

PRIMUS GUARANTY LTD

Form S-1/A

September 24, 2004

As filed with the Securities and Exchange Commission on September 24, 2004.

Registration No. 333-114818

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

AMENDMENT No. 5
TO
FORM S-1

REGISTRATION STATEMENT
Under
THE SECURITIES ACT OF 1933

PRIMUS GUARANTY, LTD.

(Exact name of registrant as specified in its charter)

Bermuda
(State or other jurisdiction of
incorporation or organization)

6199
(Primary Standard Industrial
Classification Code Number)

N/A
(I.R.S. employer
Identification Number)

Primus Guaranty, Ltd.
Clarendon House, 2 Church Street
Hamilton HM 11, Bermuda
441-296-0519

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after this Registration Statement is declared effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933 (the Securities Act), check the following box:

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion, dated September 24, 2004

PROSPECTUS

10,344,828 Shares

Primus Guaranty, Ltd.

Common Shares

This is our initial public offering of common shares. We are offering 9,143,493 common shares and the selling shareholders identified in this prospectus are offering 1,201,335 common shares. No public market currently exists for our common shares. We will not receive any proceeds from the sale of the common shares offered by the selling shareholders.

Our common shares have been approved for listing on the New York Stock Exchange under the symbol "PRS". We currently estimate that the initial public offering price will be between \$13.50 and \$15.50 per share.

Investing in the shares involves risks. Risk Factors begin on page 9.

	Per Share	Total
Public offering price	\$	\$
Underwriting discount	\$	\$
Proceeds to Primus Guaranty, Ltd. (before expenses)	\$	\$
Proceeds to selling shareholders (before expenses)	\$	\$

The selling shareholders have granted the underwriters a 30-day option to purchase up to an aggregate of 1,551,724 additional common shares on the same terms and conditions as set forth above to cover over-allotments, if any.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

Lehman Brothers, on behalf of the underwriters, expects to deliver the shares on or about _____, 2004.

LEHMAN BROTHERS MORGAN STANLEY

CREDIT SUISSE FIRST BOSTON

UBS INVESTMENT BANK

WILLIAM BLAIR & COMPANY

KEEFE, BRUYETTE & WOODS

, 2004

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Through and including _____, 2004 (the 25th day after the date of this prospectus), all dealers effecting transactions in our common shares, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers' obligations to deliver a prospectus when acting as underwriters and with respect to their unsold allotment or subscriptions.

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PROSPECTUS SUMMARY

This summary does not contain all of the information that you should consider before investing in our common shares. You should read the entire prospectus carefully, including the "Risk Factors" section beginning on page 9 and our consolidated financial statements and related notes to these financial statements beginning on page F-1 before making an investment decision. Unless otherwise indicated or the context requires otherwise, references in this prospectus to "we", "us" or "our" refer to the consolidated operations of Primus Guaranty, Ltd., or Primus Guaranty, and references to a company name refer solely to such company. Unless otherwise indicated, all information in this prospectus (1) reflects the automatic conversion upon consummation of this offering of all outstanding Series A convertible voting preferred shares, or Series A preferred shares, into an aggregate of 29,980,691 common shares, (2) reflects a one for eight reverse share split of our common shares to be effected immediately prior to the completion of this offering (with fractional shares satisfied in cash) and (3) assumes no exercise of the underwriters' over-allotment option.

Our Company

Overview

Our principal business is selling credit protection under which we assume the risk of default on investment grade credit obligations. The protection we sell takes the form of a credit default swap, or credit swap. In exchange for a fixed quarterly premium we agree, upon a default or other credit event (e.g., bankruptcy, moratorium or repudiation) affecting a designated issuer, which we refer to as a Reference Entity, to pay our customer, which we refer to as a counterparty, an agreed amount. We pay this agreed amount, which we call a notional amount, upon our counterparty's delivery to us of the Reference Entity's debt obligation. Credit swaps are an efficient and standardized mechanism to reduce credit risk exposure arising from the ownership of financial obligations such as bonds, loans and receivables. See "Industry Overview—Overview of Credit Swaps" for additional information regarding credit swaps. The primary purchasers of credit swaps are commercial and investment banks as well as credit portfolio managers, insurance companies and other financial institutions.

Primus Financial Products, LLC, or Primus Financial, our principal subsidiary, has the highest counterparty credit ratings offered by Standard & Poor's Rating Services (AAA), or S&P, and Moody's Investors Service, Inc. (Aaa), or Moody's, and is managed by an experienced team of professionals who have expertise in credit analysis, trading, risk management and market analysis. At June 30, 2004, we had relationships with 34 counterparties to which we were prepared to sell credit protection. At June 30, 2004, Primus Financial had sold credit protection with respect to \$8.7 billion (in notional amount) of referenced obligations representing 453 Reference Entities spread across 40 industries and 22 countries. Our credit swap portfolio had a weighted average credit rating of A ("strong"; sixth of 21 categories) by S&P and A3 ("good financial security"; seventh of 21 categories) by Moody's and had an average maturity of 2.8 years at June 30, 2004.

We were capitalized in March 2002 and sold our first credit swaps in June 2002.

Growth In The Credit Swap Market

The credit swap market has been transformed from a small, niche segment of the capital markets to a global market that is rapidly growing with diverse product applications and a wide range of participants. The notional amount referenced by outstanding credit swaps (excluding asset swaps) is estimated by the British Bankers Association, a trade association in the banking and financial services industry, and the International Swaps and Derivatives Association, Inc., or ISDA, to have grown from \$180.0 billion at December 31, 1997, to \$3.6 trillion at December 31, 2003. There are approximately 1,200 Reference Entities that have investment grade credit ratings by both S&P and Moody's. We believe that the credit swap market will continue to grow as commercial and investment banks and other credit portfolio managers more actively manage their credit and investment portfolios.

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Competitive Strengths

We believe we are well-positioned to continue to compete effectively in the credit swap market. The following are our competitive strengths:

Highest Available Counterparty Credit Ratings. Primus Financial has a AAA ("extremely strong") counterparty credit rating from S&P and a Aaa ("exceptional") counterparty credit rating from Moody's, the highest of their

respective twenty-one rating levels. These ratings are based on an analysis of the risks of Primus Financial's business of selling credit swaps in relation to its capital.

Experienced Management Team with Strong Market Relationships. Our management team has extensive industry experience with strong and long-standing market relationships with participants and counterparties in the credit swap market.

Disciplined Underwriting and Risk Management. We underwrite credit risks using a rigorous credit analysis that allows us to sell credit protection on Reference Entities that we believe offer attractive risk-adjusted returns.

Efficient and Scalable Operations. We believe that our scalable operations enable us to leverage our management's expertise and provide opportunities to realize increased profitability as our business grows and matures.

Our competitive strengths are more fully discussed on pages 47 through 48.

Business Strategy

The major elements of our strategy are:

Continue to Expand our Credit Swap Business. We intend to leverage our competitive strengths to continue to build a diversified credit risk portfolio and increase and efficiently utilize our capital resources to support our growth.

Maintain Primus Financial's AAA/Aaa Ratings. We believe that having the highest ratings from S&P and Moody's gives Primus Financial the ability to attract large and growing amounts of business with a wide range of counterparties and the ability to select Reference Entities along the full spectrum of investment grade credits.

Pursue Opportunities in Complementary Businesses. We intend to diversify our sources of revenue by expanding into complementary businesses.

The proceeds from this offering will facilitate executing our business strategy by increasing our capital resources and enabling us to expand our business, maintain our highest counterparty credit ratings and pursue opportunities in complementary businesses. In particular, we will provide at least \$60.0 million of proceeds received from this offering to Primus Financial to enhance its capital and enable it to sell additional credit swaps.

Our business strategy is more fully discussed on page 48.

Risks Relating to Our Business and this Offering

As part of your evaluation of an investment in our common shares, you should take into account the various risks to which our business is subject. We may incur significant losses on the credit protection we sell; the operating guidelines we agreed upon with the rating agencies may change and may restrict our future growth; we have only a limited operating history; and the continued perception of our creditworthiness is critical to rating agencies and our counterparties. The credit swap industry, in which we are a very recent and comparatively small entrant, is highly competitive and includes significantly more diversified and better capitalized participants. You should also be aware that there are various risks specific to owning our common shares, including the continued voting control by our existing shareholders, future potential sales by such shareholders of substantial amounts of our common shares, potential share price volatility and the significant United States income tax consequences to holders of our common shares. For more information about these and other risks, see "Risk Factors" beginning on page 9. You should consider carefully these risks before making an investment in our common shares.

Corporate Structure

We are a Bermuda company. Primus Financial is our principal subsidiary and a AAA/Aaa rated seller of credit swaps. Primus Asset Management, Inc., or Primus Asset Management, another of our subsidiaries, manages Primus Financial's credit swap business and intends to manage the credit swap portfolios of third parties. We also have a Bermuda registered financial guaranty insurance company, Primus Re, Ltd., or Primus Re, that offers credit insurance protection to companies that prefer insurance products to credit swaps. See "Business—Corporate Structure" for additional information regarding our structure. We are currently owned primarily by XL Insurance (Bermuda) Ltd, a subsidiary of XL Capital Ltd, Transamerica Life Insurance Company, an indirect wholly-owned subsidiary of AEGON, N.V., a Netherlands based holding company, CalPERS/PCG Corporate Partners Fund, LLC, Radian Group Inc. and management. Executives of our institutional shareholders serve on our board of directors and these directors provide us valuable assistance and expertise in conducting and expanding our business.

Our registered office is at Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda and our telephone number is 441-296-0519. The offices of our principal operating subsidiary, Primus Financial, are located at 360 Madison Avenue, 23rd Floor, New York, New York 10017 and its telephone number is 212-697-2227.

Recent Events

On July 23, 2004, Primus Financial issued \$75.0 million of AAA/Aaa rated subordinated deferrable interest notes with a 30-year maturity to increase its capital base in order to permit it to sell additional credit swaps. The initial interest rate for the notes is 2.57%. This interest rate will remain in effect through July 25, 2005. Thereafter, the interest rate will be reset every 28 days through a Dutch auction process.

Potential Conflicts

Some of our principal shareholders sell products and offer services that compete with ours. In addition, they may hire us to provide credit risk advisory and asset management services. Our board of directors monitors transactions with our principal shareholders and their affiliates to ensure that such transactions are conducted on an arm's-length basis. Additionally, our directors customarily recuse themselves when transactions with our shareholders with whom they are associated are discussed or approved by the board of directors. For more information concerning the potential conflicts that may arise, please see the section "Business—Potential Conflicts With Certain Shareholders".

