is consistent with the strategy that began in 1990. In 1993, we discontinued our Other Financial Services (OFS) business, which included the sale of The Van Kampen Merritt Companies, Inc. and Furman Selz Holding Corporation. During 1995, we sold Xerox Financial Services Life Insurance Company and related companies, which was part of OFS. Also in 1995, we sold two Talegen Holdings, Inc. (Talegen) insurance operating groups, Constitution Re Corporation (CRC) and Viking Insurance Holdings, Inc. (Viking), which are included in the "Dispositioned" insurance line of the Insurance operating results. At year-end 1995, our "Remaining" insurance operating companies consisted of Coregis Group, Inc. (Coregis), Crum & Forster Holdings, Inc. (CFI), Industrial Indemnity Holdings, Inc. (II), Westchester Specialty Group, Inc. (Westchester), The Resolution Group, Inc. (TRG), and three insurance-related service companies. In January 1996, we announced that we had discontinued the Insurance business as a result of the agreements to sell the Remaining insurance companies to investor groups led by Kohlberg Kravis Roberts & Co. (KKR) and existing management.

Status of Insurance

In 1993, Talegen completed a restructuring that established and capitalized seven insurance operating groups as independent legal entities: CRC, Coregis, CFI, II, Viking, Westchester and TRG. The insurance segment now includes Talegen, a holding company of four property-casualty insurance operating groups and three insurance-related service companies; TRG, a former Talegen company, primarily involved in run-off activities and collection of reinsurance; Ridge Reinsurance Limited (Ridge Re) and that portion of the Xerox Financial Services, Inc. (XFSI) headquarters costs and interest expense associated with the insurance business activities.

In connection with the restructuring of Talegen completed in 1993, XFSI agreed that support would be provided in the form of aggregate excess of loss reinsurance. This reinsurance protection is provided through XFSI's single purpose, wholly-owned reinsurance company Ridge Re, established in 1992. XFSI is

obligated to pay annual premium installments of $49 million, plus finance charges, for 10 years, for coverage totaling $1,245 million, net of 15 percent coinsurance. A total of seven annual premium installments remain to be paid as of December 31, 1995. Xerox has guaranteed the payment by XFSI of all such premiums. Xerox has also guaranteed Ridge Re's performance under a $400 million letter of credit facility required to provide security with respect to aggregate excess of loss reinsurance obligations under contracts with the Remaining Talegen insurance companies, TRG and Dispositioned companies.

XFSI may also be required, under certain circumstances, to purchase over time additional redeemable preferred shares up to a maximum of $301 million. In addition, XFSI has guaranteed to the Talegen insurance companies that Ridge Re will meet all of its financial obligations under the foregoing excess of loss reinsurance issued to them.

Sale of Talegen Insurance Companies

In April 1995, CRC, one of the seven insurance operating groups of Talegen, was sold to EXOR America Inc. for a purchase price of $421 million in cash. In July 1995, Viking, another of the seven insurance operating groups of Talegen, was sold to Guaranty National Corporation for approximately $103 million in cash plus future upward price adjustments based on loss reserve development. Both transactions approximated book value. The proceeds of both transactions were primarily used to retire debt.



In January 1996, we announced agreements to sell all of our Remaining insurance units to investor groups led by KKR and senior management of the Remaining companies. The sales, expected to close in the middle of this year, will consist of two concurrent transactions with proceeds totaling $2.7 billion, including the assumption of Talegen debt.

For the four Talegen insurance operating units (Coregis, CFI, II and Westchester) and insurance-related service companies, Xerox will receive approximately $1.25-$1.3 billion in cash, $450-$500 million in preferred stock in a new company formed by the KKR group and the assumption of debt (which amounted to $372 million at December 31, 1995).

For TRG, the unit that manages Talegen's run-off business, Xerox will receive approximately $150 million in cash and $462 million in performance-based instruments issued by another company formed by the KKR group.

The transactions are subject to customary closing conditions, including buyer financing and regulatory approvals. In connection with the announced sales, we recorded a fourth quarter $1,546 million after-tax charge. As a result of the sales of the Talegen units, the insurance segment has been classified as a discontinued operation for all periods presented.

XFSI will continue to provide support in the form of aggregate excess of loss reinsurance agreements issued by Ridge Re and the guarantee of Ridge Re's performance under such agreements. In addition to our guarantee of payment of premiums under such agreements and the $400 million letter of credit facility, Xerox will guaranty Ridge Re's payment and performance obligations under such agreements.

Operating Results

Full year results are summarized below:

Insurance Income Summary

| (In millions) | 1995 | 1994 | 1993 |
|---|---|---|---|
| Talegen Remaining Companies and TRG | $ 146 | $ 138 | $126 |
| Talegen Dispositioned Companies | (3) | 48 | 44 |
| Cessions to Ridge Re | (85) | (35) | - |
| Interest/Other | (158) | (151) | (166) |
| Total before Fourth Quarter Charges | (100) | - | 4 |
| Fourth Quarter Charges: | | | |
| Increased Talegen and TRG Reserves | (176) | - | - |
| Ridge Re Related and Other Accruals | (392) | - | - |
| Net Loss from Operations | (668) | - | 4 |
| Fourth Quarter Charge - Loss on Sale | (978) | - | - |
| Total Insurance | $(1,646) | $ - | $ 4 |

Insurance Results Before Fourth Quarter Charges

Talegen Remaining companies and TRG after-tax income totaled $146 million in 1995, compared with $138 million in 1994 and $126 million in 1993. The improving trend of the Remaining companies and TRG results reflects improved underwriting, higher investment income and higher capital gains (1995 compared with 1994), partially offset by higher interest expense related to the $425 million in debt issued in the fourth quarter of 1994. The decline in Talegen Dispositioned companies income primarily reflects the absence of income in 1995 due to the sales of CRC and Viking. Cessions to Ridge Re totaled $85 million after-tax in 1995, compared with $35 million in 1994. Interest and other charges on an after-tax basis were $158 million in 1995, compared with $151 million in 1994 and $166 million in 1993. These charges primarily include net interest expense.

Fourth Quarter Charges - Talegen and TRG Sales to KKR

In connection with the Talegen and TRG sales, we recorded fourth quarter after-tax charges of $1,546 million in 1995 consisting of a non-cash loss on the sales



of $978 million, including a goodwill write-off of $245 million, reserve strengthening at the Talegen insurance groups and TRG of $176 million and Ridge Re related and other accruals of $392 million to cover all estimated future expenses associated with the excess of loss reinsurance coverage to Talegen and TRG.

Talegen and TRG Reserves

Losses from claims and related loss adjustment expenses (LAE) comprise the majority of costs from providing insurance products. Therefore, unpaid losses and loss expenses are generally the largest liability on a property and casualty insurer's balance sheet. In order to moderate the potential financial impact of unusually severe or frequent losses, insurers often cede (i.e., transfer) through reinsurance mechanisms a portion of their gross policy premiums to reinsurers in exchange for the reinsurer's agreement to share a portion of the covered losses with the insurer. Although the ceding of insurance does not discharge the original insurer from its primary liability to its policyholder, the reinsurance company that accepts the risk assumes an obligation to the original insurer. The ceding insurer retains a contingent liability with respect

to reinsurance ceded to the extent that any reinsuring company might not be able to meet its obligations.

Reserve provisions are established by the insurer to provide for the estimated level of claim payments that will be made under the policies it writes. Over the policy period, as premiums are earned, a portion of the premiums are set aside as gross loss reserves for incurred but not reported (IBNR) losses. IBNR reserves also include amounts to supplement case reserves, when established, to provide for further loss development. In addition, gross reserves are established for internal and external (i.e., allocated) LAE associated with handling the claims inventory. When a claim is reported, case reserves are established on the basis of all pertinent information available at the time. Reinsurance recoverables on gross reserves are recorded for amounts anticipated to be recovered from reinsurers and are determined in a manner consistent with the liabilities associated with the reinsured policies. Net reserves are gross reserves less anticipated reinsurance recoverables on those reserves.

Reinsurance

Talegen has a reinsurance security committee composed of senior management who approve those reinsurers to whom the Remaining insurance companies cede business, and the criteria under which such approvals are granted have become increasingly restrictive over the past several years.

The potential uncollectibility of ceded reinsurance is an industry-wide issue. With respect to the management of recoveries due from reinsurers, the Remaining insurance companies operate within common guidelines for the early identification of potential collection problems and assign these cases to a specialized unit within TRG staffed by "work-out" experts. This unit aggressively pursues collection of reinsurance recoverables through mediation, arbitration and, where necessary, litigation to enforce the Remaining insurance companies contractual right against reinsurers. Nevertheless, periodically, it becomes necessary for management to adjust estimates of potential losses to reflect their ongoing evaluation of developments that affect recoverability, including the financial difficulties that some reinsurers can experience. Based upon the review of financial condition and assessment of other available information, the Remaining insurance companies maintain an allowance for uncollectible amounts due from reinsurers. The remaining balance of reinsurance recoverable is considered to be valid and collectible.

Latent Exposures

Claims resulting from asbestos-related, environmental and other latent exposures have provided unique challenges to the insurance industry. The possibility that these claims would emerge was often not contemplated at the time the policies were written, and traditional actuarial reserving methodologies have not



been useful in accurately estimating ultimate losses. Beginning in 1994 and continuing in 1995, Talegen and certain other companies within the insurance industry developed analytical methods to provide estimates of ultimate losses for such exposures.

Asbestos-related claims, which began to emerge in the 1970s, were the first type of latent exposure to cause significant losses to the insurance industry. In addition to bodily injury claims, asbestos-in-buildings claims have been tendered to certain of the Remaining insurance companies seeking reimbursement for the expense of replacing insulation material and other building components containing asbestos. At this point, sufficient time has elapsed for case law to become reasonably well developed in the asbestos bodily injury claims area. Case law is not as well developed in the asbestos-in-buildings claim area.

Environmental claims were the second major type of such claims to emerge and significantly impact the insurance industry. Environmental claims have

generally been defined by the insurance industry as loss or potential loss related to the alleged contamination of a site from operations on the sites, from waste disposal or from other causes. Inconsistent federal and state case law and uncertainty with respect to Superfund reform have compounded the industry's difficulties in adequately assessing these complex exposures.

Other latent exposures include claims such as repetitive stress, chemical exposure and surgical breast implants, as well as other exposures where the possibility of such claims arising was not contemplated when the policies were written.

As judicial patterns emerge through the appellate process and remove uncertainties surrounding asbestos-related, environmental and other latent exposures, additional liabilities and reinsurance recoverables could arise. Due to the unique complexities and uncertanties related to latent exposure claims, additional information regarding these exposures is provided, although it is the policy of Talegen not to disclose established case reserves on specific claims.

Reserves For The Remaining Insurance Companies

Gross and net unpaid losses and loss expenses for the Remaining insurance companies as of December 31, 1995 and 1994, in total and for each latent exposure area are summarized in the following table:

Unpaid Losses and Loss Expenses For The Remaining Insurance Companies

| (In millions) | Gross Reserves | Net Reserves |
|---|---|---|
| DECEMBER 31, 1995 | | |
| In Total | $8,478 | $5,648 |
| Latent exposure areas/1/: | | |
| Asbestos bodily injury | $ 493 | $ 224 |
| Asbestos-in-buildings | 63 | 2 |
| Environmental | 530 | 253 |
| Other latent exposures | 155 | 46 |
| Total | $1,241 | $ 525 |
| DECEMBER 31, 1994 | | |
| In Total | $7,835 | $5,591 |
| Latent exposure areas/1/: | | |
| Asbestos bodily injury | $ 266 | $ 68 |
| Asbestos-in-buildings | 66 | 3 |
| Environmental | 391 | 127 |
| Other latent exposures | 178 | 60 |
| Total | $ 901 | $ 258 |

/1/ Included are case, IBNR and allocated LAE reserves. Ridge Re recoverable balances are not included in net reserves because the Ridge Re contract is an aggregate excess of loss contract covering all lines of business for the Insurance Companies.

In the fourth quarter of 1995, gross unpaid loss and loss expense reserves for the Remaining insurance companies and XFSI were strengthened by $690 million. After consideration of $349 million ceded to Ridge Re and $70 million ceded to other reinsurers, net unpaid losses and loss expenses were strengthened by a total of $271 million on a pre-tax basis. While cessions to Ridge Re are

beneficial to Talegen, they do not result in a benefit to the consolidated Xerox accounts. Before consideration of Ridge Re, the net strengthening was comprised of an addition of $310 million to latent exposure reserves, $255 million to non-latent exposure reserves and $55 million to uncollectible reinsurance reserves.

In 1995, prior to the strengthening discussed above and exclusive of a settlement between Monsanto Company and Talegen, the Remaining insurance



companies strengthened 1994 and prior accident year net reserves by $151 million, including a $64 million strengthening of uncollectible reinsurance reserves. Those strengthening actions resulted in a cession to Ridge Re of $120 million.

Latent Exposure Reserves

Prior to 1995, the Remaining insurance companies established case and IBNR reserves for asbestos bodily injury and environmental exposures for claims that had been reported. Under that reserving methodology, the IBNR reserves were established primarily to cover adverse development on known claims. Case reserves have been, and continue to be, determined by a specialized claim and legal staff. Beginning in the summer of 1994 and continuing through 1995, Talegen developed methods of analysis and gathered additional data to support IBNR reserves estimates for asbestos bodily injury and environmental claims. During 1995, the methods of analysis were evaluated by internal and external actuarial and claims professionals knowledgeable in the latent exposure field. The following table identifies low and high estimates of the range of potential unpaid costs of asbestos bodily injury and environmental exposures at December 31, 1995:

Low and High Estimates of Gross and Net Unpaid Loss and Allocated LAE
Compared To Carried Reserves of The Remaining Insurance Companies

| | As of December 31, 1995 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Estimated Values | | | | | | |
| | Asbestos Bodily Injury | | Environmental/2/ | | Total | | |
| (In millions) | Low | High | Low | High | Low | High | Carried Reserves/2/ |
| Gross Reserves | $424 | $846 | $251 | $1,072 | $675 | $1,918 | $875 |
| Reinsurance/1/ | 272 | 576 | 71 | 599 | 343 | 1,175 | 406 |
| Net Reserves | $152 | $270 | $180 | $ 473 | $332 | $ 743 | $469 |

/1/ The values presented do not include provisions for uncollectible reinsurance.

/2/ Estimated values and carried reserve information exclude amounts associated with policies expressly written for environmental exposures. As of December 31, 1995, gross and net reserves associated with these exposures are $148 million and $8 million, respectively.

At December 31, 1995, Talegen and the Remaining insurance companies do not expect that liabilities associated with incurred asbestos bodily injury and environmental claims will have a material adverse effect on their future liquidity or financial position. With respect to asbestos-in-buildings and other latent exposures, because of the relatively low amount of cumulative net loss and allocated LAE payments, the reserves established for identified claims and the relatively low number of open claims, Talegen and the Remaining insurance companies also do not expect that liabilities associated with incurred claims in these latent exposure areas will have a material adverse affect on their future liquidity or financial position. However, given the complexity of coverage and other legal issues, and the significant assumptions used in estimating such exposures, actual results could significantly differ from our current estimates.