Notice to United States Investors—Tax Consequences of Owning Our Common Shares

We and our subsidiary, Primus (Barbados), Ltd., or Primus Barbados, are likely to be and remain passive foreign investment companies, or PFICs, for United States federal income tax purposes. There are potentially adverse United States federal income tax consequences of investing in a PFIC for a shareholder who is a United States taxpayer. These consequences include the following:

- if a shareholder makes a qualified electing fund election, or QEF election, with respect to Primus Guaranty and Primus Barbados, the shareholder will have to include annually in his or her taxable income an amount reflecting an allocable share of the income of Primus Guaranty or Primus Barbados, regardless of whether dividends are paid by Primus Guaranty to the

shareholder;

- if a shareholder makes a mark-to-market election with respect to Primus Guaranty, the shareholder will have to include annually in his or her taxable income an amount reflecting any year-end increases in the price of our common shares, regardless of whether dividends are paid by Primus Guaranty to the shareholder; it is unclear how such an election would affect the shareholder with respect to Primus Barbados; and

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- if a shareholder does not make a QEF election or a mark-to-market election, he or she may incur significant additional United States federal income taxes with respect to dividends on, or gain from, the sale or other disposition of, our common shares, or with respect to dividends from Primus Barbados to us, or with respect to our gain on any sale or other disposition of Primus Barbados shares.

Please review carefully "Risk Factors—Risks Related to Taxation" and "Tax Considerations—Taxation of Shareholders—United States Holders—Passive Foreign Investment Companies".

Prospective investors are urged to consult their own tax advisors concerning their particular circumstances and the United States federal, state, local and non-United States tax consequences to them of owning and disposing of our common shares. In particular, prospective United States holders of our common shares are urged to consult with their tax advisors as to the tax consequences of holding shares of PFICs directly and indirectly (in the case of Primus Barbados) and the possible advisability of electing to have each of Primus Guaranty and Primus Barbados treated as a "qualified electing fund", or QEF, or of making a mark-to-market election with respect to Primus Guaranty.

You should rely only on the information contained in this prospectus. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or insufficient information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where an offer or sale is not permitted. You should assume that the information appearing in this prospectus is accurate as of the date on the front cover of this prospectus only. Our business, financial condition, results of operations and prospects may have changed since that date.

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The Offering

Common shares offered by Primus Guaranty	9,143,493 shares
Common shares offered by selling shareholders	1,201,335 shares
Common shares to be outstanding after this offering	42,787,843 shares
Use of proceeds	

We intend to use a portion of the net proceeds from this offering to provide at least \$60.0 million in additional capital to Primus Financial to expand its capacity to enter into credit swaps and to use the remainder as working capital and for general corporate purposes, including expanding our credit swap business and pursuing opportunities in complementary businesses. We will not receive any of the proceeds from the sale of common shares by the selling shareholders.

Dividend policy

We do not intend to pay dividends on our common shares for the foreseeable future. We plan to retain our earnings for use in the operation of our business and to fund future growth.

New York Stock Exchange symbol

"PRS"

Except as otherwise indicated, the number of common shares stated to be outstanding after this offering gives effect to the common shares being sold by us in this offering, a one for eight reverse share split that we intend to effect immediately prior to the completion of this offering (with fractional shares satisfied in cash), the automatic conversion of all outstanding shares of our Series A preferred shares into an aggregate of 29,980,691 common shares upon completion of this offering and the proposed issuance by us of an aggregate of 9,372 common shares to our non-employee directors upon completion of this offering. Such number of common shares excludes:

- 519,375 common shares issuable upon exercise of options outstanding as of September 23, 2004, under our 2002 stock incentive plan, with a weighted average exercise price of \$8.65 per share;
- 1,414,746 common shares issuable upon exercise of warrants outstanding as of September 23, 2004, with an exercise price of \$5.18 per share and an expiration date of March 14, 2007;
- 715,348 common shares issuable upon exercise of restricted share units outstanding as of September 23, 2004; and
- 5,134,353 additional common shares reserved for issuance under our employee incentive plan.

You should read the discussion under "Management—Share Option and Other Benefit Plans" for additional information about our employee option plans.

There has been no public market for our common shares prior to this offering. We and the underwriters will negotiate the initial public offering price at which our common shares will be sold in this offering. Factors that we and the underwriters will consider include: prevailing conditions in the securities markets at the time of this offering; the history of and prospects for our industry; an assessment of our management; our present operations; our historical results of operations; the trend

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of our revenues and earnings; our earnings prospects; recent market prices of, and the demand for, publicly traded common stock of generally comparable companies; and any other relevant factors.

We cannot be sure that the initial public offering price will correspond to the price at which the common shares will trade in the public market following this offering or that an active trading market for the common shares will develop and continue after this offering.

Summary Historical Financial Data

The following tables summarize our historical financial and operating data as of the dates or for the periods indicated. We derived the summary for each of the three years ended December 31, 2003, 2002 and 2001 from our consolidated financial statements, which have been prepared in accordance with United States generally accepted accounting principles, or United States GAAP, and audited by Ernst & Young LLP. The statement of operations data for the six months ended June 30, 2004 and 2003, and the balance sheet data as of June 30, 2004, are derived from, and are qualified by reference to, our unaudited consolidated financial statements included elsewhere in this prospectus. The unaudited consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, that we consider necessary for the fair presentation of our financial position and results of operations for these periods. The results of operations for prior accounting periods are not necessarily indicative of the results to be expected for any future accounting periods. Until March 2002, we were in a development stage. We were capitalized on March 14, 2002 and began to sell credit swaps in June 2002. You should read this summary in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and related notes appearing elsewhere in this prospectus.

	Six Months Ended June 30,		Year Ended December 31,		
	2004	2003	2003	2002	2001
(\$ in thousands, except per share data)					
Consolidated Statement of Operations:					
Revenues:					
Net credit swap revenue	\$ 2,835	\$ 57,746	\$ 103,326	\$ 14,761	\$ —
Interest income earned	1,368	1,308	2,617	1,610	2
Other income	236	54	107	12	—
Total revenues	\$ 4,439	\$ 59,108	\$ 106,050	\$ 16,383	\$ 2
Expenses:					
Employee compensation	\$ 7,284	\$ 5,032	\$ 11,701	\$ 8,156	\$ 1,020
Other expenses	3,979	6,076	14,196	11,042	1,769
Total expenses	\$ 11,263	\$ 11,108	\$ 25,897	\$ 19,198	\$ 2,789
Distributions on preferred securities of subsidiary	\$ (1,147)	\$ (832)	\$ (1,854)	\$ —	\$ —
Income (loss) before benefit (provision) for income taxes	\$ (7,971)	\$ 47,168	\$ 78,299	\$ (2,815)	\$ (2,787)
Benefit (provision) for income tax	(117)	(105)	172	(254)	—
Net income (loss)	\$ (8,088)	\$ 47,063	\$ 78,471	\$ (3,069)	\$ (2,787)
Per Share Data:					
Earnings (loss) per share:					
Basic	\$ (2.41)	\$ 18.71	\$ 31.18	\$ (1.22)	\$ (1.12)
Diluted	\$ (2.41)	\$ 1.39	\$ 2.33	\$ (1.22)	\$ (1.12)
Book value per share:					
Basic ⁽¹⁾	\$ 58.40	\$ 70.24	\$ 82.63	\$ 51.95	\$ (2.28)

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Diluted ⁽²⁾	\$	6.04	\$	5.40	\$	6.41	\$	4.23	\$	(2.28)
Weighted average number of common shares outstanding:										
Basic		3,353		2,515		2,517		2,510		2,479
Diluted		3,353		33,843		33,737		2,510		2,479

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	As of June 30, 2004	
	Actual	Pro Forma ⁽³⁾
Balance Sheet Data:		
Cash and cash equivalents	\$ 272,523	\$ 466,585
Short-term investments	3,441	3,441
Unrealized gain on credit swaps, at fair value	29,121	29,121
Other assets	14,948	15,886
Total assets	\$ 320,033	\$ 515,033
Unrealized loss on credit swaps, at fair value	\$ 2,664	\$ 2,664
Long-term debt obligations of subsidiary	—	75,000
Total liabilities	7,875	82,875
Preferred securities of subsidiary	98,521	98,521
Shareholders' equity	213,637	333,637
Total liabilities, preferred securities of subsidiary and shareholders' equity	\$ 320,033	\$ 515,033

(1)Book value per share is based on total shareholders' equity divided by basic common shares outstanding.

(2)Diluted book value per share is based on total shareholders' equity plus the assumed exercise of all dilutive options and warrants divided by diluted common shares outstanding.

(3)Gives effect to our sale of a total of 9,143,493 common shares in this offering at an assumed public offering price of \$14.50 per share, the midpoint of the range set forth on the cover of the prospectus, reflects the pro forma effect of the conversion of all the Series A preferred shares into 29,980,691 common shares in connection with this offering, a one for eight reverse share split of our common shares to be effected immediately prior to the completion of this offering (with fractional shares being satisfied in cash) and Primus Financial's issuance of \$75.0 million of AAA/Aaa rated subordinated deferrable interest notes less capitalized debt issuance cost of \$937,500.

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RISK FACTORS

Your investment in our common shares will involve some risks. You should carefully consider the following discussion of these risks, together with the other information contained in this prospectus, before deciding whether an investment in our common shares is suitable for you.

The risks and uncertainties described in this prospectus are not the only risks we face. However, these are the risks our management believes are material. Additional risks not presently known to us or that we currently deem immaterial may also impair our business or results of operations. Any of the risks described below could have a significant or material adverse effect on our results of operations or financial condition, and a corresponding decline in the market price of our common shares.

Risks Related to our Business

The failure to manage effectively the risk of credit losses could have a material adverse effect on our financial condition, results of operations and credit ratings.

We cannot assure you that any of the loss mitigation methods we use in managing our credit swap portfolio will be effective. If, for example, multiple credit defaults or other credit events that exceed our expectations occur within a short time period, the payments we would be required to make under the related credit swaps could materially and adversely affect our financial condition, results of operations and credit ratings. Many of Primus Financial's credit swaps are new and the underlying Reference Entities may not have had time to exhibit problems. Moreover, even though we may identify a heightened risk of default with respect to a particular Reference Entity, our ability to limit our losses, such as through hedging or terminating the credit swap, before a default or other credit event actually occurs could be limited by inadequate liquidity in the credit swap market. We also intend to enter into new businesses, including selling credit swaps referencing obligations of Reference Entities that are below investment grade, which may not have the same or similar loss limitation methods. We have not initially sold credit swaps on Reference Entities that are below investment grade. There can be no assurance that we will be able to manage higher risks of credit losses effectively or that any of our existing loss mitigation methods will be effective in any of these new businesses.

Primus Financial's operating guidelines and S&P's and Moody's capital requirements are subject to change and may limit our growth. Additionally, a decline in our current counterparty credit ratings from S&P and Moody's would likely have a material adverse impact on our business and cause our revenues and earnings to decrease.

In order to obtain and maintain its counterparty credit ratings, Primus Financial has adopted operating guidelines, the terms of which have been agreed upon with S&P and Moody's. We cannot assure you that S&P and Moody's will not require changes to Primus Financial's operating guidelines or that, if such changes are made, Primus Financial will be able to comply with them. For example, if S&P and Moody's were to require Primus Financial to maintain additional capital to retain its AAA/Aaa ratings, we cannot be certain that we could raise additional capital when needed. Moreover, if Primus Financial suffers losses to such an extent that it is not in compliance with the capital criteria of its operating guidelines and it is not able to cure the capital deficiency in a timely manner, its operating guidelines require it to cease entering into new credit swaps (except for limited hedging transactions, as described in the operating guidelines). If the foregoing occur, S&P and Moody's could reduce or withdraw their AAA/Aaa credit ratings of Primus Financial which, in turn, would likely have a material adverse effect on our business and our financial performance.

We are dependent on counterparties' perception of our creditworthiness.

In establishing relationships, Primus Financial's counterparties generally analyze its financial condition prior to entering into a credit swap, establish credit limits, and monitor the appropriateness of these limits on an ongoing basis to limit the risk that it will be financially unable to make payments

in accordance with the credit swap. Once a counterparty reaches its credit exposure limit to Primus Financial, the counterparty may not enter into any additional transactions with Primus Financial until the counterparty credit limit is increased. In the event these counterparty credit limits are not increased as Primus Financial's credit swap portfolio expands or if limits are reduced, our financial performance would suffer. In addition, while there are buyers of credit swaps, such as our existing counterparties, that do not require us to post collateral, there are some buyers, including some of the leading participants in the credit swap market, that require even the highest rated counterparties from which they purchase credit swaps to post collateral. As of June 30, 2004, none of our existing counterparties have required us to post collateral. Under the operating guidelines agreed to with S&P and Moody's, Primus Financial cannot enter into credit swaps with any counterparty that would require it to post collateral. If our existing counterparties were to require us to post collateral, it may have a material adverse effect on us and our financial condition and restrict our growth.

We depend on a limited number of key executives.

The loss of any of our key personnel, including Thomas Jasper, our chief executive officer, and other individuals listed in the "Management" section of this prospectus, many of whom have long-standing relationships with our counterparties, could have a material adverse effect on us. As our business develops and expands, we believe that our success will depend greatly on our continued ability to attract and retain highly skilled and qualified personnel. We cannot assure you that we will continue to be able to employ key personnel or that we will be able to attract and retain qualified personnel in the future. We do not have "key person" life insurance to cover our executive officers. We have employment contracts with all of our executive officers. See "Management—Employment Agreements". Failure to retain or attract key personnel could have a material adverse effect on us.

We have a limited operating history, and our future performance is uncertain.

We and our subsidiaries are relatively new companies with a narrow business focus and limited operating histories. As a result, there is limited historical financial and operating information available to help you evaluate our past performance or to make a decision about an investment in our common shares. Companies in their initial stages of development present substantial business and financial risks and may suffer significant losses. New companies must successfully develop business relationships, establish operating procedures, hire staff, install management information and other systems, establish facilities and obtain licenses, as well as take other steps necessary to conduct their intended business activities. As a result of these risks, it is possible that we may not be successful in implementing our business strategy or in completing the development of the infrastructure necessary to run our business. In addition, because of our limited operating history, our historical financial results may not accurately predict our future performance. Because of our narrow business focus, our financial results are more sensitive to changes and downturns within our industry than companies with more diversified lines of business. For example, as a result of industry factors or factors specific to us, we may have to alter our anticipated methods of conducting our business, such as the nature, amount and types of risks we assume.

Our financial results depend on certain market conditions and growth in the credit swap market which are not within our control.

Our financial results depend to a significant degree upon the premiums that we receive on credit swaps in our portfolio. Historically, these premiums have been a function of credit spreads that change over time as a result of a variety of factors which we do not control, including changes in the overall economy, supply and demand conditions in the credit swap market and other factors affecting the corporate credit markets in general. If a low credit swap premium environment develops and persists, we may not be able to achieve profitable growth, which may have a material adverse effect on our financial condition and our results of operations. In addition, there can be no assurance that the credit swap market will continue to grow as it has historically or at all or that it will not decline. Any such

decline could have a material adverse effect on our business and financial condition and restrict our growth.

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Variations in credit swap premiums could cause our earnings to be inconsistent and our share price to fluctuate significantly.

Any event causing credit swap premiums to widen or tighten on an underlying Reference Entity in our portfolio will affect the fair value of related credit swaps and may increase the volatility of our earnings and, in turn, our share price. Common events that may cause our credit swap premiums to fluctuate include changes in national or regional economic conditions, industry cyclicality, credit events within an industry, changes in a Reference Entity's operating results, credit rating, cost of funds, management or any other factors leading investors to revise expectations about a Reference Entity's ability to pay principal and interest on its debt obligations when due. Changes in fair value of our credit swaps are recorded as unrealized gains or losses in our consolidated income statement. In 2003, a decline in premium levels caused an increase in the fair value of our credit swap portfolio which resulted in net unrealized gain of \$46.7 million, or 44% of our consolidated revenues for the year ended December 31, 2003. Wide fluctuations in the premium levels that we receive on credit swaps in our portfolio may have a material effect on our reported results of operations. For example, for the six months ended June 30, 2004, increasing premium levels on credit swaps in our portfolio caused a decrease in the fair value of our credit swap portfolio which contributed to a net unrealized loss of \$20.1 million.

We may require additional capital in the future which may not be available on favorable terms or at all.

If we require additional capital, we may need to raise additional funds through financings or curtail our growth and reduce our assets. Any equity or debt financing, if available at all, may be on terms that are not favorable to us. In the case of equity financings, dilution to our shareholders could result, and in any case such securities may have rights, preferences and privileges that are senior to those of the common shares offered hereby. If we cannot obtain adequate capital, our business, results of operations and financial condition could be adversely affected.

Certain of our existing shareholders control us and will continue to control us after this offering.

After the offering, our principal shareholders, directors and executive officers and entities affiliated with them will own 75.4% of our outstanding common shares (including 1,600,574 shares issuable within 60 days of September 23, 2004 upon the exercise of warrants for cash, restricted share units and options). As a result, these existing shareholders will continue, collectively, to be able to control the election of our directors, determine our corporate and management policies and determine, without the consent of our other shareholders, the outcome of any corporate action submitted to our shareholders for approval, including potential mergers, amalgamations or acquisitions, asset sales and other significant corporate transactions. These existing shareholders will also have sufficient voting power to amend our organizational documents. We cannot assure you that the interests of our existing shareholders will coincide with the interests of other holders of our common shares. This concentration of ownership may also discourage, delay or prevent a change in control of our company, which could deprive our shareholders of an opportunity to receive a premium for their common shares as part of a sale of our company and might reduce our share price.

The commercial and investment activities of some of our existing shareholders may compete with our business.

Certain of our existing shareholders engage in commercial activities and enter into transactions or agreements with us or in competition with us. Some of our existing shareholders or their affiliates may in the future sponsor other entities

engaged in the credit swap business, some of which may compete with us. Certain of our existing shareholders and their affiliates have also entered into agreements with and made investments in numerous companies that may compete with us. Our existing shareholders may also pursue acquisition opportunities that may be complementary to our business, and as a result, those acquisition opportunities may not be available to us. So long as our existing shareholders continue to own a significant amount of our outstanding common shares, they will continue to be able to influence strongly or effectively control our decisions.

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We do not intend to pay cash dividends on our common shares for the foreseeable future.

We do not intend to pay cash dividends on our common shares for the foreseeable future. We intend to retain all available funds for use in the operation and expansion of our business. Additionally, we are a holding company with no operations or significant assets other than our ownership of all of our subsidiaries. There are certain restrictions on Primus Financial contained in its operating guidelines which could affect the ability of Primus Guaranty to pay dividends in future years. The payment of dividends and making of distributions by each of Primus Guaranty and Primus Re is limited under Bermuda law and regulations. Any determination to pay cash dividends will be at the discretion of our board of directors and will be dependent upon our results of operations and cash flows, our financial position and capital requirements, general business conditions, legal, tax, regulatory and any contractual restrictions on the payment of dividends and any other factors our board of directors deems relevant. See "Tax Considerations" for other consequences of owning our common shares.

We may not be able to continue to compete in the credit swap market.

The credit swap market is highly competitive. We face competition from providers of similar products, including certain insurance companies and affiliates of our shareholders, and, to a limited extent, the credit swap dealers of commercial and investment banks. Many of these competitors are more established, have substantially greater financial resources than we do and have established ongoing relationships with market participants giving them ready access to the credit swap marketplace. In addition, while there are significant business obstacles to overcome in establishing a similar enterprise to ours, there are no regulatory impediments for any new entrants to the credit swap market. To the extent new participants enter the credit swap market, competition may intensify. While we believe we have a number of competitive advantages over new entrants, there can be no assurance that increased competition will not materially adversely affect our business and financial condition.

We cannot assure you that we will not incur losses as we begin selling credit swap protection on tranches of pools of obligations of Reference Entities and selling credit swaps for non-investment grade obligations. We also cannot assure you that we will not incur losses as we continue to purchase credit protection.

We cannot assure you that we will not incur losses when we begin selling credit swap protection on tranches of pools of obligations of Reference Entities. Additionally, we may enter into the credit swap market for non-investment grade obligations where the risk of credit losses is typically higher than in our existing business. If we do not accurately analyze the Reference Entity credit risks and assess the risks and leverage associated with selling credit protection for tranches of these pools, then we may suffer unexpected losses, which could adversely affect our results of operations and our credit ratings.

We have recently started on a limited basis to purchase credit swap protection to take advantage of short-term market fluctuations. The notional amount outstanding on credit swaps we purchased as short-term investments was \$217.1

million at June 30, 2004. This is a different activity from our normal course investing activity and is highly dependent on the absolute level of credit swap premiums, premium volatility and credit selection. We have a limited track record in purchasing protection and our performance to date has only added marginally to our net income. We cannot predict that opportunities will exist for us to buy protection nor can we assure you that we will not incur losses from this activity.

There can be no assurance that our diversification strategy will be effective or profitable.

We may experience delays, regulatory impediments and other complications in implementing our diversification strategy that could reduce our profitability and ultimately cause the strategy to fail. This may include obtaining rating agency approvals and required licenses and registrations, adapting our technology platform, hiring personnel and raising capital. We plan to diversify through the

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development and marketing of ancillary businesses, such as asset management for third parties and, in select instances, by acquisition. Each new business line requires the investment of additional capital and the significant involvement of our senior management to acquire or develop a new line of business and integrate it with our operations.