Discontinued Operations - Other Financial Services and Third-Party and

Real-Estate

Other Financial Services (OFS), which were discontinued in the fourth quarter of 1993, had no after-tax income in the full year 1995 and 1994. The net investment in OFS was $169 million and $232 million at December 31, 1995 and 1994, respectively.



We currently believe that the liquidation of the remaining OFS units will not result in a net loss.

The sale of the business and assets of Shields, a former Furman Selz subsidiary, and Regent, a subsidiary of Shields, to Alliance Capital Management L.P. was completed in March 1994. Under the terms of the Furman Selz sales agreement, the sales proceeds yielded cash of approximately $60 million before settlement of related liabilities.

On June 1, 1995, XFSI completed the sale of Xerox Financial Services Life Insurance Company and related companies (Xerox Life Companies) to a subsidiary of General American Life Insurance Company. After the sale, the Xerox Life Companies names were changed to replace the name "Xerox" in the corporate titles with the name "Cova" (Cova Companies). OakRe Life Insurance Company (OakRe), an XFSI subsidiary formed in 1994, has assumed responsibility for existing Single Premium Deferred Annuity (SPDA) policies issued by Xerox Life's Missouri and California companies via coinsurance agreements (Coinsurance Agreements). The Coinsurance Agreements include a provision for the assumption (at their election) by the Cova Companies, of all of the SPDA policies at the end of their current rate reset periods. A Novation Agreement with an affiliate of the new owner provides for the assumption of the liability under the Coinsurance Agreements for any SPDA policies not so assumed by the Cova Companies. Other policyholders (of Immediate, Whole Life, and Variable annuities as well as a minor amount of SPDAs issued by Xerox Life New York) will continue to be the responsibility of the Cova Companies.

As a result of the Coinsurance Agreements, at December 31, 1995, OakRe retained approximately $2.5 billion of investment portfolio assets (transferred from the Xerox Life Companies) and liabilities related to the reinsured SPDA policies. Interest rates on these policies are fixed and were established upon issuance of the respective policies. Substantially all of these policies will reach their rate reset periods within the next five years and will be assumed under the Agreements as described above. At December 31, 1995, the "maturities" of OakRe's assets and liabilities were not fully matched as the Xerox Life Companies' portfolio was designed to recognize that policy renewals extended liability "maturities," thereby permitting investments of somewhat longer average duration. OakRe's practice is to selectively improve this match over time as market conditions allow. As of December 31, 1995, we estimate that "maturities" are effectively matched for approximately 60% of ultimate policy liabilities.

In connection with the aforementioned sale, XFSI established a $500 million letter of credit and line of credit with a group of banks to support OakRe's coinsurance obligations. The term of this letter of credit is five years and it is unused and available at December 31, 1995. Upon a drawing under the letter of credit, XFSI has the option to cover the drawing in cash or to draw upon the credit line.

In January 1996, we announced an agreement to sell the remaining portion of First Quadrant Corp., an asset management subsidiary of Talegen, to Affiliated Managers Group, Inc. This transaction is expected to close in the first quarter, 1996 and is subject to regulatory approvals and customary closing conditions.

During 1995, sales of real-estate and third-party assets and run-off activity reduced assets associated with these businesses by $58 million to a total of $489 million. Assigned debt totaled $231 million at year-end 1995 unchanged from the year-end 1994 level. The 1995 debt activity primarily

includes an increase related to a tax payment made in 1995 as a result of the 1994 sale of a portion of the direct financing lease portfolio, fully offset by debt reductions from the run-off of assets. We believe that the combination of existing reserves together with run-off profits should adequately provide for any credit losses or losses on disposition.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars In Millions, Except Per-Share Data and Unless Otherwise Indicated)

1 Summary Of Significant Accounting Policies

Basis Of Consolidation. The consolidated financial statements include the accounts of Xerox Corporation and all majority-owned subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated.

Rank Xerox Limited, Rank Xerox Holding BV, Rank Xerox Investment Limited, R-X Holdings Limited and their respective subsidiaries, and the other subsidiaries owned by the Company and The Rank Organisation Plc are referred to as the Rank Xerox Companies.

Investments in which the Company has a 20 to 50 percent ownership interest are accounted for on the equity method.

Effective January 1, 1995, the Company changed the reporting periods of the Rank Xerox Companies and Latin American operations from fiscal years ending October 31 and November 30, respectively, to a calendar year ending December 31. The results of these operations during the period between the end of the 1994 fiscal year and the beginning of the new calendar year (the stub period) amounted to a loss of $21. The loss was charged to retained earnings to avoid reporting more than 12 months results of operations in one year. Accordingly, 1995 worldwide operations include the results for all consolidated subsidiaries beginning January 1, 1995. The cash activity for the stub period is included in Other, net in the consolidated statement of cash flows.

Discontinued Operations. In January 1993, the Company announced its intent to sell or otherwise disengage from its Insurance and Other Financial Services businesses, which is consistent with the strategy that began in 1990. A formal plan for the disposal of Other Financial Services was adopted in 1993, at which time the Other Financial Services businesses were accounted for as discontinued operations. The Insurance business, which now consists of Talegen Holdings, Inc. (Talegen), The Resolution Group, Inc. (TRG), Ridge Reinsurance Limited and headquarters costs and interest expense associated with the insurance activities of Xerox Financial Services, Inc., remained a continuing operation of the Company at that time.

During 1995, two of the seven operating groups of Talegen were sold. In January 1996, the Company announced separate agreements to sell all of the remaining insurance units of Talegen and TRG to investor groups led by Kohlberg Kravis Roberts & Co. and existing management. The sales are subject to customary closing conditions, including buyer financing and regulatory approvals. As a result, the Insurance businesses have been accounted for as a discontinued operation and all prior periods have been restated. See Note 9 on Page 60 for additional information.

The announced sale agreements, on closing, effectively complete the Company's strategy to exit financial services.

Business Segment Information. As a result of the decision to sell its Insurance operations, the Company now operates in a single industry segment that consists of the worldwide development, manufacturing, marketing, financing and servicing of document processing products and services. This business is unitary

from both a company and a customer perspective in that the marketing, financing and servicing of the Company's products represent an integrated document services solution.

Earnings Per Share. Primary earnings per share are based on net income less preferred stock dividend requirements divided by the average common shares outstanding during the period and common equivalent shares related to dilutive stock options and Xerox Canada Inc. exchangeable Class B stock. Fully diluted earnings per share assume full conversion of convertible debt and convertible preferred stock into common stock at the beginning of the year or date of issuance, unless they are antidilutive.

Use Of Estimates. The preparation of financial statements in accordance with generally accepted accounting principles 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.



Goodwill. Goodwill represents the cost of acquired businesses in excess of the net assets purchased and is amortized on a straight-line basis, generally over 40 years. Goodwill is reported net of accumulated amortization and the recoverability of the carrying value is evaluated on a periodic basis. Accumulated amortization at December 31, 1995 and 1994 was $25 and $22, respectively.

[PHOTO]
GARY KABURECK
Corporate Accounting Services

Accounting Changes. In March 1995, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 121 - "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Commencing in 1996, SFAS No. 121 requires companies to review assets for possible impairment and provides guidelines for recognition of impairment losses related to long-lived assets, certain intangibles and assets to be disposed of. The impact of the adoption of SFAS No. 121 will be immaterial.

In October 1995, the FASB issued SFAS No. 123 - "Accounting for Stock-Based Compensation." As allowable by SFAS No. 123, the Company will not recognize compensation cost for stock-based employee compensation arrangements, but rather, commencing in 1996, will disclose in the notes to the consolidated financial statements the impact on net income and earnings per share as if the fair value based compensation cost had been recognized.

Revenue Recognition. Revenues from the sale of equipment under installment contracts and from sales-type leases are recognized at the time of sale or at the inception of the lease, respectively. Associated finance income is earned on an accrual basis under an effective annual yield method. Revenues from equipment under other leases are accounted for by the operating lease method and are recognized over the lease term. Service revenues are derived primarily from maintenance contracts on the Company's equipment sold to customers and are recognized over the term of the contracts. Sales of equipment subject to the Company's operating leases to third-party lease finance companies are recorded as sales at the time the equipment is accepted by the third-party.

Provisions For Losses On Uncollectible Receivables. The provisions for losses on uncollectible trade and finance receivables are determined principally on the basis of past collection experience.

Inventories. Inventories are carried at the lower of average cost or market.

Buildings And Equipment. Buildings and equipment are depreciated over their estimated useful lives. Depreciation is computed using principally the straight-line method. Significant improvements are capitalized; maintenance and repairs are expensed.

Classification Of Commercial Paper And Bank Notes Payable. It is the Company's policy to classify as long-term debt that portion of commercial paper and bank notes payable that is intended to match fund finance receivables due after one year to the extent that it has the ability under its revolving credit agreement to refinance such commercial paper and notes payable on a long-term basis. See Note 10 on Page 64.



Foreign Currency Translation. The functional currency for most foreign operations is the local currency. Net assets are translated at current rates of exchange and income and expense items are translated at the average exchange rate for the year. The resulting translation adjustments are recorded as a separate component of shareholders' equity. The U.S. dollar is used as the functional currency for the Company's subsidiaries, primarily those in Latin America, which conduct their business in U.S. dollars or operate in hyperinflationary economies. A combination of current and historical exchange rates are used in remeasuring the local currency transactions of these subsidiaries and the resulting exchange adjustments are included in income. Aggregate foreign currency losses were $18, $136 and $174 in 1995, 1994 and 1993, respectively, and are included in Other, net in the consolidated statements of income. As more fully discussed in the accompanying Financial Review on Page 38 within the discussion of Other expenses, net, the decline in currency losses in 1995 from prior years is primarily due to the relative stabilization of exchange rates in Brazil commencing after July 1, 1994.

## 2 Acquisition

On February 28, 1995, the Company paid The Rank Organisation Plc (RO) (Pounds)620 million, or approximately $972, for 40 percent of RO's financial interest in the Rank Xerox Companies. The transaction increased the Company's financial interest in the Rank Xerox Companies to 80 percent from 67 percent. The Company's additional interest in the operating results of the Rank Xerox Companies is included in the consolidated statement of income from the date of acquisition. Based on the allocation of the purchase price, this transaction resulted in goodwill of $574 (including transaction costs), a decline in minorities' interests in equity of subsidiaries of approximately $400 and an increase in long-term debt of $972.

## 3 1993 Special Charges, Net

In 1993, the Company recorded special charges which aggregated $1,373 and included the following pre-tax amounts: $1,195 related to a restructuring of operations and $278 related to litigation settlements, partially offset by $100 in reduced performance-based employee profit sharing. These special charges resulted in an after-tax charge of $813 or $7.96 per share.

The restructuring program announced in December 1993 is a worldwide action aimed at significantly reducing the Company's cost base and at improving productivity.

The $1,195 pre-tax provision consisted of the following: $843 related to severance pay and other employee separation benefits; $258 related to lease cancellation and other facilities rationalization and site consolidation costs; and $94 for the write-off or write-down of various assets in certain non-strategic businesses the Company will exit and other costs directly related to the restructuring program. Approximately 70 percent of this provision related to the Company's domestic operations.

The Company's objectives were to reduce its worldwide work force by more than

10,000 employees and to close or consolidate a number of facilities.

[PHOTO]

ALLEN VASAN
Executive
Assistant
Operations



A summary of the original reserve and charges through December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Net charges to restructuring reserve | $370* | $430 | $ - |
| Reserve balance: | | | |
| Current | $298 | $429 | $ 395 |
| Non-current | 97 | 336 | 800 |
| Total reserve balance | $395 | $765 | $1,195 |

* Includes $30 charged to the reserve during the stub period.

Management believes that the aggregate reserve balance of $395 at December 31, 1995 is adequate for completion of the restructuring program.

4 Finance Receivables, Net

Finance receivables represent installment sales and sales-type leases resulting from the marketing of the Company's business equipment products. These receivables generally mature over two to five years and are typically collateralized by a security interest in the underlying assets. The components of finance receivables, net at December 31, 1995, 1994 and 1993 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Gross receivables | $12,721 | $12,135 | $11,119 |
| Unearned income | (2,207) | (2,074) | (2,032) |
| Unguaranteed residual values | 283 | 206 | 165 |
| Allowance for doubtful accounts | (322) | (319) | (300) |
| Finance receivables, net | 10,475 | 9,948 | 8,952 |
| Less current portion | 4,069 | 3,910 | 3,358 |
| Amounts due after one year, net | $ 6,406 | $ 6,038 | $ 5,594 |

Contractual maturities of the Company's gross finance receivables subsequent to December 31, 1995 follow:

| 1996 | 1997 | 1998 | 1999 | 2000 | Thereafter |
|---|---|---|---|---|---|
| $5,138 | $ 3,427 | $ 2,338 | $ 1,284 | $ 459 | $ 75 |

Experience has shown that a portion of these finance receivables will be prepaid prior to maturity. Accordingly, the preceding schedule of contractual maturities should not be considered a forecast of future cash collections.

[PHOTO]

Rita Overal
Rank Xerox, UK

## 5 Inventories

The components of inventories at December 31, 1995, 1994 and 1993 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Finished goods | $1,642 | $1,458 | $1,421 |
| Work in process | 88 | 88 | 80 |
| Raw materials | 289 | 268 | 297 |
| Equipment on operating leases, net | 627 | 480 | 364 |
| Inventories | $2,646 | $2,294 | $2,162 |

Equipment on operating leases consists of the Company's business equipment products which are rented to customers and are depreciated to estimated residual value. Depreciable lives vary from two to four years. The Company's business equipment operating lease terms vary, generally from 12 to 36 months. Accumulated depreciation on equipment on operating leases for the years ended December 31, 1995, 1994 and 1993 amounted to $1,065, $824 and $790, respectively. Minimum future rental revenues on the remaining non-cancelable operating leases with original terms of one year or longer are:

| 1996 | 1997 | 1998 | Thereafter |
|---|---|---|---|
| $439 | $206 | $107 | $43 |

Total contingent rentals, principally usage charges in excess of minimum allowances relating to operating leases, for the years ended December 31, 1995, 1994 and 1993 amounted to $190, $197 and $217, respectively.



## 6 Land, Buildings And Equipment, Net

The components of land, buildings and equipment at December 31, 1995, 1994 and 1993 follow:

| | Estimated Useful Lives (Years) | 1995 | 1994 | 1993 |
|---|---|---|---|---|
| Land | | $ 85 | $ 87 | $ 83 |
| Buildings and building equipment | 20 to 40 | 941 | 876 | 824 |
| Leasehold improvements | Lease term | 344 | 339 | 322 |
| Plant machinery | 4 to 12 | 1,892 | 1,843 | 1,732 |
| Office furniture and equipment | 3 to 10 | 1,157 | 1,245 | 1,576 |
| Other | 3 to 20 | 199 | 139 | 171 |
| Construction in progress | | 231 | 227 | 277 |
| Subtotal | | 4,849 | 4,756 | 4,985 |
| Less accumulated depreciation | | 2,757 | 2,648 | 2,766 |
| Land, buildings and equipment, net | | $2,092 | $2,108 | $2,219 |

The Company leases certain land, buildings and equipment, substantially all of which are accounted for as operating leases. Total rent expense under operating leases for the years ended December 31, 1995, 1994 and 1993 amounted to $425, $502 and $538, respectively. Future minimum operating lease commitments that have remaining non-cancelable lease terms in excess of one year at December 31, 1995 follow:

| 1996 | 1997 | 1998 | 1999 | 2000 | Thereafter |
|---|---|---|---|---|---|
| $344 | $230 | $179 | $140 | $111 | $475 |

In certain circumstances, the Company subleases space not currently required in operations. Future minimum sublease income under leases with non-cancelable terms in excess of one year amounted to $56 at December 31, 1995.