We may have difficulty executing our growth strategy and managing our growth effectively.

Continuing to grow our business will require increased investment in personnel and the assumption of risks that may be greater than we have previously assumed. Unless our growth results in an increase in our revenues that is proportionate to the increase in our costs associated with this growth, our gross margin, and our future profitability, will be adversely affected.

We may be adversely affected by foreign currency fluctuations.

We enter into credit swaps under which we are obligated to pay losses in currencies other than United States dollars. We may, from time to time, experience losses from fluctuations in the values of non-United States currencies, which could significantly affect our results of operations. Credit swap premiums on Euro-denominated credit swaps are paid to us in Euros and we do not convert such premiums into United States dollars. However, all of our capital is United States dollar-denominated. We cannot assure you that the credit swap premiums retained will be sufficient to cover Euro-denominated losses and that we will not incur significant conversion costs in order to cover such losses.

Our operations may become subject to increased regulation under federal and state law or existing regulations may change, which may result in administrative burdens, increased costs or other adverse consequences for us.

There can be no assurance that new legal or administrative interpretations or regulations under the United States commodities and securities laws, or other applicable legislation on the federal or state levels, or in Bermuda or other applicable jurisdictions, will not result in administrative burdens, increased costs, or other adverse consequences for us. Periodically, proposals have been made in Congress to enact legislation that would increase regulation of the credit swap market. We cannot predict what restrictions any such legislation, if adopted, would impose and the effect those restrictions would have on our business. In addition, federal statutes allocate responsibility for insurance regulation to the states and state insurance regulators may interpret their state insurance laws to include credit swaps as insurance contracts subject to regulation. Again, we cannot predict what effect any such regulation would have on our business.

Credit swap buyers typically use credit swaps to manage risk and regulatory capital requirements that limit their credit exposure to a Reference Entity. Regulatory changes that modify the permissible limits of credit risk exposure, or affect the use of credit swaps to reduce risk, may have a material adverse effect on our business.

In addition, we believe that we are not required to be registered as an "investment company" under the Investment Company Act of 1940. If we are required to so register as an investment company, we would have to comply with a variety of restrictions, including limitations on our capital structure, restrictions on our investments, prohibitions on transactions with affiliates and compliance requirements that could limit our growth and increase our costs. There is no assurance that we could function effectively if we are required to register as an investment company.

Risks Related to Taxation

Our status as a PFIC may result in significant additional tax costs for shareholders who are United States taxpayers.

Primus Guaranty and Primus Barbados are likely to be and remain PFICs for United States federal income tax purposes. There are potentially adverse United States federal income tax

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consequences of investing in a PFIC for a shareholder who is a United States taxpayer. These consequences include the following: (1) if a shareholder makes a QEF election with respect to Primus Guaranty and Primus Barbados, the shareholder will have to include annually in his or her taxable income an amount reflecting an allocable share of the income of Primus Guaranty or Primus Barbados, regardless of whether dividends are paid by Primus Guaranty to the shareholder, (2) if a shareholder makes a mark-to-market election with respect to Primus Guaranty, the shareholder will have to include annually in his or her taxable income an amount reflecting any year-end increases in the price of our common shares, regardless of whether dividends are paid by Primus Guaranty to the shareholder (moreover, it is unclear how such an election would affect the shareholder with respect to Primus Barbados), and (3) if a shareholder does not make a QEF election or a mark-to-market election, he or she may incur significant additional United States federal income taxes with respect to dividends on, or gain from, the sale or other disposition of, our common shares, or with respect to dividends from Primus Barbados to us, or with respect to our gain on any sale or other disposition of Primus Barbados shares. See "Tax Considerations—Taxation of Shareholders—United States Holders—Passive Foreign Investment Companies."

If we are found to be engaged in a United States business, we may be liable for significant United States taxes.

We believe that Primus Guaranty and Primus Barbados, both directly and through Primus Barbados' indirect ownership interest in Primus Financial (which for United States federal income tax purposes is treated as a partnership interest), will operate their businesses in a manner that should not result in their being treated as engaged in a trade or business within the United States. In particular, we believe that the sales of credit swaps by Primus Financial are best treated as transactions of an investor or trader and thus should not be treated as the conduct of a United States trade or business. Consequently, we do not expect to pay United States corporate income or branch profits tax on Primus Financial's income. However, because the determination of whether a foreign corporation is engaged in a trade or business in the United States is inherently factual and there are no definitive standards for making such a determination, there can be no assurance that the United States Internal Revenue Service, or IRS, will not contend successfully that Primus Guaranty, Primus Barbados or Primus Financial are engaged in a trade or business in the

United States. The maximum combined rate of United States corporate federal, state and local income tax that could apply to Primus Financial or Primus Barbados, were they found to be engaged in a United States business in New York City and subject to income tax, is approximately 46%. This combined income tax rate does not include United States branch profits tax that would be imposed on Primus Barbados were Primus Financial found to be engaged in a United States business and deemed to be making distributions to Primus Barbados. The branch profits tax, were it to apply, would apply at the rate of 30% on amounts deemed distributed, unless Primus Barbados then qualified for the benefits of the Barbados tax treaty with the United States, which would reduce the rate to 5%. The United States and Barbados recently executed a Second Protocol to amend the treaty, which is subject to ratification before becoming effective. If the Second Protocol becomes effective, Primus Barbados would not qualify for the treaty benefits discussed above and, if then subject to the branch profits tax as a result of being found to be engaged in a trade or business in the United States and deemed to have received distributions from Primus Financial, would be subject to the branch profits tax at a rate of 30%. See "Tax Considerations—Taxation of Primus Guaranty and its Subsidiaries—United States Taxation—Primus Guaranty, Primus Barbados and Primus Financial."

If the IRS successfully challenges the treatment Primus Financial has adopted for its credit swap transactions, the timing and character of taxable income recognized by Primus Financial could be adversely affected.

Consistent with its treatment of the credit swaps sold by Primus Financial as the sale of options for United States federal income tax purposes, we have determined that in general Primus Financial will recognize income or loss as a protection seller only upon default or termination of the credit swaps. There is no definitive authority in support of the treatment by Primus Financial of its credit

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swaps as options for United States federal income tax purposes, and we do not intend to seek a ruling from the IRS on this point. In addition, the IRS has been studying the treatment of derivative transactions generally, including credit swaps, and has recently issued a notice requesting submissions from taxpayers regarding the manner in which they conduct their credit swap activities and indicating that the United States Department of the Treasury and the IRS are contemplating issuing specific guidance in this area. No assurance can be given as to whether or when such guidance may be issued, whether it would be applied retroactively or whether it will be adverse to Primus Financial. Certain proposals under discussion could be inconsistent with the tax treatment adopted by Primus Financial. If the IRS were to assert successfully that the credit swaps sold by Primus Financial should be treated differently or these proposals were adopted, (1) the timing of the income recognized by Primus Financial could be accelerated, (2) the character of this income could be altered and (3) Primus Barbados, as a non-United States person, could be subject to United States income or withholding tax at the rate of 30%. In addition, were these changes in character to apply and were Primus Barbados (through its investment in Primus Financial) found to be engaged in a United States trade or business, Primus Barbados's recognition of taxable income would be accelerated. See "Tax Considerations—Taxation of Primus Guaranty and its Subsidiaries—United States Taxation—Primus Guaranty, Primus Barbados and Primus Financial."

Prospective investors are urged to consult their own tax advisors concerning their particular circumstances and the United States federal, state, local and non-United States tax consequences to them of owning and disposing of our common shares.

Risks Related to Our Status as a Bermuda Company

All references in this section to Primus Guaranty do not include its combined operations.

It may be difficult to enforce service of process and enforcement of judgments against us and our officers and directors.

Because Primus Guaranty is organized under the laws of Bermuda, it may not be possible to enforce court judgments obtained in the United States against Primus Guaranty based on the civil liability provisions of the federal or state securities laws of the United States in Bermuda or in countries other than the United States where Primus Guaranty has assets. In addition, there is some doubt as to whether the courts of Bermuda and other countries would recognize or enforce judgments of United States courts obtained against Primus Guaranty or its directors or officers based on the civil liabilities provisions of the federal or state securities laws of the United States, or would hear actions against Primus Guaranty or those persons based on those laws. We have been advised by our legal advisors in Bermuda that the United States and Bermuda do not currently have a treaty providing for the reciprocal recognition and enforcement of judgments in civil and commercial matters. Therefore, a final judgment for the payment of money rendered by any federal or state court in the United States based on civil liability, whether or not based solely on United States federal or state securities law, would not automatically be enforceable in Bermuda. There are grounds upon which a Bermuda court may not enforce the judgments of United States courts and some remedies available under the laws of United States jurisdictions, including some remedies available under United States federal securities laws, may not be permitted under Bermuda courts as contrary to public policy in Bermuda. Similarly, those judgments may not be enforceable in countries other than the United States where Primus Guaranty has assets. Further, no claim may be brought in Bermuda by or against Primus Guaranty or its directors and officers in the first instance for violation of United States federal securities laws because these laws have no extraterritorial application under Bermuda law and do not have force of law in Bermuda; however, a Bermuda court may impose civil liability, including the possibility of monetary damages, on Primus Guaranty or its directors and officers if the facts alleged in a complaint constitute or give rise to a cause of action under Bermuda law.

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

The Companies Act 1981, as amended, of Bermuda, or the Bermuda Companies Act, which applies to Primus Guaranty and Primus Re, differs in certain material respects from laws generally

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applicable to United States corporations and their shareholders. As a result of these differences, United States persons who own our common shares may have more difficulty protecting their interests than would United States persons who own common shares of a United States corporation. To further understand the risks associated with United States persons who own our common shares, see "Description of Share Capital—Differences between Bermuda and Delaware Corporate Law" for more information on the differences between Bermuda and Delaware corporate laws.

We may become subject to taxes in Bermuda after 2016, which may have a material adverse effect on our financial condition and operating results and on an investment in our common shares.

The Bermuda Minister of Finance, under the Exempted Undertakings Tax Protection Act 1966, as amended, of Bermuda, has given each of Primus Guaranty and Primus Re an assurance that if any legislation is enacted in Bermuda that would impose tax computed on profits or income, or computed on any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax, then subject to certain limitations, the imposition of any such tax will not be applicable to Primus Guaranty, Primus Re or any of their respective operations, shares, debentures or other obligations until March 28, 2016. Given the limited duration of the Minister of Finance's

assurance, we cannot be certain that we will not be subject to any Bermuda tax after March 28, 2016. Since we are incorporated in Bermuda, we will be subject to changes of law or regulation in Bermuda that may have an adverse impact on our operations, including imposition of tax liability. See "Tax Considerations—Taxation of Primus Guaranty and Its Subsidiaries—Bermuda Taxation."

The effect of Bermuda's letter of commitment to the OECD to eliminate harmful tax practices is uncertain and could adversely affect our tax status in Bermuda.

A number of multinational organizations, including the Organization for Economic Cooperation and Development, the European Union, the Financial Action Task Force and the Financial Stability Forum, have all recently identified some countries as not participating in adequate information exchange, engaging in harmful tax practices or not maintaining adequate controls to prevent corruption, such as money laundering activities. The Organization for Economic Cooperation and Development, which is commonly referred to as the OECD, has published reports and launched a global dialogue among member and non-member countries on measures to limit harmful tax competition. These measures are largely directed at counteracting the effects of tax havens and preferential tax regimes in countries around the world. In the OECD's report published in June 2000, Bermuda was not listed, and continues not to be listed as an "uncooperative tax haven" because it had previously signed a letter committing itself to eliminate harmful tax practices by the end of 2005, and to embrace international tax standards for transparency, exchange of information and the elimination of any aspects of the regimes for financial and other services that attract business with no substantial domestic activity. However, it is possible that the OECD could change its view in the future and decide to list Bermuda as an uncooperative tax haven, or that one of the other multinational organizations could take a different view from the OECD and decide to recommend sanctions against Bermuda. We are not able to predict what changes will arise from the commitment or whether such changes will subject us to additional taxes and reduce our net income.

Risks Related to this Offering

We cannot predict how actively our common shares will trade, the possible volatility of our share price or the effect that these factors may have on the value of the common shares you purchase in this offering.

The public offering price of our common shares offered by this prospectus will be determined by negotiation between us and the representatives for the underwriters. The price of our common shares after this offering may fluctuate widely. The reasons for these fluctuations may include the investment community's perception of our prospects and of our industry in general. Differences between our actual operating results and those expected by investors and analysts and changes in analysts' recommendations or projections could also affect the price of our common shares. Other factors potentially causing volatility in the price for our common shares may include:

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- changes in general economic or market conditions and broad market fluctuations, particularly those affecting the prices of the common shares of companies engaged in businesses similar or related to our business;
 - how actively our common shares trade; and
 - the research reports that industry or securities analysts publish about us or our business.

Our common shares have been approved for listing on the New York Stock Exchange, or NYSE. Such a listing does not, however, guarantee that an active and liquid trading market for our common shares will develop.

Substantial future sales of our common shares in the public market could cause our share price to fall.

Additional sales of our common shares in the public market after this offering, or the perception that these sales could occur, could cause the market price of our common shares to decline. Upon completion of this offering, we will have 42,787,843 common shares outstanding. All shares sold in this offering will be freely transferable without restriction or additional registration under the Securities Act of 1933, as amended, or the Securities Act, or after this offering will be available for sale, subject to 180-day lock-up agreements under which our directors, executive officers and all except one of our shareholders have agreed not to sell or otherwise dispose of their common shares in the public market, and subject to, in the case of our directors and executive officers and our larger shareholders, the manner of sale and notice requirements and the volume limitations on sales of shares contained in Rule 144 under the Securities Act. One of our shareholders, who owns 15,104 of our common shares, is subject to lock-up for a period of 90 days after the date of this prospectus.

Any or all of these common shares may be released prior to expiration of such periods at the discretion of Lehman Brothers Inc., or Lehman Brothers. To the extent common shares are released before the expiration of the lock-up period and these common shares are sold into the market, the market price of our common shares could decline. Immediately following the 90-day lock-up period, 15,104 of our common shares outstanding after this offering will become available for sale. Immediately following the 180-day lock-up period, 34,238,403 of our common shares outstanding after this offering will become available for sale assuming the cashless exercise of all outstanding warrants. Such number includes 477,833 restricted share units that will have vested prior to the expiration of the 180-day lock-up period and 285,073 options that will be exercisable upon the expiration of the 180-day lock-up period. The remaining common shares will become available for sale at various times thereafter upon the expiration of one-year holding periods.

In addition, beginning 180 days after this offering, the holders of approximately 36,528,405 common shares, which are not freely tradeable under the Securities Act, will be entitled to rights to cause us to register the sale of those common shares under the Securities Act. Such number includes (1) 1,414,746 outstanding warrants if exercised for cash, (2) 234,302 unvested options and (3) 237,515 unvested restricted share units. Registration of these common shares under the Securities Act would result in these common shares, other than common shares purchased by our affiliates, becoming freely tradeable without restriction under the Securities Act immediately upon the effectiveness of the registration. See "Shares Eligible for Future Sale".

Purchasers in this offering will immediately experience substantial dilution in net tangible book value.

Because our common shares have in the past been sold at prices substantially lower than the initial public offering price that you will pay, you will suffer immediate dilution of \$6.70 per share in pro forma net tangible book value, based on an assumed initial offering price of \$14.50 per share, the midpoint of the range set forth on the cover page of this prospectus. The exercise of outstanding options and warrants may result in further dilution. See "Dilution".

Our anti-takeover provisions could prevent or delay a change of control of our company, even if a change of control would be beneficial to our shareholders, and could impede an attempt to replace or remove our directors, which could diminish the value of our common shares.

Our Bye-laws contain provisions that may make it more difficult for shareholders to replace directors even if the shareholders consider it beneficial to do so. In addition, these provisions could

delay or prevent a change of control that a shareholder might consider favorable. For example, these provisions may prevent a shareholder from receiving the benefit from any premium over the market price of our common shares offered by a bidder in a potential takeover. Even in the absence of an attempt to effect a change in management or a takeover attempt, these provisions may adversely affect the prevailing market price of our common shares if they are viewed as discouraging takeover attempts in the future.

For example, our Bye-laws contain the following provisions that could have such an effect:

- election of our directors is staggered, meaning that only one-third of our directors are elected each year;
- shareholders have only limited ability to remove directors;
- authorization, without prior shareholder approval, to create and issue preferred shares with voting or other rights or preferences that could impede the success of any attempt to acquire us or change our control, commonly referred to as "blank check" preferred shares;
- our directors may decline to approve or register the transfer of any common shares on our share register if it appears to the board of directors that any adverse tax, regulatory or legal consequences to us, any of our subsidiaries or any registered owner of our shares or its affiliates, would result from such transfer (other than such as our board of directors considers to be minimal); and
- business combinations with persons who acquire 15% or more of our common shares without our board's approval are restricted for three years.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements that involve substantial risks and uncertainties. All statements, other than statements of historical facts, included in this prospectus regarding our strategy, future operations, future financial position, future revenues, projected costs, prospects, plans and objectives of management are forward-looking statements. The words "anticipate," "believe," "estimate," "expect," "intend," "may," "plan," "project," "will," "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements we make. We have included important factors in the cautionary statements included in this prospectus, particularly in the "Risk Factors" section, that we believe could cause actual results or events to differ materially from the forward-looking statements that we make. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make. We do not assume any obligation to update any forward-looking statements.

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USE OF PROCEEDS

We expect that the net proceeds we will receive from the sale of the common shares offered by us will be approximately \$120.0 million, based on an assumed initial public offering price of \$14.50 per share, the midpoint of the range set forth on the cover page of this prospectus, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. We intend to use at least \$60.0 million of the net proceeds of this offering to provide additional capital to Primus Financial in order to increase its capacity to sell additional credit swaps. Primus Financial will invest this additional capital in accordance with its operating guidelines in United States government securities and money market instruments. The remainder of the proceeds from the offering will be used as working capital and for general corporate purposes, including providing additional capital to Primus Financial to enable it to further expand its credit swap business and to pursue opportunities in complementary businesses, such as asset management for third parties and selling credit swaps referencing a broader range of obligations. See "Business – Business Strategy". While specific amounts have not been allocated for these additional purposes, we believe that the proceeds from this offering will provide sufficient flexibility to our management to dedicate appropriate amounts to the specific purposes enumerated above as suitable opportunities arise. We will not receive any of the proceeds from the sale of common shares by the selling shareholders.

Pending use of the net proceeds as described above, we intend to invest the net proceeds of this offering, not contributed to Primus Financial, in United States government securities and money market instruments.

DIVIDEND POLICY

We intend to retain all available funds for use in the operation and expansion of our business and do not anticipate paying any cash dividends for the foreseeable future. Any determination to pay cash dividends will be at the discretion of our board of directors and will be dependent upon our results of operations and cash flows, our financial position and capital requirements, general business conditions, legal, tax, regulatory and any contractual restrictions on the payment of dividends and any other factors our board of directors deems relevant. See "Prospectus Summary—Notice to United States Investors—Tax Consequences of Owning Our Common Shares".

We are a holding company and have no direct operations. Our ability to pay dividends depends, in part, on the ability of our subsidiaries to pay distributions to us.

Primus Financial's operating guidelines restrict the payment of dividends to once per year. The payment of dividends by Primus Financial is contingent upon a dividend payment not resulting in a capital shortfall under its operating guidelines and the dividend not exceeding 25% of Primus Financial's net income (excluding mark-to-market unrealized gains or losses on credit swaps). Primus Financial is further restricted from paying dividends under the terms of its Floating Rate Cumulative Preferred Stock, or PFP Cumulative Preferred Stock, unless all of the cumulative distributions on the PFP Cumulative Preferred Stock have been previously made or set aside. Primus Financial's \$37.5 million credit facility also restricts payment of dividends by Primus Financial except as permitted by its operating guidelines. Our insurance subsidiary, Primus Re, is also subject to significant regulatory restrictions limiting its ability to declare and pay dividends.

Further, we are subject to Bermuda law and regulatory constraints that will affect our ability to pay dividends on our common shares and make other payments. Under the Bermuda Companies Act, each of Primus Guaranty and Primus Re may not declare or pay a dividend out of distributable reserves if there are reasonable grounds for believing that each of us is, or would after the payment be, unable to pay our respective liabilities as they become due; or if the realizable value of our respective assets would thereby be less than the aggregate of our respective liabilities and issued share capital and share premium accounts. See "Business—Certain Bermuda Law Considerations".

CAPITALIZATION

The following table sets forth our capitalization as of June 30, 2004:

- on an actual basis;
- on a pro forma basis to give effect to (1) a one for eight reverse share split to be effected immediately prior to the completion of this offering (with fractional shares satisfied in cash); and (2) the automatic conversion of all outstanding Series A preferred shares into an aggregate of 29,980,691 common shares upon completion of this offering; and (3) Primus Financial's issuance of AAA/Aaa rated subordinated deferrable interest notes.
- on a pro forma as adjusted basis to give effect to (1) our sale of a total of 9,143,493 common shares in this offering at an assumed public offering price of \$14.50 per share, the midpoint of the range set forth on the cover of the prospectus; (2) the issuance of an aggregate of 9,372 common shares to our non-employee directors upon the completion of this offering; and (3) the net reduction of 3,646 common shares in August and September 2004.