In 1994, the Company awarded a contract to Electronic Data Systems Corp. (EDS) to operate the Company's worldwide data processing and telecommunications network. Minimum payments due EDS under the contract for each of the next five years follow:

| 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|
| $349 | $325 | $289 | $250 | $222 |

These minimum payments will be amended over time to reflect the transfer to EDS of responsibility for the management of any new data processing applications.

## 7 Investments In Affiliates, At Equity

Investments in corporate joint ventures and other companies in which the Company has a 20 to 50 percent ownership interest at December 31, 1995, 1994 and 1993 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Fuji Xerox | $1,223 | $1,183 | $1,004 |
| Other investments | 105 | 95 | 90 |
| Investments in affiliates, at equity | $1,328 | $1,278 | $1,094 |

Rank Xerox Limited, a consolidated subsidiary of the Company, owns 50 percent of the outstanding stock of Fuji Xerox, a corporate joint venture with Fuji Photo Film Co., Ltd. Fuji Xerox is headquartered in Tokyo and operates throughout the Far East (except China). Condensed financial data of Fuji Xerox for its last three fiscal years follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| SUMMARY OF OPERATIONS | | | |
| Revenues | $8,500 | $7,235 | $6,259 |
| Costs and expenses | 7,989 | 6,829 | 5,915 |
| Income before income taxes | 511 | 406 | 344 |
| Income taxes | 287 | 235 | 195 |
| Net income | $ 224 | $ 171 | $ 149 |
| Rank Xerox' equity in net income | $ 112 | $ 86 | $ 75 |
| Xerox' equity in net income | $ 88 | $ 57 | $ 50 |
| BALANCE SHEET DATA | | | |
| ASSETS | | | |

| | | | |
|---|---|---|---|
| Current assets | $3,518 | $3,428 | $3,175 |
| Non-current assets | 3,085 | 3,038 | 2,573 |
| Total assets | $6,603 | $6,466 | $5,748 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | |
| Current liabilities | $2,675 | $2,567 | $2,276 |
| Long-term debt | 594 | 658 | 794 |
| Other non-current liabilities | 884 | 871 | 668 |
| Shareholders' equity | 2,450 | 2,370 | 2,010 |
| Total liabilities and shareholders' equity | $6,603 | $6,466 | $5,748 |

8 Geographic Area Data

Revenues and assets of the Rank Xerox Companies are substantially attributable to European operations; their consolidated operations in Africa, Asia and the Middle East together comprise less than two percent of the Company's consolidated amounts. The Other Areas classification includes operations principally in Latin America and Canada.



Intercompany revenues are generally based on manufacturing cost plus a markup to recover other operating costs and to provide a profit margin to the selling company.

Geographic area data for the Company's continuing operations follow:

| | Year ended December 31, | | |
|---|---|---|---|
| | 1995 | 1994 | 1993 |
| Revenues from unrelated entities: | | | |
| United States | $ 8,068 | $ 7,822 | $ 7,238 |
| Rank Xerox Companies | 5,496 | 4,633 | 4,479 |
| Other Areas | 3,047 | 2,633 | 2,512 |
| Total | $16,611 | $15,088 | $14,229 |
| Intercompany revenues: | | | |
| United States | $ 1,376 | $ 1,291 | $ 1,104 |
| Rank Xerox Companies | 226 | 262 | 216 |
| Other Areas | 463 | 362 | 353 |
| Total | $ 2,065 | $ 1,915 | $ 1,673 |
| Total revenues: | | | |
| United States | $ 9,444 | $ 9,113 | $ 8,342 |
| Rank Xerox Companies | 5,722 | 4,895 | 4,695 |
| Other Areas | 3,510 | 2,995 | 2,865 |
| Less intercompany revenues | (2,065) | (1,915) | (1,673) |
| Total | $16,611 | $15,088 | $14,229 |
| Net income (loss) (before intercompany eliminations): | | | |
| United States | $ 288 | $ 379 | $ (371) |
| Rank Xerox Companies | 409 | 218 | (43) |
| Other Areas | 446 | 250 | 190 |
| Total* | $ 1,143 | $ 847 | $ (224) |

| | | | |
|---|---|---|---|
| Net income (loss) (after intercompany eliminations): | | | |
| United States | $ 418 | $ 386 | $ (334) |
| Rank Xerox Companies | 408 | 215 | (47) |
| Other Areas | 348 | 193 | 188 |
| Total* | $ 1,174 | $ 794 | $ (193) |
| Assets: | | | |
| United States | $ 9,876 | $ 9,133 | $ 8,966 |
| Rank Xerox Companies | 7,566 | 7,171 | 6,349 |
| Other Areas | 3,717 | 3,070 | 2,843 |
| Subtotal | 21,159 | 19,374 | 18,158 |
| Investment in discontinued operations | 4,810 | 7,904 | 8,841 |
| Total | $25,969 | $27,278 | $26,999 |

* The 1993 special charges reduced net income by $813. On a geographic basis, this charge was incurred as follows: $605-United States; $147-Rank Xerox Companies; and $61-Other Areas.

[PHOTO]

DAVID LEANING
Rank Xerox
Accounting

## 9 Discontinued Operations

In January 1993, the Company announced its intent to sell or otherwise disengage from its Insurance and Other Financial Services (IOFS) businesses, which is consistent with the strategy that began in 1990. As more fully discussed below and in the accompanying Financial Review on Page 48 within the section entitled Sale of Talegen Insurance Companies, the Company has discontinued its Insurance business as a result of the announced sales of the remaining Talegen insurance operating groups and The Resolution Group, Inc. (TRG). In 1993, the Company discontinued its Other Financial Services businesses and in 1990 discontinued its Real-Estate and Third-Party Financing businesses.

Insurance. The Insurance segment includes Talegen Holdings, Inc. (Talegen), a holding company with originally seven property-casualty insurance operating groups; TRG; Ridge Reinsurance Limited (Ridge Re); and headquarters costs and interest expense associated with the insurance activities of Xerox Financial Services, Inc. (XFSI). In 1993, Talegen completed a restructuring which established and capitalized seven insurance operating groups as independent legal entities: Constitution Re Corporation (CRC), Coregis, Crum & Forster Insurance, Industrial Indemnity, TRG, Viking Insurance Holdings, Inc. (Viking) and Westchester Specialty Group. TRG is the unit that manages Talegen's run-off businesses.



In connection with the restructuring of Talegen, XFSI agreed that support would be provided in the form of aggregate excess of loss reinsurance. This reinsurance protection is provided through XFSI's single purpose, wholly-owned reinsurance company Ridge Re, which was established in 1992. Commencing in 1993, XFSI is obligated to pay annual premium installments of $49, plus finance charges, for 10 years, for coverage totaling $1,245, net of 15 percent coinsurance. The XFSI premium payments have been guaranteed by the Company. The

Company has also guaranteed Ridge Re's performance under a $400 letter of credit facility required to provide security with respect to aggregate excess of loss reinsurance obligations.

XFSI may also be required, under certain circumstances, to purchase up to $301 in redeemable preferred stock of Ridge Re. In addition, XFSI has guaranteed to the Talegen insurance companies that Ridge Re will meet all of its financial obligations under all of the foregoing excess of loss reinsurance issued to them.

[PHOTO]

MARTIN DURRIG
Rank Xerox

Sale of Talegen Insurance Operating Groups. In April 1995, CRC, one of the seven insurance operating groups of Talegen, was sold to EXOR America Inc. for a purchase price of $421 in cash, which approximated book value.

In July 1995, Viking, another of the seven insurance operating groups of Talegen, was sold to Guaranty National Corporation for approximately $103 in cash plus future upward price adjustments based on loss reserve development. The transaction approximated book value.

The proceeds of both transactions were used to retire debt. Collectively, CRC and Viking had $680 of revenue in 1994, the last full year of ownership by the Company.

In January 1996, the Company announced separate agreements to sell all of the remaining insurance operating groups of Talegen and TRG, for approximately $2.7 billion to investor groups (the Buyer) led by Kohlberg Kravis Roberts & Co. and existing management. The transactions will consist of $1,400-$1,450 in cash, $450-$500 in preferred stock, $462 in a performance-based instrument and the assumption of debt, which amounted to $372 at December 31, 1995. The agreements, which are expected to close mid-1996, are subject to customary closing conditions, including buyer financing and regulatory approvals.

The Company will receive $450-$500 in face value of twenty-year Trust Originated Preferred Securities (TOPrS) in connection with the sale of the remaining Talegen units other than TRG. TOPrS are a tax-deductible preferred stock issued by a trust established by the Buyer's holding company. Dividends on the TOPrS may be deferred with a concurrent increase in the value of the TOPrS for the first seven years. Subsequently, dividends must be paid in cash. The TOPrS may be redeemed from the Company at face value, plus accrued dividends, before maturity and the Company can sell the TOPrS after one year. The TOPrS mature in 20 years and will pay a dividend rate equal to 499 basis points over the published long-term Applicable Federal Rate at the date of closing. At December 31, 1995, the TOPrS dividend rate would have been 11.20 percent.

The Company will participate in the future cash flows of TRG via a performance-based instrument carried at $462. The recovery of this instrument is dependent upon the sufficiency of TRG's available cash flows, as defined. Based on current forecasts at December 31, 1995, the Company expects to realize $462 for this instrument. However, ultimate realization may be greater or less than this amount.



The Company will continue to provide support in the form of aggregate excess of loss reinsurance to the Talegen units through Ridge Re. In addition, XFSI is obligated to pay the seven remaining premium installments of $49 plus finance charges. In addition to its guarantee of payment of premiums under such agreements and the $400 letter of credit facility, the Company will guarantee, upon closing, that Ridge Re will meet all of its payment and performance obligations under the foregoing excess of loss reinsurance agreements. At December 31, 1995, Ridge Re has accrued approximately $750 of the $1,245 excess

of loss reinsurance coverage estimated to be required based on actuarial projections.

In connection with the announced sale, the Company recorded a $1,546 loss on disposal of the remaining Talegen insurance operating groups and TRG. The loss on disposal, recorded in the fourth quarter of 1995, is composed of the following:

| | |
|---|---|
| Loss on sale | $ 978 |
| Increased Talegen and TRG reserves, net of income tax benefit of $95 | 176 |
| Ridge Re related and other accruals, net of tax benefit of $195 | 392 |
| Total after-tax loss | $1,546 |

As a result of these sales, the Insurance businesses have been classified as discontinued operations for all periods presented.

Insurance Financial Information. Summarized operating results of Insurance for the three years ended December 31, 1995 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Revenues | $ 2,352 | $2,749 | $2,809 |
| Net income (loss) from operations* | $ (668) | $ -- | $ 4 |
| Loss on disposal | (978) | | |
| Income (loss) from Insurance | $(1,646) | $ -- | $ 4 |

* The 1995 amount includes $568 of after-tax reserves recorded during the fourth quarter.

The net assets at December 31, 1995, 1994 and 1993 of the Insurance businesses included in the Company's consolidated balance sheets as discontinued operations are summarized as follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Insurance Assets | | | |
| Investments | $ 7,871 | $ 8,384 | $ 8,344 |
| Reinsurance recoverable | 2,616 | 3,063 | 3,835 |
| Premiums and other receivables | 1,191 | 1,276 | 1,443 |
| Deferred taxes and other assets | 1,450 | 1,743 | 1,796 |
| Total Insurance assets | $13,128 | $14,466 | $15,418 |
| Insurance Liabilities | | | |
| Unpaid losses and loss expenses | $ 8,761 | $ 8,809 | $ 9,684 |
| Unearned income | 859 | 1,066 | 1,077 |
| Notes payable | 372 | 425 | -- |
| Other liabilities | 1,513 | 954 | 990 |
| Total Insurance liabilities | 11,505 | 11,254 | 11,751 |

| | | | |
|---|---|---|---|
| Investment in Insurance, net | $ 1,623 | $ 3,212 | $ 3,667 |

At December 31, 1995 and 1994, intercompany transactions aggregating approximately $465 and $522, respectively, have been included as assets in Investment in Discontinued Operations in the consolidated balance sheets. The corresponding obligations are included in Deferred Taxes and Other Liabilities in the consolidated balance sheets and represent funding commitments by XFSI guaranteed by the Company. Substantially all of these funding commitments will be paid at the time the Talegen sale is completed.

[PHOTO]

TAMMY POWER
Olympic Document Printing Specialist



The Investments caption consists mainly of short-term investments as shown below. At December 31, 1995, approximately 97 percent of the fixed maturity investments are investment grade securities. The amortized cost and fair value of the investment portfolio at December 31, 1995 follow:

| | Amortized Cost | Fair Value |
|---|---|---|
| Fixed maturities | $1,035 | $1,035 |
| Equity securities | 8 | 7 |
| Short-term investments | 6,829 | 6,829 |
| Total investments | $7,872 | $7,871 |

Activity related to unpaid losses and loss expenses for the three years ended December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| UNPAID LOSSES AND LOSS EXPENSES | | | |
| Gross unpaid losses and loss expenses, January 1 | $8,809 | $9,684 | $10,657 |
| Reinsurance recoverable | 2,391 | 2,935 | 3,788 |
| Net unpaid losses and loss expenses, January 1 | 6,418 | 6,749 | 6,869 |
| Incurred related to: | | | |
| Current year accident losses | 1,461 | 1,748 | 1,795 |
| Prior year accident losses | 570 | 21 | 41 |
| Total incurred | 2,031 | 1,769 | 1,836 |
| Paid related to: | | | |
| Current year accident losses | 427 | 486 | 495 |
| Prior year accident losses | 1,203 | 1,577 | 1,317 |

| | | | |
|---|---|---|---|
| Total paid | 1,630 | 2,063 | 1,812 |
| Sale of CRC and Viking | (769) | -- | -- |
| Other adjustments | 421 | (37) | (144) |
| Net unpaid losses and loss expenses, December 31 | 6,471 | 6,418 | 6,749 |
| Reinsurance recoverable | 2,290 | 2,391 | 2,935 |
| Gross unpaid losses and loss expenses, December 31 | $8,761 | $8,809 | $ 9,684 |

The increase in 1995 incurred prior year accident losses compared to prior years relates to reserve strengthening which was either identified by the Company or negotiated in conjunction with the sale of Talegen. This includes the recording of future Ridge Re loss development.