This table should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and the notes thereto included elsewhere in this prospectus.

(\$ in thousands)	As of June 30, 2004		
	Actual	Pro Forma	As Adjusted
Long-term debt obligations of subsidiary	\$ —	\$ 75,000	\$ 75,000
Preferred shares of subsidiary	\$ 98,521	\$ 98,521	\$ 98,521
Shareholders' equity:			
Common shares, \$0.01 par value, 500,000,000 shares authorized, 29,263,479 shares issued and outstanding, actual; \$0.08 par value, 62,500,000 shares authorized, 33,638,624 shares issued and outstanding, pro forma; \$0.08 par value, 62,500,000 shares authorized, 42,787,843 shares issued and outstanding, pro forma as adjusted	331	2,729	3,460
Additional paid-in-capital	8,569	150,079	269,348
Series A Convertible Voting Preferred Shares, \$0.01 par value, 100,000,000 shares authorized, 6,212,000 shares issued and outstanding, actual; none authorized, issued and outstanding, pro forma and pro forma as adjusted	143,908	—	—
Warrants	612	612	612
Retained earnings	60,217	60,217	60,217
Total shareholders' equity	213,637	213,637	333,637
Total preferred shares of subsidiary and shareholders' equity	\$ 312,158	\$ 312,158	\$ 432,158
Total capitalization	\$ 312,158	\$ 387,158	\$ 507,158

The number of common shares excludes:

- 531,875 common shares issuable upon exercise of options outstanding as of June 30, 2004, under our 2002 stock incentive plan, with a weighted average exercise price of \$8.65 per share;
- 1,414,746 common shares issuable upon exercise of warrants outstanding as of June 30, 2004, with an exercise price of \$5.18 per share and an expiration date of March 14, 2007;

- 728,315 common shares issuable upon exercise of restricted share units outstanding as of June 30, 2004; and
- 5,134,353 additional common shares reserved for issuance under our employee incentive plan following the completion of this offering.

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DILUTION

If you invest in our common shares, your interest will be diluted to the extent of the difference between the public offering price per share of our common shares and the pro forma as adjusted net tangible book value per share of our common shares immediately after this offering. Pro forma net tangible book value per share represents the amount of our total tangible assets less total liabilities, divided by the pro forma number of shares of our common shares outstanding. Investors participating in this offering will incur immediate, substantial dilution.

Our net tangible book value at June 30, 2004, before adjustment for this offering, was approximately \$213,637 thousand, or approximately \$6.35 per share, after giving effect to the conversion of all outstanding shares of our Series A preferred shares into common shares upon the closing of this offering. After giving effect to the sale of common shares in this offering, at an assumed initial public offering price of \$14.50 per share, the midpoint of the range set forth on the cover page of this prospectus, and after deducting the estimated offering expenses, our as adjusted net tangible book value at June 30, 2004 would have been \$333,637 thousand or \$7.80 per share. This represents an increase in net tangible book value of \$1.45 per share to our existing shareholders and an immediate dilution (i.e., the difference between the public offering price per unit and the net tangible book value per share adjusted for this offering) at June 30, 2004 of \$6.70 per share to purchasers of the common shares offered hereby. The following table illustrates this per share dilution:

Assumed initial public offering price per share		\$ 14.50
Net tangible book value per share at June 30, 2004	\$ 6.35	
Increase in net tangible book value per share attributable to the new investors	\$ 1.45	
As adjusted net tangible book value per share after this offering		\$ 7.80
Dilution per share to new investors		\$ 6.70

The above table excludes the possible exercise of 1,414,746 outstanding warrants to purchase our common shares which have an exercise price of \$5.18 per share and expire on March 14, 2007.

The following table summarizes at June 30, 2004, after giving effect to our sale of 9,143,493 common shares at an assumed initial public offering price of \$14.50 per share, the midpoint of the range set forth on the cover page of this prospectus, the number of common shares purchased from us, the total consideration paid to us for those common shares and the consideration given by the existing shareholders and by the new investors assuming approximately 42,787,843 common shares are outstanding:

Shares Purchased	Total Consideration	Average Price
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	Number	Percent	Amount	Percent	Per Share
Existing shareholders	33,644,350	78.6%	\$166,733,000	55.7%	\$ 4.96
New investors	9,143,493	21.4	132,580,649	44.3	14.50
Total	42,787,843	100.00%	\$299,313,649	100.00%	

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SELECTED HISTORICAL CONSOLIDATED FINANCIAL DATA

The following tables present our historical financial and operating data as of the dates or for the periods indicated. We derived the data for the years ended December 31, 2003, 2002 and 2001 from our consolidated financial statements, which have been prepared in accordance with United States GAAP and audited by Ernst & Young LLP. Our historical financial statements for the years ended December 31, 2000 and 1999 have not been audited, but, in the opinion of management, contain all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of our results of operations for these periods and financial position as of those dates. The statement of operations data for the six months ended June 30, 2004 and 2003, and the balance sheet data as of June 30, 2004, are derived from, and are qualified by reference to, our unaudited consolidated financial statements included elsewhere in this prospectus. The unaudited consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, that we consider necessary for the fair presentation of our financial position and results of operations for these periods. The results of operations for past accounting periods are not necessarily indicative of the results to be expected for any future accounting periods. Until March 2002, we were in a development stage. We were capitalized on March 14, 2002 and began to sell credit swaps in June 2002. The following information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes appearing elsewhere in this prospectus.

	Six Months Ended June 30,			Year Ended December 31,			
	2004	2003	2003	2002	2001	2000	1999
(\$ in thousands, except per share data)							
Consolidated Statements of Operations Data:							
Revenues:							
Net credit swap revenue	\$ 2,835	\$ 57,746	\$103,326	\$ 14,761	\$ —	\$ —	\$ —
Interest income earned	1,368	1,308	2,617	1,610	2	5	3
Other income	236	54	107	12	—	—	—
Total revenues	\$ 4,439	\$ 59,108	\$106,050	\$ 16,383	\$ 2	\$ 5	\$ 3
Expenses:							
Employee compensation	\$ 7,284	\$ 5,032	\$ 11,701	\$ 8,156	\$ 1,020	\$ 768	\$ 47
Other expenses	3,979	6,076	14,196	11,042	1,769	2,341	954
Total expenses	\$ 11,263	\$ 11,108	\$ 25,897	\$ 19,198	\$ 2,789	\$ 3,109	\$ 1,001
	\$ (1,147)	\$ (832)	\$ (1,854)	\$ —	\$ —	\$ —	\$ —

Distributions on preferred securities of subsidiary

Income (loss) before benefit (provision) for income taxes	\$ (7,971)	\$ 47,168	\$ 78,299	\$ (2,815)	\$ (2,787)	\$ (3,104)	\$ (998)
Benefit (provision) for income taxes	(117)	(105)	172	(254)	—	—	—
Net income (loss)	\$ (8,088)	\$ 47,063	\$ 78,471	\$ (3,069)	\$ (2,787)	\$ (3,104)	\$ (998)
Basic earnings (loss) per share	\$ (2.41)	\$ 18.71	\$ 31.18	\$ (1.22)	\$ (1.12)	\$ (258.66)	\$ (83.16)
Diluted earnings (loss) per share	\$ (2.41)	\$ 1.39	\$ 2.33	\$ (1.22)	\$ (1.12)	\$ (258.66)	\$ (83.16)

Weighted average number of common shares outstanding:

Basic	3,353	2,515	2,517	2,510	2,479	12	12
Diluted	3,353	33,843	33,737	2,510	2,479	12	12

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	As of June 30,			As of December 31,			
	2004	2003	2003	2002	2001	2000	1999
(\$ in thousands, except per share data)							
Balance Sheet Data:							
Assets							
Cash and cash equivalents	\$ 272,523	\$ 236,255	\$ 257,967	\$ 220,975	\$ 136	\$ 138	\$ 123
Short-term investments	3,441	—	3,968	—	—	—	—
Unrealized gain on credit swaps, at fair value	29,121	31,250	46,594	5,705	—	—	—
Fixed assets and capitalized software	6,600	11,307	7,124	12,322	—	—	—
Other assets	8,348	5,368	5,776	5,859	—	—	—
Total assets	\$ 320,033	\$ 284,180	\$ 321,429	\$ 244,861	\$ 136	\$ 138	\$ 123
Liabilities and shareholders' equity							
Unrealized loss on credit swaps, at fair value	\$ 2,664	\$ 22	\$ 68	\$ 5,918	\$ —	\$ —	\$ —
Other liabilities	5,211	2,810	8,002	5,191	6,981	4,328	1,208
Total liabilities	\$ 7,875	\$ 2,832	\$ 8,070	\$ 11,109	\$ 6,981	\$ 4,328	\$ 1,208
Preferred securities of subsidiary	\$ 98,521	\$ 98,521	\$ 98,521	\$ 98,521	\$ —	\$ —	\$ —
Shareholders' equity							
Common stock	\$ 331	\$ 218	\$ 230	\$ 208	\$ 240	\$ 12	\$ 12
Convertible preferred stock	143,908	143,908	143,908	143,908	12	—	—

Retained earnings (accumulated deficit)	60,217	36,897	68,305	(10,166)	(7,097)	(4,310)	(1,205)
Additional paid-in-capital	8,569	735	1,325	211	—	108	108
Warrants	612	1,070	1,070	1,070	—	—	—
Total shareholders' equity (deficit)	\$ 213,637	\$ 182,827	\$ 214,838	\$ 135,231	\$ (6,845)	\$ (4,190)	\$ (1,085)
Total liabilities, preferred securities of subsidiary and shareholders' equity	\$ 320,033	\$ 284,180	\$ 321,429	\$ 244,861	\$ 136	\$ 138	\$ 123
Per Share Data:							
Book value per share ⁽¹⁾	\$ 58.40	\$ 70.24	\$ 82.63	\$ 51.95	\$ (2.28)	\$ (349.17)	\$ (90.42)
Diluted book value per share ⁽²⁾	\$ 6.04	\$ 5.40	\$ 6.41	\$ 4.23	\$ (2.28)	\$ (349.17)	\$ (90.42)

(1) Book value per share is based on total shareholders' equity divided by basic common shares outstanding. For years prior to 2001, the only shares issued were 12,000 common shares, par value \$1.00 per share, issued to the founder. This total has not been adjusted for the reverse share split.

(2) Diluted book value per share is based on total shareholders' equity plus the assumed exercise of all dilutive options and warrants divided by diluted common shares outstanding.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and accompanying notes which appear elsewhere in this prospectus. It contains forward-looking statements that involve risks and uncertainties. Please see "Special Note Regarding Forward-Looking Statements" for more information. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those discussed below and elsewhere in this prospectus, particularly under the headings "Risk Factors" and "Special Note Regarding Forward-Looking Statements."

Overview

Our principal business is selling credit protection under which we assume the risk of default on investment grade credit obligations through our subsidiary, Primus Financial. Primus Financial has the highest counterparty credit ratings offered by S&P (AAA) and Moody's (Aaa) and is managed by an experienced team of professionals who have expertise in credit analysis, trading, risk management and market analysis.

In exchange for a fixed quarterly premium we agree, upon a payment default or other credit event (e.g., bankruptcy, moratorium or repudiation) affecting a Reference Entity, to pay a counterparty the notional amount for a specified debt obligation of the Reference Entity. Under these circumstances, the obligation is likely to have a market value of substantially less than par and we would incur an economic loss as a result. We monitor the credit swap market and the credit quality of individual Reference Entities on a continuous basis. If we believe there is an increased probability of a Reference Entity credit event, we may offset our risk through the purchase of credit swaps with respect to the

specific Reference Entity or by terminating the related credit swaps we have sold. As of June 30, 2004, we had not suffered a credit event on any credit swap we have sold and our purchases of credit swaps to offset risk have been limited in scope. Further details are included in our discussion of operating results.

The market for credit swaps and, consequently, market credit swap premium levels are affected by a number of factors, including defaults by Reference Entities, volatility in the capital markets, economic conditions, changes in interest rates and political uncertainties. During 2002, market credit swap premium levels were generally high compared with historical averages. This presented us with an opportunity to sell credit swaps at attractive levels and, by December 31, 2002, the notional amount of our outstanding portfolio of credit swaps was \$4.7 billion. However, throughout 2003 there was a fairly steady decline in market credit swap premium levels. The decline in market credit swap premium levels increased the fair value of our credit swap portfolio as the credit swaps we had written during 2002 and the early part of 2003 appreciated in value. During 2003, we slowed the pace of portfolio growth as the market credit swap premium levels became less attractive relative to the risks borne. At December 31, 2003, Primus Financial had \$6.4 billion (in notional amount) of credit swaps outstanding with a weighted average remaining life of 2.8 years. In the first half of 2004, we have seen a general increase in market credit swap premium levels. This has presented more attractive opportunities to sell credit swaps and we have increased the pace of portfolio growth in 2004. At June 30, 2004, Primus Financial had \$8.7 billion of credit swaps outstanding with a weighted average remaining life of 2.8 years.

We expanded the range of our activities in 2003 to include the sale of Euro-denominated credit swaps, the purchase of credit swaps as short-term investments and the sale of financial guaranty insurance protection. We started selling Euro-denominated credit swaps in February 2003 and by June 30, 2004, Euro-denominated credit swaps comprised 23.8% of the notional amount of our credit swap portfolio. Toward the end of 2003, we also began to purchase credit swaps as short-term investments by buying credit swaps on selected Reference Entities at, we believe, relatively low credit swap premium levels with the expectation that the credit swap premium levels on these Reference Entities will rise. If the premium levels rise, we will be able to terminate the credit swaps at a gain. At June 30, 2004, we had purchased credit swaps as short-term investments on a notional principal

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amount of \$217.1 million. We carry these credit swaps at fair value, using valuation techniques similar to those used for the credit swaps we have sold. Additionally, in 2003 Primus Re issued its first financial guaranty protection on a total notional amount of obligations equaling \$56.5 million.

Our net income is determined primarily by the growth in our credit swap portfolio, the premium levels at which the credit swaps in our portfolio are sold, our success in developing diversified sources of revenue and the expenses we incur. The growth in our portfolio depends on the growth in the overall market for credit swaps, coupled with our willingness and capacity to assume additional credit risk with respect to particular Reference Entities, industries and countries. Our pace of growth may also be affected by our ability to continue to attract and expand counterparty lines, which are influenced by our capital resources, our credit ratings and counterparty demand for credit protection.

Market credit swap premium levels are driven by a number of factors. See "—Critical Accounting Policies—Valuation of Credit Swaps".

Our expenses have grown since we commenced business and we expect our expenses to continue to grow, both in order to implement our diversification strategy and as a result of additional costs of being a public company, such as additional reporting and governance requirements. We do not expect significant expense increases in the immediate

future due to the expansion of our current lines of business.

Our net income is also significantly influenced by the periodic change in the fair value of our portfolio, based primarily on market credit swap premium levels at the time the portfolio is valued. We have experienced considerable volatility in market credit swap premium levels over time, and therefore we may experience considerable volatility in reported net income. We believe that the volatility of net income is not necessarily indicative of the underlying performance in meeting our business strategy. See "—Additional Information".

We are in the preliminary stages of evaluating selling credit swaps referencing obligations of Reference Entities that are below investment grade and have not definitely determined whether we will sell such credit swaps. Accordingly, we do not know nor are we able to predict the timing, if any, of engaging in this activity or the impact selling credit swaps referencing obligations of entities that are below investment grade will have on our results of operations.

Revenues

We record revenues or losses from our credit swaps as net credit swap revenue (loss) in our statement of operations. This item comprises the premiums earned and premium expense on credit swaps, gains or losses realized as a result of the termination of credit swaps and changes in the fair value of our credit swaps. Our experience is that considerable fluctuation may occur in the fair values of credit swaps from period to period and, as a consequence, the reader of our financial statements should not infer future results from historical net credit swap revenues or losses. See "Risk Factors—Risks Related to our Business—Variations in credit swap premiums could cause our earnings to be inconsistent and our share price to fluctuate significantly".

We receive premium income from the credit swaps we sell. In general, premiums are received quarterly in arrears and accrued daily into income. In accordance with United States GAAP, we carry our credit swaps on our balance sheet at their fair value. Changes in the fair value of our credit swap portfolio are recorded as unrealized gains or losses in our consolidated income statement. If a credit swap has an increase in fair value during a period, the increase will add to our net credit swap revenues for that period. Conversely, if a credit swap has a decline in fair value during the period, the decline will subtract from our net credit swap revenues for that period. Changes in the fair value of our credit swap portfolio are a function of the notional amount and composition of the portfolio and prevailing market credit swap premiums for comparable credit swaps. We generally hold the credit swaps we sell to maturity, at which point, assuming no credit event has occurred, the cumulative unrealized gains and losses on each credit swap would equal zero. In general, we aggregate the fair values of individual credit swaps by counterparty. If the aggregate total of fair values for a counterparty is a net gain, the total is recorded as a component of unrealized gains on credit swaps, at

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fair value. If the aggregate total of fair values for a counterparty is a net loss, the total is recorded as a component of unrealized losses on credit swaps, at fair value. Aggregation by counterparty is applied where an executed ISDA master agreement is in place with the counterparty. In instances where we do not yet have an executed ISDA master agreement with the counterparty, the fair values of individual credit swap transactions are recorded as components of unrealized gains or losses on credit swaps, at fair value, dependent upon whether the individual contract was at a gain or a loss. As of June 30, 2004, we did not have any counterparties with whom we had not yet executed ISDA master agreements.

As a general rule, when we sell credit default protection, it is our intention to maintain the transaction until maturity. However, there are two sets of circumstances in which we could elect to terminate transactions prior to maturity, and

we monitor our portfolio on a continuing basis to assess whether those circumstances are present.

First, whenever we receive new information suggesting that the credit quality of the underlying risk has deteriorated to a material degree, we consider the possibility of terminating the transaction, usually at a loss, to avoid the larger loss that could result if the credit swap were to remain in place until a credit event occurs. The principal factor that governs our decision regarding termination in these circumstances is whether we believe that the underlying risk has become substantially greater than the level of risk we would choose to assume in entering into a new sale of credit default protection. Over our two years of operating history, we have terminated less than 1% of the notional amount of credit swaps under which we sold credit default protection due to credit considerations.

Second, we may also terminate a transaction for which we have an unrealized gain based on one or more of the following considerations: the likelihood of further gains arising from the position, our view as to whether the capital dedicated to the position could be profitably reallocated, our total exposure to a particular Reference Entity, the total size of our portfolio in relation to our capital and the total size of our swap positions and exposures with a particular counterparty which might be reduced so that they might enter into additional swaps with us. We refer to terminations effected under these circumstances as "resizing" or "rebalancing". Much of our resizing occurred during the second and third quarters of 2003, when market credit swap premium levels had dropped dramatically from their historic 2002 highs. Over our two years of operating history, we have terminated less than 10% of credit swaps under which we sold credit default protection based on resizing or rebalancing considerations.

We terminate (or offset) a credit swap in any one of three ways. We may negotiate an agreed termination through the original counterparty (an unwind). We may negotiate an assignment and novation of our rights and obligations under the credit swap to a third party (an assignment). As an alternative to terminating a transaction, we may enter into an equal and opposite transaction with a third party under which we purchase credit default protection on terms that match the terms of the original transaction (an offset). In this last case, both sides of the position may subsequently be unwound or assigned.

In the event of an unwind or assignment, we pay or receive a cash settlement negotiated with the counterparty or assignee, based on the fair value of the credit swap contract and the accrued premium on the swap contract at the time of negotiation. The amounts we pay or receive are recorded as a realization of fair value and as a realization of accrued premiums in the period in which the termination occurs.

We invest our cash in short-term, high quality fixed income instruments. The yield on our investments is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. We invest in obligations of the United States or direct obligations of United States agencies rated AAA and Aaa by S&P and Moody's, respectively, commercial paper rated A-1 and P-1 by S&P and Moody's, respectively, and money market funds.

When we purchase credit protection as short-term investments, we incur the cost of paying premiums until we terminate the purchased protection. We undertake these transactions in the expectation that the market credit swap premium level for the Reference Entity will rise subsequent

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to our purchase of protection, but any gains upon termination may not suffice to offset the premium expense we have incurred while holding the purchased protection. Indeed, the market credit swap premium level for the Reference Entity may fall and we may incur termination losses as well as premium expenses as a result. The fair value of our

credit swaps purchased will be affected by market credit swap premium levels.

Expenses

Our expenses are primarily employee compensation and other administrative expenses, including rent for our premises, professional fees and depreciation of our software and fixtures. Employee compensation expense includes salaries and benefits, cash bonuses and stock-based compensation, which is addressed further under "—Critical Accounting Policies". We expect to hire approximately five to seven people in professional positions in the next twelve months, with a corresponding increase in employee compensation.