Other Financial Services. In 1993, the Company discontinued its Other Financial Services (OFS) segment, which was composed of The Van Kampen Merritt Companies, Inc. (VKM), Furman Selz Holding Corporation (Furman Selz), Xerox Financial Services Life Insurance Company (Xerox Life) and First Quadrant Corp.

In 1993, the Company sold VKM for approximately $360, which resulted in pre- and after-tax gains of approximately $101 and $62, respectively. The proceeds were used to retire debt.

Also in 1993, the Company sold Furman Selz for $99 and the proceeds were used to retire debt. The gain on the sale was immaterial.

On June 1, 1995, the Company completed the sale of Xerox Life for approximately $104 before settlement costs and capital funding of OakRe Life Insurance Company (OakRe), a single-purpose XFSI subsidiary formed in 1994. OakRe assumed responsibility for the Single Premium Deferred Annuity (SPDA) policies issued by Xerox Life's Missouri and California companies via coinsurance agreements. As a result of these coinsurance agreements, at December 31, 1995, the Company has retained on its consolidated balance sheet approximately $2.5 billion of investment portfolio assets and reinsurance reserves related to its former SPDA policies. These amounts will decrease through the year 2000 as the SPDA policies are either terminated by the policyholder or renewed and transferred to the buyer.

In connection with the aforementioned sale, XFSI established a $500 letter of credit and line of credit with a group of banks to support OakRe's coinsurance obligations. The term of this letter of credit is five years and it is unused and available at December 31, 1995. Upon a drawing under the letter of credit, XFSI has the option to cover the drawing in cash or to draw upon the credit line.

In January 1996, the Company announced an agreement to sell the remaining portion of First Quadrant Corp. This transaction is expected to close in the first quarter of 1996 and is subject to regulatory approvals and customary closing conditions.



[PHOTO]

LINDA YOSHINO
Business Strategy & Planning

Real-Estate And Third-Party Financing. During the last five years, the Company made substantial progress in disengaging from the Real-Estate and Third-Party Financing businesses that were discontinued in 1990. During the three

years ended December 31, 1995, the Company received net cash proceeds of $614 ($64 in 1995, $259 in 1994 and $291 in 1993) from the sale of individual assets and from run-off collection activities. The amounts received were consistent with the Company's estimates in the disposal plan and were used primarily to retire debt.

The remaining assets primarily represent direct financing leases, many with long-duration contractual maturities and unique tax attributes. Accordingly, the Company expects that the wind-down of the portfolio will be slower during 1996 and in future years, as it was in 1995, compared with prior years.

Total Discontinued Operations. The consolidated financial statements have been restated, as appropriate, to segregate the effect of the discontinued operations. Debt has been assigned to discontinued operations based on historical levels assigned to the businesses when they were continuing operations adjusted for subsequent paydowns. Interest expense thereon is primarily determined based on annual average domestic borrowing costs of the Company. Assigned interest expense for the discontinued businesses for the years ended December 31, 1995, 1994 and 1993 was $255, $246 and $291, respectively.

Summarized information of discontinued operations for the three years ended December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| SUMMARY OF OPERATIONS | | | |
| Income (loss) before income taxes | $(1,025) | $ (44) | $ (29) |
| Income tax benefits | 357 | 44 | 34 |
| Gain (loss) on disposal | (978) | -- | 62 |
| Net income (loss) | $(1,646) | $ -- | $ 67 |
| BALANCE SHEET DATA | | | |
| ASSETS | | | |
| INSURANCE | | | |
| Investment, net | $ 1,623 | $3,212 | $3,667 |
| OTHER FINANCIAL SERVICES | | | |
| Investments | 2,508 | 3,604 | 3,832 |
| Other assets, net | 190 | 541 | 523 |
| OFS assets | 2,698 | 4,145 | 4,355 |
| REAL-ESTATE AND THIRD-PARTY FINANCING | | | |
| Gross finance receivables | 472 | 538 | 841 |
| Unearned income and other | 17 | 9 | (22) |
| Investment, net | 489 | 547 | 819 |
| Investment in Discontinued Operations | $ 4,810 | $7,904 | $8,841 |
| LIABILITIES | | | |
| OFS policyholders' deposits | $ 2,528 | $3,576 | $3,716 |
| Other OFS liabilities | 1 | 337 | 395 |
| Assigned debt | 281 | 281 | 474 |
| Discontinued Operations Liabilities | $ 2,810 | $4,194 | $4,585 |

At December 31, 1995 and 1994, approximately $2.3 billion and $2.6 billion, respectively, of third-party indebtedness assigned to the Company's Insurance operations is included in the consolidated balance sheet caption Long-Term Debt.

The Company's net investment in discontinued operations is approximately $2,000 and $3,710 at December 31, 1995 and 1994, respectively. The Company believes that the liquidation of the remaining net discontinued assets will not result in a net loss.



10 Debt

Short-Term Debt. Short-term borrowings data of the Company at December 31, 1995 and 1994 follow:

| | Weighted average interest rates at December 31, 1995 | 1995 | 1994 |
|---|---|---|---|
| Bank notes payable | 7.72% | $ 884 | $ 235 |
| Foreign commercial paper | -- | -- | 1,024 |
| Total short-term debt | | 884 | 1,259 |
| Current maturities of long-term debt | | 2,381 | 1,900 |
| Total | | $3,265 | $3,159 |

Bank notes payable generally represent foreign currency denominated borrowings of non-U.S. subsidiaries.

Long-Term Debt. A summary of long-term debt, by final maturity date, at December 31, 1995 and 1994 follows:

| | Weighted average interest rates at December 31, 1995 | 1995 | 1994 |
|---|---|---|---|
| U.S. OPERATIONS: | | | |
| XEROX CORPORATION (PARENT COMPANY) | | | |
| Guaranteed ESOP notes due 1999-2004 | 7.62% | $ 547 | $ 596 |
| Notes due 1995 | -- | -- | 350 |
| Notes due 1996 | 8.77 | 420 | 100 |
| Notes due 1997 | 9.63 | 200 | 200 |
| Notes due 1999 | 5.21 | 484 | 738 |
| Notes due 2000 | 7.33 | 600 | 300 |
| Notes due 2001 | 7.39 | 62 | 62 |
| Notes due 2002 | 8.13 | 200 | 200 |
| Notes due 2004 | 7.15 | 200 | 225 |
| Notes due 2005 | 7.15 | 50 | -- |
| Notes due 2006 | -- | -- | 45 |
| Notes due 2007 | 7.38 | 25 | -- |
| Other debt due 1995-2014 | 8.24 | 97 | 97 |
| Capital lease obligations | 5.60 | 5 | 7 |
| Subtotal | | 2,890 | 2,920 |
| XEROX FINANCIAL SERVICES, INC. (XFSI) | | | |
| XEROX CREDIT CORPORATION | | | |
| Notes due 1995 | -- | -- | 400 |
| Notes due 1996 | 8.39 | 850 | 670 |
| Notes due 1997 | 5.75 | 677 | 347 |
| Notes due 1998 | 6.50 | 220 | -- |
| Notes due 1999 | 10.00 | 150 | 150 |

| | | | |
|---|---|---|---|
| Notes due 2000 | 7.13 | 303 | -- |
| Floating rate notes due 2048 | 5.80 | 61 | 61 |
| Other debt due 1996 | 10.00 | 18 | 19 |
| Subtotal | | 2,279 | 1,647 |
| OTHER XFSI DEBT | | | |
| XFSI Notes due 1995-1996 | 9.05 | 135 | 310 |
| Subtotal | | 2,414 | 1,957 |
| TOTAL U.S. OPERATIONS | | $5,304 | $ 4,877 |

| | Weighted average interest rates at December 31, 1995 | 1995 | 1994 |
|---|---|---|---|
| INTERNATIONAL OPERATIONS: | | | |
| INTERNATIONAL MARKETING AND FINANCE SUBSIDIARIES | | | |
| Various obligations, payable in: | | | |
| Canadian dollars due 1995-2007 | 10.68% | $ 263 | $ 265 |
| Dutch guilders due 1995-1999 | 6.48 | 216 | 187 |
| French francs due 1995-1998 | 7.79 | 76 | 76 |
| German marks due 1995-1999 | 6.60 | 280 | 297 |
| Pounds sterling due 1995-1997 | 7.69 | 283 | 353 |
| Swiss francs due 1995-1999 | 5.50 | 81 | 96 |
| Italian lira due 1995-1997 | 11.08 | 99 | 81 |
| U.S. dollars due 1995-1999 | 6.56 | 268 | 220 |
| Other currencies due 1995-1999 | 8.22 | 363 | 314 |
| Capital lease obligations | 8.94 | 9 | 14 |
| TOTAL INTERNATIONAL OPERATIONS | | 1,938 | 1,903 |
| OTHER BORROWINGS DEEMED LONG-TERM | | 3,287 | 2,475 |
| Subtotal | | 10,529 | 9,255 |
| Less current maturities | | 2,381 | 1,900 |
| TOTAL LONG-TERM DEBT | | $8,148 | $7,355 |

Consolidated Long-Term Debt Maturities. Payments due on long-term debt for the next five years follow:

| 1996 | 1997 | 1998 | 1999 | 2000 | Thereafter |
|---|---|---|---|---|---|
| $2,381 | $1,431 | $ 543 | $1,076 | $ 704 | $1,107 |

These payments do not include amounts relating to domestic commercial paper and foreign bank notes payable which have been classified as long-term debt under the caption Other borrowings deemed long-term. These borrowings are classified as long-term because the Company has the intent to refinance them on a long-term basis, and the ability to do so under its revolving credit agreement.

Certain of the Company's debt agreements allow the Company to redeem outstanding debt prior to scheduled maturity. Outstanding debt issues with these call features are classified in the preceding five-year maturity table in accordance with management's current expectations. The actual decision as to early redemption will be made at the time the early redemption option becomes exercisable and will be based on prevailing economic and business conditions.



Lines Of Credit. The Company's domestic operations have a revolving credit agreement totaling $5.0 billion with a group of banks, which expires in 2000. This agreement is unused and is available to back the Company's domestic commercial paper borrowings, which amounted to $2.8 billion and $2.4 billion at December 31, 1995 and 1994, respectively. In addition, the Company's foreign subsidiaries had unused committed long-term lines of credit aggregating $1.7

billion in various currencies at prevailing interest rates that are used to back short-term indebtedness.

[PHOTO]

NAVIN CHHEDA
North American
Capital Markets

Match Funding Of Finance Receivables And Indebtedness. The Company employs a match funding policy for customer financing assets and related liabilities. Under this policy, which is more fully discussed in the accompanying Financial Review on Page 45, the interest and currency characteristics of the indebtedness are, in most cases, matched to the interest and currency characteristics of the finance receivables. At December 31, 1995, these operations had approximately $10.7 billion of net finance receivables, which will service approximately $8.8 billion of assigned short- and long-term debt, including $0.3 billion of debt assigned to discontinued third-party financing businesses.

Guarantees. At December 31, 1995, the Company has guaranteed $506 of indebtedness of its Latin American subsidiaries and the borrowings of its ESOP.

Interest. Including amounts relating to debt assigned to discontinued operations, interest paid by the Company on its short- and long-term debt amounted to $705, $751 and $860, respectively, for the years ended December 31, 1995, 1994 and 1993.

Total Short-And Long-Term Debt. The Company's total indebtedness, excluding the direct indebtedness of Talegen, at December 31, 1995 and 1994 is reflected in the consolidated balance sheet captions as follows:

| | 1995 | 1994 |
|---|---|---|
| Short-term debt and current portion of long-term debt | 3,265 | $ 3,159 |
| Long-term debt | 7,867 | 7,074 |
| Discontinued operations liabilities -- policyholders' deposits and other | 281 | 281 |
| Total debt | $11,413 | $10,514 |

A summary of changes in consolidated indebtedness for the three years ended December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Increase (decrease) in short-term debt, net | $ 94 | $ (146) | $ (451) |
| Proceeds from long-term debt | 3,169 | 2,058 | 1,866 |
| Principal payments on long-term debt | (2,497) | (1,555) | (1,784) |
| Subtotal | 766 | 357 | (369) |
| Less discontinued operations | -- | (193) | (584) |
| Total change in debt of continuing operations | $ 766 | $ 550 | $ 215 |

11 Financial Instruments

Derivative Financial Instruments. Certain financial instruments with off-balance-sheet risk have been entered into by the Company to manage its interest rate and foreign currency exposures. These instruments are held solely for hedging purposes and include interest rate swap agreements, forward-foreign exchange contracts and foreign currency swap agreements. The Company does not

enter into derivative instrument transactions for trading or other speculative purposes.



The Company typically enters into simple, unleveraged derivative transactions which, by their nature, have low credit and market risk. The Company's policies on the use of derivative instruments prescribe an investment grade counterparty credit floor and at least quarterly monitoring of market risk on a counterparty-by-counterparty basis. The Company utilizes numerous counterparties to ensure that there are no significant concentrations of credit risk with any individual counterparty or groups of counterparties. Based upon its ongoing evaluation of the replacement cost of its derivative transactions and counterparty creditworthiness, the Company considers the risk of credit default significantly affecting its financial position or results of operations to be remote.

The Company employs the use of hedges to reduce the risks that rapidly changing market conditions may have on the underlying transactions. Typically, the Company's currency and interest rate hedging activities are not affected by changes in market conditions as forward contracts and swaps are arranged and normally held to maturity in order to lock in currency rates and interest spreads related to underlying transactions.

None of the Company's hedging activities involve exchange traded instruments.

Interest Rate Swaps. The Company enters into interest rate swap agreements to manage interest rate exposure. An interest rate swap is an agreement to exchange interest rate payment streams based on a notional principal amount. The Company follows settlement accounting principles for interest rate swaps whereby the net interest rate differentials to be paid or received are recorded currently as adjustments to interest expense.

Virtually all customer financing assets earn fixed rates of interest. Accordingly, through the use of interest rate swaps in conjunction with the contractual maturity terms of outstanding debt, the Company "locks in" an interest spread by arranging fixed-rate interest obligations with maturities similar to the underlying assets. Additionally, customer financing assets are consistently funded with liabilities denominated in the same currency. The Company refers to the effect of these conservative practices as "match funding" its customer financing assets. This practice effectively eliminates the risk of a major decline in interest margins resulting from adverse changes in the interest rate environment. Conversely, this practice does effectively eliminate the opportunity to materially increase margins when interest rates are declining.

The aggregate notional amounts of interest rate swaps by maturity date and type at December 31, 1995 and 1994 follow:

| | | 1995 | 1996 | 1997-1999 | 2000-2007 | Total |
|---|---|---|---|---|---|---|
| 1995 | Pay fixed/receive variable | $ -- | $ 1,466 | $3,244 | $ 291 | $5,001 |
| | Pay variable/receive variable | -- | 150 | 625 | 273 | 1,048 |
| | Pay variable/receive fixed | -- | 168 | 37 | 830 | 1,035 |
| | Total | $ -- | $ 1,784 | $3,906 | $1,394 | $7,084 |
| | Memo: | | | | | |
| | Interest rate paid | -- | 6.61% | 6.83% | 6.71% | 6.75% |
| | Interest rate received | -- | 6.69% | 5.94% | 7.08% | 6.35% |
| 1994 | Pay fixed/receive variable | $1,071 | $ 1,137 | $1,390 | $ 200 | $3,798 |
| | Pay variable/receive variable | 100 | 150 | 175 | 274 | 699 |
| | Pay variable/receive fixed | -- | 31 | 35 | 416 | 482 |
| | Total | $1,171 | $ 1,318 | $1,600 | $ 890 | $4,979 |
| | Memo: | | | | | |
| | Interest rate paid | 6.41% | 6.78% | 7.41% | 7.28% | 6.72% |

| | | | | | |
|---|---|---|---|---|---|
| Interest rate received | 5.44% | 5.60% | 6.07% | 7.06% | 6.02% |



More specifically, pay fixed/receive variable interest rate swaps are often used in place of more expensive fixed rate debt for the purpose of match funding fixed rate customer contracts. Pay variable/receive variable interest rate swaps ("basis swaps") are used to transform variable rate, medium-term debt into commercial paper or local currency LIBOR rate obligations. Occasionally, pay variable/receive fixed interest rate swaps are used to transform term fixed rate debt into variable rate obligations. The transactions performed within each of these three categories enable the cost-effective management of interest rate exposures. During 1995, the average notional amount of an interest rate swap agreement was $23.

At December 31, 1995 and 1994, the total notional amounts of these transactions, based on contract maturity, follow:

| | 1995 | 1994 |
|---|---|---|
| Commercial paper/bank borrowings | $1,784 | $1,171 |
| Medium-term debt | 3,906 | 2,193 |
| Long-term debt | 1,394 | 1,615 |
| Total | $7,084 | $4,979 |

For the three years ended December 31, 1995, no interest rate swap agreements were terminated prior to maturity.

Forward-Foreign Exchange Contracts. The Company utilizes forward-foreign exchange contracts to hedge against the potentially adverse impacts of foreign currency fluctuations on foreign currency denominated receivables and payables and firm foreign currency commitments. Firm foreign currency commitments generally represent committed purchase orders for foreign sourced inventory. These contracts generally mature in six months or less. At December 31, 1995 and 1994, the Company had outstanding forward-foreign exchange contracts of $1,474 and $1,476, respectively. Of the outstanding contracts at December 31, 1995, the largest single currency represented was the Japanese yen. Contracts denominated in Japanese yen, Pounds sterling, French francs, Italian lira, German deutschmarks and Swiss francs accounted for over 75 percent of the Company's forward-foreign exchange contracts. Gains and losses on contracts that hedge foreign currency denominated receivables and payables are reported currently in income and are included in Other, net in the consolidated statements of income. Gains and losses on contracts that hedge firm commitments are deferred and subsequently recognized as part of the cost of the underlying transaction, such as inventory. At December 31, 1995, deferred losses amounted to $32. During 1995, the average notional amount of a forward-foreign exchange contract amounted to $6.

[PHOTO]

RUTH BOSCO
Corporate
Accounting
Services

Foreign Currency Swap Agreements. During 1995, the Company entered into a foreign currency and related interest rate swap agreement, whereby the Company issued foreign currency denominated debt and swapped the proceeds with a counterparty. In return, the Company received and effectively denominated the debt in U.S. dollars. Currency swaps are utilized as hedges of the underlying foreign currency borrowings, and exchange gains or losses are recognized currently in Other, net in the consolidated statements of income. At December 31, 1995, a $53 foreign currency and related interest rate swap agreement was outstanding.

Fair Value Of Financial Instruments. The estimated fair values of the Company's financial instruments at December 31, 1995 and 1994 follow:

| | 1995 | | 1994 | |
|---|---|---|---|---|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Cash | $ 130 | $ 130 | $ 35 | $ 35 |
| Accounts receivable, net | 1,894 | 1,894 | 1,811 | 1,811 |
| Short-term debt | 884 | 884 | 1,259 | 1,259 |
| Long-term debt | 10,529 | 10,864 | 9,255 | 9,458 |
| Interest rate and currency swap agreements | -- | (73) | -- | (10) |
| Forward-foreign exchange contracts | -- | (29) | -- | (7) |

The fair value amounts for Cash, Accounts receivable, net and Short-term debt approximate carrying amounts due to the short maturities of these instruments.

The fair value of long-term debt was estimated based on quoted market prices for these or similar issues or on the current rates offered to the Company for debt of the same remaining maturities. The difference between the fair value and the carrying value represents the theoretical net premium the Company would have to pay to retire all debt at such date. The Company has no plans to retire significant portions of its long-term debt prior to scheduled maturity. The Company is not required to determine the fair value of its finance receivables, the match funding of which is the source of much of the Company's interest rate swap activity.

The fair values for interest rate swap agreements and forward-foreign exchange contracts were calculated by the Company based on market conditions at year-end and supplemented with quotes from brokers. They represent amounts the Company would receive (pay) to terminate/ replace these contracts. The Company has no present plans to terminate/replace significant portions of these contracts.

12 Employee Benefit Plans

Retirement Income Guarantee Plan (RIGP). Approximately 51,000 salaried and union employees participate in the Company's RIGP plans. The RIGP plans are defined benefit plans, which provide employees with the greater of (i) the benefit calculated under a highest average pay and years of service formula, (ii) the benefit calculated under a formula that provides for the accumulation of salary and interest credits during an employee's work life, or (iii) the individual account balance from the Company's prior defined contribution plan (Transitional Retirement Accounts or TRA).

At December 31, 1995, these domestic plans accounted for approximately 65 percent of the Company's total pension assets and were invested as follows: domestic and international equity securities -69 percent; fixed-income investments -28 percent; and real estate -3 percent. No plan assets are invested in the stock of the Company.

The RIGP plans are in compliance with the minimum funding standards of the Employee Retirement Income Security Act of 1974 (ERISA).

The transition asset and prior service cost are amortized over 15 years. Pension costs are determined using assumptions as of the beginning of the year while the funded status is determined using assumptions as of the end of the year. The assumptions used in the accounting for the U.S. defined benefit plans follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|

| | | | |
|---|---|---|---|
| Assumed discount rates | 7.25% | 8.75% | 7.75% |
| Assumed rates for compensation increases | 4.25 | 5.75 | 5.25 |
| Expected return on plan assets | 9.50 | 9.50 | 9.50 |

The Company's discount rate considers, among other items, the aggregate effects of a relatively young work force and, because pension benefits are settled at retirement, the absence of retirees receiving pension benefits from plan assets. Accordingly, the duration of the Company's pension obligation tends to be relatively longer in comparison to other companies. Changes in the assumed discount rates and rates of compensation increases primarily reflect changes in the underlying rates of long-term inflation.

Other Plans. The Company maintains various supplemental executive retirement plans (SERPs) that are not tax-qualified and are unfunded.

The Company sponsors numerous pension plans for its international operating units in Europe, Canada and Latin America, which generally provide pay- and service-related



benefits. Plan benefits are provided through a combination of funded trusteed arrangements or through book reserves. The Rank Xerox pension plan in the United Kingdom is the largest international plan and accounted for approximately 22 percent of the Company's total pension assets at December 31, 1995. It is primarily invested in marketable equity securities.

[PHOTO]

LOLITA WHITE
Xerox United Way Campaign

Financial Information. The Company's disclosures about the funded status and components of pension cost are in accordance with U.S. accounting principles. Such principles recognize the long-term nature of pension plan obligations and the need to make assumptions about events many years into the future. In any year there may be significant differences between a plan's actual experience and its actuarially assumed experience. Such differences are deferred and do not generally affect current net pension cost. The objective of deferring such differences is to allow actuarial gains and losses an opportunity to offset over time. These deferrals are included in the captions Unrecognized net gain (loss) and Net amortization and deferrals in the accompanying tables. Due to variations in investment results, the effect of revising actuarial assumptions, and actual plan experience which differs from assumed experience, certain of the Company's plans may be classified as overfunded in one year and underfunded in another year. Under ERISA and other laws, the excess assets of overfunded plans are not available to fund deficits in other plans.

The non-funded plans are the SERPs and the Rank Xerox pension plans in Germany and Austria. For tax reasons, these plans are most efficiently and customarily funded on a pay-as-you-go basis.

A reconciliation of the funded status of the Company's retirement plans to the amounts accrued in the Company's consolidated balance sheets at December 31, 1995 and 1994 follows:

| | 1995 | | | | 1994 | | | |
|---|---|---|---|---|---|---|---|---|
| | Over-funded | Under-funded | Non-funded | Total | Over-funded | Under-funded | Non-funded | Total |
| Accumulated benefit obligation | $5,066 | $ 41 | $ 240 | $5,347 | $4,559 | $ 17 | $ 210 | $4,786 |
| Effect of projected compensation increases | 440 | 37 | 53 | 530 | 418 | 4 | 40 | 462 |
| Projected benefit obligation (PBO) | 5,506 | 78 | 293 | 5,877 | 4,977 | 21 | 250 | 5,248 |
| Plan assets at fair value | 5,830 | 38 | -- | 5,868 | 5,263 | 12 | -- | 5,275 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Excess (deficit) of plan assets over PBO | 324 | (40) | (293) | (9) | 286 | (9) | (250) | 27 |
| Items not yet reflected in the financial statements: | | | | | | | | |
| Unamortized transition obligations (assets) | (137) | 19 | 12 | (106) | (154) | 3 | 14 | (137) |
| Unrecognized prior service cost | 48 | -- | (12) | 36 | 54 | -- | (12) | 42 |
| Unrecognized net (gain) loss | 49 | (14) | 31 | 66 | 55 | 6 | 18 | 79 |
| Prepaid (accrued) pension cost recognized in the consolidated balance sheets at December 31 | $ 284 | $(35) | $(262) | $ (13) | $ 241 | $ -- | $ (230) | $ 11 |



The components of pension cost for the three years ended December 31, 1995 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| DEFINED BENEFIT PLANS | | | |
| Service cost | $ 143 | $ 150 | $ 149 |
| Interest cost--change in PBO due to: | | | |
| Passage of time | 186 | 171 | 159 |
| Net investment income (loss) allocated to TRA accounts | 624 | (45) | 538 |
| Subtotal | 810 | 126 | 697 |
| Net investment (income) loss on: | | | |
| TRA assets | (624) | 45 | (538) |
| Other plan assets | (372) | (96) | (412) |
| Subtotal | (996) | (51) | (950) |
| Net amortization and deferrals | 120 | (144) | 205 |
| Settlement and curtailment gains | (32) | (12) | (4) |
| DEFINED BENEFIT PLANS --net pension cost | 45 | 69 | 97 |
| DEFINED CONTRIBUTION PLAN --pension cost | 13 | 13 | 22 |
| Total pension cost | $ 58 | $ 82 | $ 119 |

Pension cost in 1995 and 1994 was lower than in prior years because of the reduction of the work force in connection with the restructuring actions announced in December 1993. Plan assets consist of both defined benefit plan assets and assets legally allocated to the TRA accounts. The combined investment results of the assets are shown above in the net investment income caption. To the extent investment results relate to TRA, such results are credited to these accounts as a component of interest cost. The TRA account assets were $3.4 billion and $3.0 billion at December 31, 1995 and 1994, respectively. Because a substantial portion of plan assets are TRA-related and are equal to TRA-related liabilities, the Company's pension plans' funding surplus tends to be less than that of comparable companies.

Other Postretirement Benefits. The primary plan for U.S. salaried employees retiring on or after January 1, 1995 provides retirees an annual allowance that can be used to purchase medical and other benefits. The allowance available to each eligible employee is partially service related and, for financial accounting purposes, is projected to increase at an annual rate of 7.5 percent until it reaches the plan's annual maximum coverage of approximately 2.5 times the 1992 level, the inception year of this plan.

The Company also has other postretirement benefit plans that cover employees retiring prior to January 1, 1995 and certain grandfathered employees. These

other plans are generally indemnity arrangements that provide varying levels of benefit coverage. The medical inflation assumption for these plans is 8.50 percent in 1995 and declines to 5.25 percent in 2002 and thereafter. A one percentage point increase in the medical inflation assumptions would increase the service and interest cost for these plans by $6 and the accumulated postretirement benefit obligation by $57.

The discount rate used to determine the funded status was 7.25 percent at December 31, 1995, 8.75 percent at December 31, 1994 and 7.50 percent at December 31, 1993.

[PHOTO]

BILL MECK
Xerox Foundation



A reconciliation of the financial status of the plans as of December 31 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Accumulated Postretirement Benefit Obligation: | | | |
| Retirees | $ 506 | $ 470 | $ 471 |
| Fully eligible employees | 251 | 205 | 249 |
| Other employees | 219 | 247 | 339 |
| Total | 976 | 922 | 1,059 |
| Unrecognized net gain (loss) | 42 | 84 | (62) |
| Accrued cost recognized in the consolidated balance sheets | $1,018 | $1,006 | $ 997 |

The components of postretirement benefit cost for the three years ended December 31, 1995 follow:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Service cost | $ 19 | $ 27 | $ 28 |
| Interest cost | 70 | 66 | 73 |
| Net amortization | (4) | -- | -- |
| Settlement gain | (8) | (25) | -- |
| Total | $ 77 | $ 68 | $ 101 |

These plans are most efficiently and customarily funded on a pay-as-you-go basis.

Employee Stock Ownership Plan (ESOP) Benefits. In 1989, the Company established an ESOP and sold to it ten million shares of Series B Convertible Preferred Stock (Convertible Preferred) of the Company for a purchase price of $785. The Convertible Preferred has a $1 par value, a guaranteed minimum value of $78.25 per share and accrues annual dividends of $6.25 per share. The ESOP borrowed the purchase price from a group of lenders. Because the ESOP borrowings are guaranteed by the Company, they are included in debt in the Company's consolidated balance sheets. A corresponding amount classified as Deferred ESOP Benefits represents the Company's commitment to future compensation expense related to the ESOP benefits.

The ESOP will repay its borrowings from dividends on the Convertible Preferred and from Company contributions. The ESOP's debt service is structured such that the Company's annual contributions (in excess of dividends) essentially

correspond to a specified level percentage of participant compensation. As the borrowings are repaid, the Convertible Preferred is allocated to ESOP participants and Deferred ESOP Benefits are reduced by principal payments on the borrowings. Most of the Company's employees are eligible to participate in the ESOP.

Information relating to the ESOP and the Company for the three years ended December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Interest on ESOP borrowings | $ 45 | $ 49 | $ 52 |
| Dividends declared on Convertible Preferred Stock | $ 59 | $ 61 | $ 62 |
| Cash contribution to the ESOP | $ 34 | $ 32 | $ 30 |
| Compensation expense | $ 35 | $ 32 | $ 31 |

ESOP costs are recognized by the Company based on the amount committed to be contributed to the ESOP plus related trustee, finance and other charges.

## 13 Income Taxes

The parent Company and its domestic subsidiaries file consolidated U.S. income tax returns. Generally, pursuant to tax allocation arrangements, domestic subsidiaries record their tax provisions and make payments to the parent Company for taxes due or receive payments from the parent Company for tax benefits utilized.

Income before income taxes from continuing operations for the three years ended December 31, 1995 consists of the following:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Domestic income (loss) | $ 747 | $ 713 | $(499) |
| Foreign income | 1,100 | 801 | 219 |
| Income (loss) before income taxes | $1,847 | $1,514 | $(280) |

Provisions for income taxes (benefits) from continuing operations for the three years ended December 31, 1995 consist of the following:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Federal income taxes | | | |
| Current | $ 285 | $ 160 | $ 182 |
| Deferred | (21) | 100 | (337) |
| Foreign income taxes | | | |
| Current | 178 | 88 | 87 |
| Deferred | 110 | 182 | (3) |
| State income taxes | | | |
| Current | 57 | 46 | 42 |
| Deferred | 6 | 19 | (49) |
| Income taxes (benefits) | $ 615 | $ 595 | $ (78) |



A reconciliation of the U.S. Federal statutory income tax rate to the effective income tax rate for continuing operations for the three years ended December 31, 1995 follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| U.S. Federal statutory income tax rate | 35.0% | 35.0% | (35.0)% |
| Foreign earnings and dividends taxed at different rates | 2.2 | 2.1 | 17.5 |
| Goodwill amortization | .3 | -- | -- |
| Tax-exempt income | (.6) | (.7) | (3.8) |
| Effect of tax rate changes on deferred tax assets and liabilities | (5.3) | -- | (14.3) |
| State taxes | 2.2 | 2.7 | (1.6) |
| Change in valuation allowance for deferred tax assets | (.8) | -- | -- |
| Other | .3 | .2 | 9.3 |
| Effective income tax rate | 33.3% | 39.3% | (27.9)% |

The 1995 effective tax rate of 33.3 percent is 6 percentage points lower than the 1994 rate. This lower 1995 rate is primarily caused by a decrease in Brazilian corporate tax rates, which created a deferred tax benefit. This benefit increased 1995 fourth quarter and full year net income by $98. Excluding the Brazilian tax benefit, the 1995 effective tax rate was 38.6 percent.

The 1994 effective tax rate of 39.3 percent is 2 percentage points higher than the 1993 tax rate before considering the effects of the 1993 restructuring charge and litigation settlements. This higher 1994 rate is primarily caused by deferred tax rate benefits, which only occurred in 1993, and is partially offset by the increased tax benefits in 1994 associated with the mix of operations and ESOP dividends.

On a consolidated basis, including the effects of dis-continued operations, the Company paid a total of $182, $163 and $197 in income taxes to federal, foreign and state income-taxing authorities in 1995, 1994 and 1993, respectively.

Total income tax expense (benefit) for the three years ended December 31, 1995 was allocated as follows:

| | 1995 | 1994 | 1993 |
|---|---|---|---|
| Income from continuing operations | $ 615 | $ 595 | $ (78) |
| Discontinued operations | (374) | (135) | 5 |
| Common shareholders' equity* | (15) | (19) | (33) |
| Total | $ 226 | $ 441 | $(106) |

* For dividends paid on shares held by the ESOP; cumulative translation adjustments; and unrealized gains and losses on investment securities.

Deferred income taxes have not been provided on the undistributed earnings of foreign subsidiaries and other foreign investments carried at equity. The amount of such earnings included in consolidated retained earnings at December 31, 1995 was approximately $3.4 billion. These earnings have been substantially reinvested and the Company does not plan to initiate any action that would precipitate the payment of income taxes thereon. It is not practicable to estimate the amount of additional tax that might be payable on the foreign earnings.

The tax effects of temporary differences that give rise to significant portions of the deferred taxes at December 31, 1995 and 1994 follow:

| | 1995 | 1994 |
|---|---|---|
| Tax effect of future tax deductions: | | |

| | | |
|---|---|---|
| Depreciation | $ 537 | $ 469 |
| Postretirement medical benefits | 393 | 388 |
| Restructuring reserves | 194 | 342 |
| Other operating reserves | 337 | 290 |
| Deferred intercompany profit | 109 | 116 |
| Allowance for doubtful accounts | 73 | 83 |
| Deferred compensation | 132 | 134 |
| Tax credit carryforwards | 101 | 56 |
| Research and development | 87 | -- |
| Other | 75 | 118 |
| Subtotal | 2,038 | 1,996 |
| Less valuation allowance | 20 | 34 |
| Total | $ 2,018 | $ 1,962 |
| Tax effect of future taxable income: | | |
| Installment sales and leases | $(1,309) | $(1,262) |
| Leverage leases | (35) | (41) |
| Deferred income | (146) | (155) |
| Other | (189) | (117) |
| Total | $(1,679) | $(1,575) |

The above amounts are classified as current or long-term in the consolidated balance sheets in accordance with the asset or liability to which they relate. Current deferred tax assets at December 31, 1995, 1994 and 1993 amounted to $608, $709 and $711, respectively.

The $20 valuation allowance at December 31, 1995 applies to deferred tax assets that may expire unused before the Company can utilize them. After consideration of the valuation allowance, the Company concludes that it is more likely than not that the deferred tax assets will be realized



in the ordinary course of operations based on scheduling of deferred tax liabilities and income from operating activities.

At December 31, 1995, the Company has tax credit carryforwards for federal income tax purposes of $40 which are available to offset future federal income taxes through 2000 and of $61 which are available to offset future federal income taxes indefinitely.

14 Litigation

Continuing Operations. On March 10, 1994, a lawsuit was filed in the United States District Court for the District of Kansas by two independent service organizations (ISOs) in Kansas City and St. Louis and their parent company. On April 15, 1994, another case was filed in the United States District Court for the Northern District of California by 21 different ISOs from 12 states. Plaintiffs in these actions claim damages (to be trebled) to their individual businesses resulting from essentially the same alleged violations of law at issue in the antitrust class action in Texas, which was settled by the Company during 1994. Claims for individual lost profits of ISOs who were not named parties were not included in that class action. In one of the pending cases damages are unspecified and in the other damages in excess of $10 are sought. In addition, injunctive relief is sought in both actions. The two actions have been consolidated for pretrial proceedings in the District of Kansas. The Company has asserted counter-claims against certain of the plaintiffs alleging patent and copyright infringement, misappropriation of Xerox trade secrets, conversion and unfair competition and/or false advertising. On December 11, 1995, the District Court issued a preliminary injunction against the parent company of the Kansas City and St. Louis ISOs for copyright infringement. The Company denies any wrongdoing and intends to vigorously defend these actions and pursue its counterclaims.

Discontinued Operations. Farm & Home Savings Association (Farm & Home) and certain Talegen insurance companies (Insurance Companies) entered into an agreement (Indemnification Agreement) under which the Insurance Companies are required to defend and indemnify Farm & Home from certain actual and punitive damage claims being made against Farm & Home relating to the Brio superfund site (Brio). In a number of lawsuits pending against Farm & Home in the District Courts of Harris County, Texas, several hundred plaintiffs seek both actual and punitive damages allegedly relating to injuries arising out of the hazardous substances at Brio. The Insurance Companies have been defending these cases under a reservation of rights because it is unclear whether certain of the claims fall under the coverage of either the policies or the Indemnification Agreement. The Insurance Companies have been successful in having some claims dismissed which were brought by plaintiffs who were unable to demonstrate a pertinent nexus to the Southbend subdivision. However, there are numerous plaintiffs who do have a nexus to the Southbend subdivision. The Insurance Companies have been in settlement discussions with respect to claims brought by plaintiffs who have or had a pertinent nexus to the Southbend subdivision. If not settled, one or more of these cases can be expected to be tried in 1996.

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[PHOTO]
Pictured here is a banner with the caption "Xerox ColorgrafX Systems produce big, bold, beautiful color like these banners. Using front-end software to produce final prints directly from a digital file, ColorgrafX printers eliminate the intermediate steps associated with traditional methods, reducing turnaround time and costs. Applications include point-of-sale displays, backlit signs, trade show graphics, posters, billboards, backdrops for photography film and video and window displays."



## 15 Preferred Stock

The Company has 22.5 million authorized shares of cumulative preferred stock, $1 par value. Two series of preferred stock are currently outstanding and are described below.

Redeemable Preferred Stock. The Company's series of Ten-Year Preferred Stock has an annual dividend rate of $3.6875 per share and is subject to redemption by the Company through a sinking fund. The mandatory sinking fund for this series is designed to retire 20 percent of the issue in each of the five years beginning on April 1, 1994. Also, the Company has the non-cumulative option to increase the annual sinking fund payments by an amount up to 100 percent of the mandatory payment. During each of 1995 and 1994, 1 million shares were redeemed at the sinking fund redemption price of $50 per share. A total of 0.5 million shares of this series, with a recorded value of $25, is outstanding. Dividends amounted to $3 in 1995; $7 in 1994; and $9 in 1993.

Shares issued under this series are non-voting, have cumulative dividends and have a $50 per share liquidation preference over the Company's common stock.

The Company's former series of Twenty-Year Preferred Stock was redeemed in 1994 for $184, including a premium of $11. Dividends amounted to $5 in 1994 and $14 in 1993.

Convertible Preferred Stock. As more fully described in Note 12 on Page 71, the Company sold, for $785, 10 million shares of its new Series B Convertible Preferred Stock (ESOP shares) in 1989 in connection with the establishment of its ESOP. At December 31, 1995, 9.4 million of these shares remain outstanding. As employees with vested ESOP shares leave the Company, these shares are redeemed by the Company. The Company has the option to settle such redemptions with either shares of common stock or cash.

Preferred Stock Purchase Rights. The Company has a shareholder rights plan designed to deter coercive or unfair takeover tactics and to prevent a person or persons from gaining control of the Company without offering a fair price to all shareholders.

Under the terms of the plan, one preferred stock purchase right (Right) accompanies each share of outstanding common stock. Each Right entitles the holder to purchase from the Company one one-hundredth of a new series of preferred stock at an exercise price of $225.

Within the time limits and under the circumstances specified in the plan, the Rights entitle the holder to acquire common stock of the Company, the surviving company in a business combination or the purchaser of the Company's assets, having a value of two times the exercise price.

The Rights may be redeemed prior to becoming exercisable by action of the Board of Directors at a redemption price of $.05 per Right. The Rights expire in April 1997.

The Rights are non-voting and, until they become exercisable, have no dilutive effect on the earnings per share or book value per share of the Company's common stock.

[PHOTO]

JENNIFER POWELL
Rank Xerox
Corporate Communications



## 16 Common Shareholders' Equity

The components of common shareholders' equity and the changes therein for the three years ended December 31, 1995 follow:

| (Shares in thousands) | Common Stock Shares | Common Stock Amount | Additional Paid-In Capital | Retained Earnings | Net Unrealized Gain (Loss) on Investment Securities | Translation Adjustments | Total |
|---|---|---|---|---|---|---|---|
| BALANCE AT DECEMBER 31, 1992 | 95,066 | $ 96 | $ 650 | $3,282 | $ 6 | $(159) | $3,875 |
| Issuance of common stock, net of issuance costs | 8,050 | 8 | 571 | | | | 579 |
| Stock option and incentive plans | 861 | 1 | 57 | | | | 58 |
| Xerox Canada Inc. exchangeable stock | 65 | 1 | 34 | 3 | | | 38 |
| Convertible securities | 80 | | | | | | |
| Net loss | | | | (126) | | | (126) |
| Cash dividends declared | | | | | | | |
| Common stock ($3.00 per share) | | | | (304) | | | (304) |
| Preferred stock (See Note 15 on Page 74) | | | | (85) | | | (85) |
| Tax benefits on ESOP dividends | | | | 23 | | | 23 |
| Translation adjustments--net of minority shareholders' interests of $(24) | | | | | | (86) | (86) |
| BALANCE AT DECEMBER 31, 1993 | 104,122 | 106 | 1,312 | 2,793 | 6 | (245) | 3,972 |
| Stock option and incentive plans | 1,056 | 1 | 94 | (3) | | | 92 |
| Xerox Canada Inc. exchangeable stock | 653 | | | | | | |
| Convertible securities | 162 | | | | | | |
| Net income | | | | 794 | | | 794 |
| Cash dividends declared | | | | | | | |
| Common stock ($3.00 per share) | | | | (322) | | | (322) |
| Preferred stock (See Note 15 on Page 74) | | | | (73) | | | (73) |
| Tax benefits on ESOP dividends | | | | 19 | | | 19 |
| Call premium on preferred stock (See Note 15 on Page 74) | | | | (11) | | | (11) |
| Net unrealized loss on investment securities | | | | | (439) | | (439) |
| Translation adjustments--net of minority shareholders' interests of $93 | | | | | | 145 | 145 |
| BALANCE AT DECEMBER 31, 1994 | 105,993 | 107 | 1,406 | 3,197 | (433) | (100) | 4,177 |
| Stock option and incentive plans | 1,654 | 2 | 146 | (11) | | | 137 |
| Xerox Canada Inc. exchangeable stock | 455 | | | | | | |
| Convertible securities | 241 | | | | | | |
| Net loss | | | | (472) | | | (472) |
| Net loss during stub period | | | | (21) | | | (21) |
| Cash dividends declared | | | | | | | |
| Common stock ($3.00 per share) | | | | (327) | | | (327) |
| Preferred stock (See Note 15 on Page 74) | | | | (62) | | | (62) |
| Tax benefits on ESOP dividends | | | | 17 | | | 17 |
| Net unrealized gain on investment securities | | | | | 432 | | 432 |
| Translation adjustments--net of minority shareholders' interests of $17 | | | | | | (3) | (3) |
| BALANCE AT DECEMBER 31, 1995 | 108,343 | $ 109 | $1,552 | $2,321 | $ (1) | $(103) | $3,878 |

Common Stock. The Company has 350 million authorized shares of common stock, $1 par value. At December 31, 1995 and 1994, 2.6 and 3.9 million shares, respectively, were reserved for issuance under the Company's incentive compensation plans. In addition, at December 31, 1995, 0.9 million common shares were reserved for the conversion of $53 of convertible debt and 9.4 million common shares were reserved for conversion of ESOP-related Convertible Preferred Stock.

In January 1996, the Board of Directors approved a three-for-one stock split of the Company's common stock, subject to shareholder approval of an increase in the number of authorized shares from 350 million shares to 1,050 million shares. Given shareholder approval, this action will become effective shortly after the 1996 annual shareholders' meeting.

In June 1993, the Company completed a public offering of 8.05 million shares of its common stock in the U.S. and abroad, at a price of $74.25 per share. The proceeds of the offering, after deducting underwriting commissions, were approximately $580 or $72.10 per newly issued share, and were used to retire commercial paper.

Stock Option And Long-Term Incentive Plans. The Company has a long-term incentive plan whereby eligible employees may be granted incentive stock options, nonqualified stock options, incentive stock rights, stock appreciation rights (SARs) and performance unit rights. Subject to vesting and other requirements, SARs and performance unit rights are typically paid in cash, and stock options and incentive stock rights are settled with newly issued or treasury shares of the Company's common stock. Substantially all long-term incentive compensation plan awards in recent years have been in the form of non-qualified stock options, performance units and incentive stock rights. Eligible employees typically receive equal amounts of options and performance units. Stock options granted prior to December 31, 1995, normally vest in two years and normally expire five years from the date of grant. Stock options granted subsequent to December 31, 1995, will vest in three years and will expire eight years from the date of grant. Because the exercise price of the options is equal to the market value of the Company's common stock on the date of grant, option awards do not result in a charge to expense. The value of each performance unit is typically

[PHOTO]

SAM LEE
Office of the General Counsel



based upon the level of return on assets during the year in which granted. Performance units ratably vest in the three years after the year awarded.

At December 31, 1995 and 1994, 3.7 and 4.3 million shares, respectively, were available for grant of options or rights. The following table provides information relating to the status of, and changes in, options granted:

| | 1995 | | 1994 | |
|---|---|---|---|---|
| (Options in thousands) | Stock Options | Average Option Price | Stock Options | Average Option Price |

| | | | | |
|---|---|---|---|---|
| Outstanding at January 1 | 3,242 | $ 84 | 3,210 | $75 |
| Granted | 1,836 | 110 | 1,168 | 98 |
| Canceled | (76) | 101 | (51) | 87 |
| Exercised | (1,364) | 79 | (1,032) | 72 |
| Surrendered for SARs | (40) | 47 | (53) | 51 |
| Outstanding at December 31 | 3,598 | 100 | 3,242 | 84 |
| Exercisable at December 31, 1995 | 1,195 | | | |
| Becoming exercisable in 1996 | 1,275 | | | |

During 1995, Xerox Canada Inc. established an executive rights plan, which grants participants at the executive level rights to acquire the Company's common stock at the participants' option. The vesting, expiration, and exercise price of each right are the same as stock options in the Company's long-term incentive plans. No rights were granted or exercised under this plan during 1995.

Xerox Canada Inc. Exchangeable Class B Stock. In 1989, the shareholders of Xerox Canada Inc. (XCI), a then 79 percent-owned subsidiary of the Company, approved a restructuring plan which, among other provisions, amend- ed the provisions of XCI's Common Shares. The XCI Common Shares had previously been owned by public shareholders and represented the 21 percent of XCI not owned by the Company. As a result of the approved restructuring plan, in 1989 a majority of the XCI public shareholders became owners of XCI's new Non-Voting Exchangeable Class B Shares (Exchangeable Shares) with a right to exchange three Exchangeable Shares for one share of the common stock of the Company. In 1993, the remaining XCI public shareholder entered into the restructuring plan. As a result, the Company's shareholders' equity was increased by $38. At December 31, 1995, the Company has reserved 1.3 million shares of the Company's common stock for purposes of this exchange.

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[PHOTO]
Pictured here are three ribbons with the words "1995 Major Awards Honors."

THE SECRETARY OF THE U. S. DEPARTMENT OF LABOR'S OPPORTUNITY 2000 AWARD TO XEROX FOR MULTIFACETED AFFIRMATIVE ACTION AND DIVERSITY PROGRAMS

THE DEPARTMENT OF LABOR'S FIRST PERKINS/DOLE GLASS CEILING AWARD TO XEROX FOR SUCCESSFUL RECRUITMENT AND DEVELOPMENT OF MINORITIES AND WOMEN AND FOR EXPANDING POLICIES AND PRACTICES IN ORDER TO REMOVE BARRIERS FACED BY MINORITIES AND WOMEN

MONEY MAGAZINE NAMED XEROX TOPS AMONG LARGE U.S. COMPANIES WITH THE BEST BENEFITS

HISPANIC MAGAZINE, HONORED XEROX ON "HISPANIC 100" LIST OF COMPANIES THAT PROVIDE THE MOST OPPORTUNITIES FOR HISPANICS

WORKING MOTHER MAGAZINE HONOR TO XEROX FOR COMMITMENT TO WORKING MOTHERS

ASAHI SHIMBUN FOUNDATION, CORPORATE CITIZENSHIP AWARD TO FUJI XEROX

JAPAN MINISTER FOR INTERNATIONAL TRADE AND INDUSTRY, AWARD TO FUJI XEROX FOR WORKING ENVIRONMENT

NATIONAL QUALITY AWARD, XEROX URUGUAY

QUALITY SCOTLAND BUSINESS EXCELLENCE AWARD,
RANK XEROX (SCOTLAND)

NATIONAL QUALITY AWARD IN PORTUGAL TO RANK XEROX IN 1995. THIS 1994 EXCELLENCE AWARD WAS THE FIRST TO BE PRESENTED IN PORTUGAL

NATIONAL WILDLIFE FEDERATION, CORPORATE CONSERVATION COUNCIL ENVIRONMENTAL ACHIEVEMENT AWARD TO XEROX CORPORATION

GERMAN BLUE ANGEL ENVIRONMENTAL LABEL AWARD TO RANK XEROX FOR THE XEROX 5614 AND 5352 COPIERS

U.S. ENVIRONMENTAL PROTECTION AGENCY - STRATOSPHERIC OZONE PROTECTION AWARD TO XEROX FOR EXEMPLARY EFFORTS TO PROTECT THE OZONE LAYER

FRENCH NATIONAL AGENCY OF ENVIRONMENT AND ENERGY MANAGEMENT, MARQUE RETOUR AWARD TO RANK XEROX FRANCE

ALL-JAPAN INVITATIONAL QC CIRCLE CONVENTION GOLD AWARD TO FUJI XEROX

USA WEEKEND NATIONAL 'MAKE A DIFFERENCE DAY' AWARD TO A ROCHESTER-BASED GROUP OF XEROX EMPLOYEE VOLUNTEERS WHO COLLECTED SEVERAL TRACTOR TRAILER-LOADS OF NEARLY NEW ITEMS THAT WERE SOLD FOR NICKLES AND DIMES AT "THE FRIENDSHIP BARGAIN BAZAAR" TO RESIDENTS OF ONE OF ROCHESTER'S NEEDIEST COMMUNITIES



Quarterly Results of Operations
(Unaudited)

| (In millions, except per-share data) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|---|---|---|---|---|---|
| **1995** | | | | | |
| Revenues | $3,770 | $4,054 | $4,027 | $ 4,760 | $16,611 |
| Costs and expenses | 3,403 | 3,642 | 3,612 | 4,107 | 14,764 |
| Income before income taxes, equity income and minorities' interests | 367 | 412 | 415 | 653 | 1,847 |
| Income taxes | 142 | 160 | 160 | 153 | 615 |
| Equity in net income of unconsolidated affiliates | 13 | 51 | 38 | 30 | 132 |
| Minorities' interests in earnings of subsidiaries | 51 | 49 | 37 | 53 | 190 |
| Income from continuing operations | 187 | 254 | 256 | 477 | 1,174 |
| Discontinued operations | (40) | (16) | (20) | (1,570) | (1,646) |
| Net income (loss) | $ 147 | $ 238 | $ 236 | $(1,093) | $ (472) |
| Primary earnings (loss) per share | | | | | |
| Continuing operations | $ 1.60 | $ 2.21 | $ 2.21 | $ 4.18 | $ 10.20 |
| Discontinued operations | (.37) | (.14) | (.18) | (14.20) | (14.89) |
| Primary earnings per share | $ 1.23 | $ 2.07 | $ 2.03 | $(10.02) | $ (4.69) |
| Fully diluted earnings (loss) per share/1/ | | | | | |
| Continuing operations | $ 1.54 | $ 2.09 | $ 2.09 | $ 3.91 | $ 9.63 |
| Discontinued operations | (.34) | (.13) | (.16) | (14.20) | (14.89) |
| Fully diluted earnings per share | $ 1.20 | $ 1.96 | $ 1.93 | $(10.29) | $ (5.26) |
| **1994** | | | | | |
| Revenues | $3,271 | $3,584 | $3,636 | $ 4,597 | $15,088 |
| Costs and expenses | 3,009 | 3,274 | 3,290 | 4,001 | 13,574 |
| Income before income taxes, equity income and minorities' interests | 262 | 310 | 346 | 596 | 1,514 |
| Income taxes | 104 | 121 | 136 | 234 | 595 |
| Equity in net income of unconsolidated affiliates | 5 | 33 | 25 | 25 | 88 |
| Minorities' interests in earnings of subsidiaries | 32 | 55 | 50 | 76 | 213 |
| Income from continuing operations | 131 | 167 | 185 | 311 | 794 |
| Discontinued operations | (2) | 1 | 1 | - | - |
| Net income | $ 129 | $ 168 | $ 186 | $ 311 | $ 794 |
| Primary earnings (loss) per share | | | | | |
| Continuing operations | $ 1.07 | $ 1.30 | $ 1.60 | $ 2.76 | $ 6.73 |
| Discontinued operations | (.02) | .01 | .01 | - | - |
| Primary earnings per share | $ 1.05 | $ 1.31 | $ 1.61 | $ 2.76 | $ 6.73 |
| Fully diluted earnings (loss) per share | | | | | |
| Continuing operations | $ 1.04 | $ 1.27 | $ 1.53 | $ 2.60 | $ 6.44 |
| Discontinued operations | (.01) | .01 | - | - | - |
| Fully diluted earnings per share | $ 1.03 | $ 1.28 | $ 1.53 | $ 2.60 | $ 6.44 |

/1/ Quarterly primary and fully diluted earnings per share may differ from full year amounts because of changes in the number of shares outstanding during the

year.



# Reports Of Management And Independent Auditors

## Report Of Management

Xerox Corporation management is responsible for the integrity and objectivity of the financial data presented in this annual report. The consolidated financial statements were prepared in conformity with generally accepted accounting principles and include amounts based on management's best estimates and judgments.

The Company maintains an internal control structure designed to provide reasonable assurance that assets are safeguarded against loss or unauthorized use and that financial records are adequate and can be relied upon to produce financial statements in accordance with generally accepted accounting principles. This structure includes the hiring and training of qualified people, written accounting and control policies and procedures, clearly drawn lines of accountability and delegations of authority. In a business ethics policy that is communicated annually to all employees, the Company has established its intent to adhere to the highest standards of ethical conduct in all of its business activities.

The Company monitors its internal control structure with direct management reviews and a comprehensive program of internal audits. In addition, KPMG Peat Marwick LLP, independent auditors, have audited the consolidated financial statements and have reviewed the internal control structure to the extent they considered necessary to support their report, which follows.

The Audit Committee of the Board of Directors, which is composed solely of outside directors, meets regularly with the independent auditors, the internal auditors and representatives of management to review audits, financial reporting and internal control matters, as well as the nature and extent of the audit effort. The Audit Committee also recommends the engagement of independent auditors, subject to shareholder approval. The independent auditors and internal auditors have free access to the Audit Committee.

/s/ Paul A. Allaire

Paul A. Allaire
Chairman of the Board and
Chief Executive Officer

/s/ Barry D. Romeril

Barry D. Romeril
Executive Vice President and
Chief Financial Officer

## Report Of Independent Auditors

To the Board of Directors and Shareholders
of Xerox Corporation

We have audited the consolidated balance sheets of Xerox Corporation and consolidated subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of income and cash flows for each of the years in the three-year period ended December 31, 1995. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial

statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements appearing on Pages 32, 41, 46, and 54-77 present fairly, in all material respects, the financial position of Xerox Corporation and consolidated subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1995, in conformity with generally accepted accounting principles.

/s/ KPMG PEAT MARWICK LLP

KPMG PEAT MARWICK LLP

Stamford, Connecticut
January 24, 1996



Ten Years In Review

| (Dollars in millions, except per-share data) | 1995 | 1994 | 1993 | 1992 | 1991 |
|---|---|---|---|---|---|
| **Per-Share Data** | | | | | |
| Earnings (loss) from continuing operations | | | | | |
| Primary | $ 10.20 | $ 6.73 | $ (2.50) | $ 5.21 | $ 3.72 |
| Fully diluted | 9.63 | 6.44 | (2.50) | 5.21 | 3.69 |
| Dividends declared | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| **Operations** | | | | | |
| Revenues | $16,611 | $15,088 | $14,229 | $14,298 | $ 13,438 |
| Research and development expenses | 951 | 895 | 883 | 922 | 890 |
| Income (loss) from continuing operations | 1,174 | 794 | (193) | 562 | 436 |
| Net income (loss) | (472) | 794 | (126) | (1,020) | 454 |
| **Financial Position** | | | | | |
| Accounts and finance receivables, net | $12,369 | $11,759 | $10,565 | $10,250 | $ 8,952 |
| Inventories | 2,646 | 2,294 | 2,162 | 2,257 | 2,091 |
| Land, buildings and equipment, net | 2,092 | 2,108 | 2,219 | 2,150 | 1,950 |
| Investment in discontinued operations | 4,810 | 7,904 | 8,841 | 8,652 | 9,164 |
| Total assets | 25,969 | 27,278 | 26,999 | 25,792 | 24,342 |
| Consolidated capitalization | | | | | |
| Short-term debt | 3,265 | 3,159 | 2,698 | 2,533 | 2,038 |
| Long-term debt | 8,148 | 7,355 | 7,386 | 8,105 | 7,825 |
| Total debt | 11,413 | 10,514 | 10,084 | 10,638 | 9,863 |

| | | | | | |
|---|---|---|---|---|---|
| Deferred ESOP benefits | (547) | (596) | (641) | (681) | (720) |
| Minorities' interests in equity of subsidiaries | 745 | 1,021 | 844 | 885 | 818 |
| Preferred stock | 763 | 832 | 1,066 | 1,072 | 1,078 |
| Common shareholders' equity | 3,878 | 4,177 | 3,972 | 3,875 | 5,140 |
| Total capitalization | 16,252 | 15,948 | 15,325 | 15,789 | 16,179 |
| **Selected Data and Ratios** | | | | | |
| Common shareholders of record at year-end | 54,262 | 56,414 | 65,820 | 68,877 | 71,213 |
| Book value per common share/1/ | $ 35.48 | $ 38.86 | $ 37.69 | $ 40.19 | $ 54.43 |
| Year-end common share market price | $137.00 | $ 99.00 | $ 88.13 | $ 79.25 | $ 68.50 |
| Employees at year-end | 85,200 | 87,600 | 97,000 | 99,300 | 100,900 |
| Working capital | $ 2,834 | $ 2,411 | $ 2,357 | $ 2,578 | $ 2,282 |
| Current ratio | 1.4 | 1.4 | 1.4 | 1.5 | 1.5 |
| Additions to land, buildings and equipment | $ 438 | $ 389 | $ 470 | $ 582 | $ 467 |
| Depreciation on land, buildings and equipment | $ 376 | $ 446 | $ 437 | $ 418 | $ 397 |

* Data that conforms with the 1995 basis of presentation were not available.

/1/ Book value per common share is computed by dividing common shareholders' equity by outstanding common shares plus common shares reserved for the conversion of the Xerox Canada Inc. Exchangeable Class B stock.



## Ten Years In Review

| (Dollars in millions, except per-share data) | 1990 | 1989 | 1988 | 1987 | 1986 |
|---|---|---|---|---|---|
| **Per-Share Data** | | | | | |
| Earnings (loss) from continuing operations | | | | | |
| Primary | $ 5.44 | $ 4.39 | $ 1.13 | $ 3.06 | $ 2.73 |
| Fully diluted | 5.21 | 4.36 | 1.13 | 3.05 | 2.73 |
| Dividends declared | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| **Operations** | | | | | |
| Revenues | $13,210 | $12,095 | $ 11,354 | $10,537 | $ 9,493 |
| Research and development expenses | 848 | 809 | 794 | 722 | 650 |
| Income (loss) from continuing operations | 599 | 488 | 148 | 353 | 316 |
| Net income (loss) | 243 | 704 | 388 | 578 | 465 |
| **Financial Position** | | | | | |
| Accounts and finance receivables, net | $ 8,016 | $ 7,272 | $ 6,109 | $ 4,948 | $ 3,887 |
| Inventories | 2,148 | 2,413 | 2,558 | 2,286 | 2,459 |
| Land, buildings and equipment, net | 1,851 | 1,781 | 1,803 | 1,639 | 1,491 |
| Investment in discontinued operations | 9,695 | * | * | * | * |
| Total assets | 24,116 | * | * | * | * |
| Consolidated capitalization | | | | | |
| Short-term debt | 1,828 | 1,482 | 1,174 | * | * |
| Long-term debt | 8,726 | 9,247 | 6,675 | * | * |
| Total debt | 10,554 | 10,729 | 7,849 | 5,771 | 4,343 |
| Deferred ESOP benefits | (756) | (785) | - | - | - |
| Minorities' interests in equity of subsidiaries | 832 | 715 | 806 | 655 | 565 |
| Preferred stock | 1,081 | 1,081 | 296 | 442 | 442 |
| Common shareholders' equity | 5,051 | 5,035 | 5,371 | 5,105 | 4,687 |
| Total capitalization | 16,762 | 16,775 | 14,322 | 11,973 | 10,037 |

Selected Data and Ratios

| | | | | | |
|---|---|---|---|---|---|
| Common shareholders of record at year-end | 74,994 | 78,876 | 84,864 | 86,388 | 90,437 |
| Book value per common share/1/ | $ 53.73 | $ 53.59 | $ 52.22 | $ 51.00 | $ 48.00 |
| Year-end common share market price | $ 35.50 | $ 57.25 | $ 58.38 | $ 56.63 | $ 60.00 |
| Employees at year-end | 99,000 | 99,000 | 100,000 | 99,200 | 100,400 |
| Working capital | $ 2,537 | * | * | * | * |
| Current ratio | 1.6 | * | * | * | * |
| Additions to land, buildings and equipment | $ 405 | $ 390 | $ 418 | $ 347 | $ 328 |
| Depreciation on land, buildings and equipment | $ 372 | $ 370 | $ 369 | $ 320 | $ 283 |

* Data that conforms with the 1995 basis of presentation were not available.

/1/ Book value per common share is computed by dividing common shareholders' equity by outstanding common shares plus common shares reserved for the conversion of the Xerox Canada Inc. Exchangeable Class B stock.

Dividends And Stock Prices

Consecutive Dividends Paid To Shareholders

During 1995, dividends paid to the Company's common stock shareholders totaled $3.00 per share, unchanged from 1994 and 1993. Xerox has declared dividends to its shareholders for 66 consecutive years and has paid consecutive quarterly dividends since 1948.

The Company's Board of Directors, at a special meeting held January 23, 1996, declared dividends on Xerox common stock at an increased rate of $.87 per share, a 16 percent increase from the prior quarterly rate of $.75 per share. At its February 5, 1996 meeting, the Board declared dividends on the Company's two issues of preferred stock, unchanged from previous quarterly payments. Payments on the $3.6875 Ten-Year Sinking Fund Preferred are $0.921875 per share. Payments on the Series B Convertible Preferred, which was issued in July 1989 in connection with the formation of a Xerox Employee Stock Ownership Plan, are $1.5625 per share. All of these dividends are payable April 1 to shareholders of record March 1.

At its January 23 meeting, the Board of Directors also approved a three-for-one stock split and an increase in the authorized number of common shares to 1.05 billion from 350 million, subject to shareholder approval at the May 16, 1996 Annual Meeting of Shareholders. If approved by the shareholders, the effective date of the split will be shortly after the Annual Meeting and the annualized dividend on each share of stock will then be $1.16.

On April 1, 1996, the Company will redeem all outstanding shares of the $3.6875 Ten-Year Sinking Fund Preferred stock at a price of $50. Dividends on the stock will cease to accrue on April 1. Notices of redemption were mailed to holders of the stock on February 26, 1996.

XEROX COMMON STOCK PRICES AND DIVIDENDS

| New York Stock Exchange Composite Prices | | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|---|
| 1995 | High | $120 1/2 | $125 7/8 | $134 3/4 | $144 5/8 |
| | Low | 96 1/2 | 109 3/4 | 109 3/4 | 126 |
| | Dividends Paid | .75 | .75 | .75 | .75 |
| 1994 | High | $103 1/4 | $104 3/4 | $109 3/8 | $112 3/4 |
| | Low | 87 3/4 | 93 7/8 | 97 | 91 1/2 |

| | | | | | |
|---|---|---|---|---|---|
| | Dividends Paid | .75 | .75 | .75 | .75 |

XEROX $3.6875 TEN-YEAR SINKING FUND
PREFERRED STOCK PRICES AND DIVIDENDS

| New York Stock Exchange Composite Prices | | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|---|
| 1995 | High | $ 54 1/2 | $ 54 | $ 54 | $ 56 |
| | Low | 49 | 49 | 49 1/2 | 50 |
| | Dividends Paid | .921875 | .921875 | .921875 | .921875 |
| 1994 | High | $ 54 | $ 55 1/2 | $ 55 | $ 54 |
| | Low | 50 1/2 | 50 1/2 | 50 | 50 |
| | Dividends Paid | .921875 | .921875 | .921875 | .921875 |

Stock Listed And Traded

Xerox common stock (XRX) is listed on the New York Stock Exchange and the Chicago Stock Exchange. It is also traded on the Boston, Cincinnati, Pacific Coast and Philadelphia exchanges and in London, Basel, Berne, Geneva, Lausanne and Zurich.

EXHIBIT 21

Subsidiaries of Xerox Corporation

A. Xerox Corporation

The following companies are subsidiaries of Xerox Corporation as of February 1, 1996. The names of a number of other subsidiaries have been omitted as they would not, if considered in the aggregate as a single subsidiary, constitute a significant subsidiary:

| Name of Subsidiary | Incorporated In | Ownership % |
|---|---|---|
| Xerox Canada Inc. | Ontario, Canada | 90 |
| Xerox Canada Finance Inc. | Ontario, Canada | 100 |
| Xerox Canada Ltd. | Ontario, Canada | 65 |
| Lyell Holdings Limited | Delaware | 100 |
| Xerox Business Equipment Limited | United Kingdom | 100 |
| Xerox Research (UK) Limited | United Kingdom | 100 |
| Xerox Business Equipment, Inc. | Delaware | 100 |
| Xerox Financial Services, Inc. | Delaware | 100 |
| International Insurance Company | Illinois | 100 |
| OakRe Life Insurance Company | Missouri | 100 |
| Xerox Credit Corporation | Delaware | 100 |
| XCC Investment Corporation | Delaware | 100 |
| Talegen Holdings, Inc. | Delaware | 100 |
| Xerox Life Management Company | Delaware | 100 |
| Ridge Reinsurance Limited | Bermuda | 100 |
| The Resolution Group, Inc. | Delaware | 100 |
| Xerox Foreign Sales Corporation | Barbados | 100 |
| Xerox Realty Corporation | Delaware | 100 |
| Xerox do Brasil, Ltda. | Brazil | 100 |
| Xerox Mexicana, S.A. de C.V. | Mexico | 100 |
| Rank Xerox Investments Limited | Bermuda | 66.7 |
| Rank Xerox Limited | United Kingdom | 51.2 |
| Bessemer Trust Limited | United Kingdom | 100 |
| Fuji Xerox Co., Ltd. | Japan | 50 |
| Modi Xerox Limited | India | 35.9 |
| Rank Xerox (U.K.) Limited | United Kingdom | 100 |
| Rank Xerox (Ireland) Limited | United Kingdom | 100 |
| Rank Xerox Espanola S.A. | Spain | 100 |
| Rank Xerox de Financiacion S.A. | Spain | 100 |
| Rank Xerox Finance (Nederland) BV | Netherlands | 100 |
| Rank Xerox Greece S.A. | Greece | 100 |
| NV Rank Xerox Credit S.A. | Belgium | 100 |
| Rank Xerox Finance AG | Switzerland | 100 |
| Rank Xerox Finance Limited | United Kingdom | 100 |
| Rank Xerox Leasing GmbH | Germany | 100 |
| Rank Xerox Leasing International Finance BV | Netherlands | 100 |
| Rank Xerox - The Document Company S.A. | France | 100 |
| Burofinance S.A. | France | 66 |
| Rank Xerox Exports Limited | United Kingdom | 100 |
| N.V. Rank Xerox S.A. | Belgium | 100 |
| Rank Xerox Austria GmbH | Austria | 100 |
| Rank Xerox A/S | Denmark | 100 |
| Rank Xerox Finans A/S | Denmark | 100 |
| Rank Xerox Oy | Finland | 100 |

| Name of Subsidiary | Incorporated In | Ownership % |
|---|---|---|
| Rank Xerox GmbH | Germany | 100 |
| Rank Xerox S.p.A. | Italy | 100 |
| Rank Xerox AG | Switzerland | 100 |
| Rank Xerox AS | Norway | 100 |
| Rank Xerox Management Services S.A. | Belgium | 100 |

| | | |
|---|---|---|
| Rank Xerox Pensions Limited | United Kingdom | 100 |
| Rank Xerox A.B. | Sweden | 100 |
| Rank Xerox (Nederland) B.V. | Netherlands | 100 |
| Rank Xerox Holding B.V. | Netherlands | 51.2 |
| Rank Xerox Manufacturing (Nederland) B.V. | Netherlands | 100 |
| R-X Holdings Limited | Bermuda | 66.7 |
| Xerox Limited | Bermuda | 100 |

B. Talegen Holdings, Inc.

Insurance Holding Company System Organizational Chart

All controlled persons and controlled insurers of Talegen Holdings, Inc., a Delaware corporation ("Talegen"), (under applicable state insurance laws), are set forth in the following table, together with the jurisdiction of domicile of each and the percentage of voting securities owned as of January 1, 1996. Unless otherwise indicated, all of the persons included in the table are corporations, the voting securities of which are directly owned by Talegen. All of the outstanding capital stock of Talegen is owned by Xerox Financial Services, Inc., a Delaware corporation ("XFSI"), which is a wholly-owned subsidiary of Xerox Corporation. XFSI also owns, effective as of December 31, 1995, all of the outstanding capital stock of The Resolution Group, Inc., a Delaware corporation which was formerly a wholly-owned subsidiary of Talegen.

| Name of Subsidiary | Incorporated In | Ownership % |
|---|---|---|
| Coregis Group, Inc. | Delaware | 100 |
| Coregis Insurance Company | Indiana | 100 (1) |
| Coregis Indemnity Company | Illinois | 100 (1) |
| California Insurance Company | California | 100 (1) |
| Coregis Managers Corporation (IL) | Illinois | 100 (1) |
| Crum & Forster Holdings, Inc. | Delaware | 100 |
| United States Fire Insurance Company | New York | 100 (1) |
| Southbend Properties, Inc. | Texas | 100 (1) |
| The North River Insurance Company | New Jersey | 100 (1) |
| Crum and Forster Insurance Company | New Jersey | 100 (1) |
| Crum & Forster Underwriters Co. of Ohio | Ohio | 100 (1) |
| Crum & Forster Indemnity Company | New York | 100 |
| Crum & Forster Custom Securities, Inc. | California | 100 (1) |
| Industrial Indemnity Holdings, Inc. | Delaware | 100 |
| Industrial Indemnity Company | California | 100 (1) |
| Claremont Holdings Limited | Bermuda | 9.2 |
| Claremont Insurance Limited | Bermuda | 100 |
| Industrial/Las Flores, Inc. (5) | California | 100 (1) |
| Industrial/Canyon Creek, Inc. (5) | California | 100 (1) |
| Industrial/Shadowridge, Inc. (5) | California | 100 (1) |
| Industrial/Mountainback, Inc. (5) | California | 100 (1) |
| Industrial/Channing, Inc. (5) | California | 100 (1) |
| Industrial Indemnity Company of Alaska | Alaska | 100 (1) |
| Industrial Indemnity Company of Idaho | Idaho | 100 (1)(2) |
| Industrial Indemnity Company of the Northwest | Washington | 100 (1) |
| Industrial Insurance Company | California | 100 (1) |
| Employers First Insurance Company | California | 100 (1) |
| 255 California Corporation | California | 100 (1) |
| Industrial Indemnity Insurance Services, Inc. | California | 100 (1) |
| American All Risk Loss Administrators | California | 40 (1) |
| Westchester Specialty Group, Inc. | Delaware | 100 |
| Westchester Fire Insurance Company | New York | 100 (1) |
| Westchester Surplus Lines Insurance Company | Georgia | 100 (1) |
| Industrial Underwriters Insurance Company | Texas | 100 (1) |
| Westchester Specialty Insurance | | |

| Name of Subsidiary | Incorporated In | Ownership % |
|---|---|---|
| Services, Inc. | Nevada | 100 (1) |
| Industrial Excess & Surplus Insurance Brokers | California | 100 (1) |
| Talegen Properties, Inc. | Delaware | 100 |
| Infocus Employee Services, Inc. | Delaware | 92.5 |
| Filoli Information Systems Company | Delaware | 40 |
| Apprise Corp. | New Jersey | 100 |
| Crum & Forster of Canada Ltd. | Canada | 100 |
| First Quadrant Corp. | New Jersey | 100 |
| First Quadrant Limited | United Kingdom | 100 (1)(4) |
| Herald Insurance Company | Canada | 100 (3) |

(1) Directly or indirectly owned by a subsidiary of Talegen.

(2) Includes qualifying shares held by directors.

(3) Includes less than 1/5 of 1% shares beneficially owned by directors.

(4) Includes one share held by Talegen in trust and as nominee for First Quadrant Corp.

(5) Subject to the receipt of a tax clearance from the California Franchise Tax Board, the effective date of the dissolution of this corporation will be December 18, 1995.

EXHIBIT 23

Consent of Independent Auditors

To the Board of Directors and Shareholders of Xerox Corporation

We consent to the incorporation by reference in the Registration Statements of Xerox Corporation on Forms S-8 (Nos. 2-81528, 2-86274, 2-86275, 33-18126, 33-44313, 33-44314 and 33-65269) and Forms S-3 (Nos. 2-82363, 33-9486, 33-32215, 33-49177 and 33-54629) of our reports dated January 24, 1996 relating to the consolidated balance sheets of Xerox Corporation and consolidated subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of income and cash flows and related schedule for each of the years in the three-year period ended December 31, 1995 which reports appear in or are incorporated by reference in the 1995 Annual Report on Form 10-K.

KPMG PEAT MARWICK LLP

Stamford, Connecticut
March 28, 1996

<ARTICLE> 5
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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM XEROX CORPORATION'S DECEMBER 31, 1995 FINANCIAL STATEMENTS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.
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