Distributions on Preferred Securities and Debt Securities

Primus Financial has issued PFP Cumulative Preferred Stock that pay periodic distributions. The cost of these distributions is included in our income statement as distributions on preferred securities of a subsidiary. Further details of the nature and cost of these securities is included in our discussion of liquidity and capital resources. Over time, we expect to issue other debt and preferred securities, which will necessitate periodic interest payments and preferred distributions. Primus Financial completed the issuance of \$75.0 million of subordinated deferrable interest notes on July 23, 2004 and may issue an additional \$75.0 million of subordinated deferrable interest notes prior to the end of 2004.

Income Taxes

Primus Guaranty, Primus Barbados and Primus Financial are not expected to be engaged in the active conduct of a trade or business in the United States and as a result are not expected to be subject to United States federal, state or local income tax. Primus Asset Management is a United States domiciled corporation and is subject to United States federal, state and local income tax on its income, including on fees received from Primus Financial. Primus Re may be subject to United States federal, state or local income tax, or Primus Asset Management may be required to include all or part of Primus Re's income in calculating its liability for United States federal, state or local income tax, depending on the manner in which Primus Re conducts its business and the tax elections it makes. The maximum combined rate of United States corporate federal, state and local income tax that could apply to Primus Financial or Primus Barbados, were they found to be engaged in a United States business in New York City and subject to income tax, is approximately 46% (not including United States branch profits tax that would be imposed on Primus Barbados were Primus Financial deemed to be making distributions to Primus Barbados). See "Tax Considerations—Taxation of Primus Guaranty and its Subsidiaries—United States Taxation—Primus Guaranty, Primus Barbados and Primus Financial." For United States federal income tax purposes, Primus Guaranty and Primus Barbados are likely to be treated as PFICs. For more information, please see "Tax Considerations."

Critical Accounting Policies

Valuation of Credit Swaps

From the inception of our business, we have applied Statement of Financial Accounting Standards, or SFAS, 133, "Accounting for Derivative Instruments and Hedging Activities," which established accounting and reporting standards for derivative instruments. SFAS 133 requires recognition of all credit swaps on the balance sheet at fair value. As a consequence of carrying our credit swaps at fair value, we are not permitted to record a reserve for anticipated losses due to credit events. The market credit swap premium levels used to determine fair value generally take into account the expectation of such events.

The fair value of the credit swaps depends on a number of factors, primarily Reference Entity credit swap premiums and interest rates. The credit swaps are valued using market-standard pricing models which calculate the net present value of differences between future premiums on currently quoted market credit swaps and the contractual future credit swap premiums on contracts we have undertaken. Our pricing model has been internally developed but is benchmarked against a market-standard model. Generally, our model uses quoted market credit swap premium data, that we purchase from an independent pricing service, on individual Reference Entities. This service takes pricing information from a number of prominent dealers and brokers in the credit swap market across a range of standard maturities and restructuring terms, and creates average market credit swap premium quotes on specific Reference Entities.

We believe there are a variety of factors that may influence market credit swap premium levels. The principal factor is the market's view of the probability that a Reference Entity will default over the multi-year horizon typical for a credit swap contract. Those views in turn are influenced by the state of the economy, the outlook for corporate profitability in general as well as the outlook for particular industries and companies. Additional factors include the magnitude of debt outstanding and debt paying capacity within those same industries and companies. One factor specific to the credit swap market is the capacity of credit swap market participants to sell credit swaps. If, for example, commercial banks are actively buying protection to manage their regulatory capital, this will tend to absorb the capacity of protection sellers and cause an increase in market credit swap premiums. Absent rapid and steep changes, interest rates have, at most, a limited effect on market credit swap premium levels.

In 2002, a number of public companies reported accounting and financial irregularities and some large companies sought bankruptcy protection. At the same time, the overall level of corporate defaults rose significantly. As a result, investors began to question the level of creditworthiness within the credit markets and became increasingly concerned about the risk of default by corporate issuers. In response, market credit swap premium levels rose to high levels that have not since been exceeded. In 2003, there were fewer prominent bankruptcies and disclosures of financial irregularities and the global economy began to improve. Consequently, market credit swap premium levels declined gradually but significantly from 2002.

Generally, in the first half of 2004, despite an improving economy, market credit swap premium levels increased, reflecting both a market-wide perception that they had fallen too low in 2003 and the fact that fewer credit swap protection sellers were willing, at those lower rates, to assume additional risk.

A decline in market credit swap premium levels generally causes an increase in the fair value of our credit swap portfolio which results in unrealized gains while an increase in market credit swap premium levels causes a decrease in fair value of the market credit swap portfolio resulting in unrealized losses. Throughout 2003, there was a fairly steady decline in credit swap premium levels, which contributed to our net unrealized gain of \$46.7 million for the year ended December 31, 2003. However, during the first six months of 2004, market credit swap premium levels have generally increased which contributed to net unrealized loss of \$20.1 million for the six months ended June 30, 2004.

Financial Guarantees

We have undertaken a limited amount of financial guarantee business through our subsidiary, Primus Re. Financial guarantees are insurance contracts that contingently require the guarantor to make payments to the guaranteed party. Primus Re designs its guarantee contracts to qualify as non-derivatives in accordance with the scope exception under paragraph 10d of SFAS 133 as amended by SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". We account for our financial guarantee contracts in accordance with SFAS 60, "Accounting and Reporting by Insurance Enterprises". This requires that premiums are deferred and recognized over the life of the

contract and that losses are recorded in the period that they occur based on an estimate of the ultimate cost of losses incurred. Policy acquisition costs include only those expenses that relate

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primarily to, and vary with, premium production. No policy acquisition costs have been deferred by us to date, as any such amounts have been immaterial.

We do not actively offer financial guarantee insurance. Rather, it is an alternative we have available when a counterparty requests an insurance product instead of a credit swap. Generally, a counterparty's choice of a financial guarantee insurance contract versus a credit swap is determined by economic terms available in the marketplace as well as regulatory and accounting considerations. Also, the purchaser of an insurance contract cannot submit a claim for payment unless it has an insurable loss, whereas the purchaser of a credit swap need not have actual exposure to the underlying risk.

Internal Use Software Costs and Formation Expenses

During our development stage (through March 13, 2002), we were developing our proprietary technology. The primary applications developed were (1) capital models to support Primus Financial's AAA/Aaa counterparty ratings and (2) a transactional platform to control our credit swap activities, ranging from trade administration to support for financial accounting and reporting.

The software and related costs of developing the capital model and control platform of approximately \$12.4 million were capitalized in accordance with American Institute of Certified Public Accountants' Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." These costs are being amortized over five years on a straight-line basis. Capitalized costs are reviewed periodically for impairment.

Stock-Based Employee Compensation Plans

Prior to 2003, we followed Accounting Principles Board, or APB, No. 25, "Accounting for Stock Issued to Employees". In 2003, we adopted the fair value approach on a prospective basis for recording stock-based employee compensation in accordance with the fair value method prescribed in SFAS 123, "Accounting for Stock-Based Compensation", as amended by SFAS 148, "Accounting for Stock-Based Compensation—Transition and Disclosure". Under these rules, compensation expense is recognized based on the fair value of stock options, restricted shares and restricted share units over the related vesting period. The fair value of the stock options granted is determined through the use of a market-standard option-pricing model, which requires judgment as to appropriate volatility and interest rate factors. In the absence of a public market for our common shares, management and the board of directors estimate the market value of our common shares for all options, restricted share units and share issuances based on valuation opinions from independent valuation consultants.

Results of Operations for the Six Months Ended June 30, 2004 and 2003

We had a net loss of \$(8.1) million for the six months ended June 30, 2004 as compared to net income of \$47.1 million for the six months ended June 30, 2003. The decrease in net income in the period ended June 30, 2004 was primarily driven by the depreciation in the value of the credit swap portfolio in that period as market credit swap premium levels increased. The results for these periods are discussed below:

Net Credit Swap Revenue

Net credit swap revenue was \$2.8 million and \$57.8 million for the six months ended June 30, 2004 and 2003, respectively. Net credit swap revenue includes:

- Net premiums earned;
- Net realized gains (losses) on credit swaps; and
- Net unrealized gains (losses) on credit swaps.

The table below shows the component parts of net credit swap revenue for the six months ended June 30, 2004 and 2003.

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(\$ in thousands)	Six Months Ended June 30,	
	2004	2003
Net premiums earned	\$ 20,114	\$ 19,238
Net realized gains on credit swaps	2,789	7,067
Net unrealized gains (losses) on credit swaps	(20,068)	31,441
Total Net Credit Swap Revenue	\$ 2,835	\$ 57,746

Net Premiums Earned

Net premiums earned were \$20.1 million and \$19.2 million for the six months ended June 30, 2004 and 2003, respectively. Net premiums earned include:

- Premium income on credit swaps sold;
- Premium expense on credit swaps purchased as short-term investments; and
- Premium expense on credit swaps purchased to offset credit risk on certain credit swaps sold.

The increase in net premiums earned was primarily driven by the increase in the portfolio of credit swaps sold in 2003 and 2004, slightly offset by the premiums paid for credit swaps purchased for short-term investment purposes in 2004. The table below shows the component parts of net premiums earned for the six months ended June 30, 2004 and 2003.

(\$ in thousands)	Six Months Ended June 30,	
	2004	2003
Premium income on credit swaps sold	\$ 20,408	\$ 19,322
Premium expense on credit swaps purchased as short-term investments	(248)	—
Premium expense on credit swaps purchased to offset credit risk on certain credit swaps sold	(46)	(84)
Total Net Premiums Earned	\$ 20,114	\$ 19,238

Premium income on credit swaps sold was higher for the six months ended June 30, 2004 primarily as a result of the expansion in our credit swap portfolio. The notional amounts outstanding of credit swaps we sold were \$8.7 billion and \$6.2 billion at June 30, 2004 and 2003, respectively.

The premium expense accrued on credit swaps purchased as short-term investments was \$248,000 for the six months ended June 30, 2004. This activity commenced after the first six months in 2003, and we therefore incurred no credit swap premium costs in the first six months of 2003. At June 30, 2004, the credit swap notional amount outstanding on credit swaps purchased as short-term investments was \$217.1 million.

The notional amounts of credit swaps that we had purchased to offset credit risk on certain swaps sold were \$5.0 million and \$10.0 million at June 30, 2004 and 2003, respectively. The premium expense incurred as a result of our credit risk offset activity declined in the first six months of 2004 because the amount of credit risk offset transactions in place had declined in 2004.

Net Realized Gains (Losses) on Credit Swaps

Our business strategy is generally to hold swaps we sell until maturity. At the time we sell credit protection, we have no intention of terminating any transaction prior to maturity. However, as described in "—Overview—Revenues" above, there are circumstances in which we may terminate a credit swap prior to maturity, either as a result of credit considerations or to resize or rebalance our portfolio. We cannot identify at the outset of any credit swap transaction whether the credit swap will be terminated or otherwise disposed of prior to its maturity. If the credit swaps we terminate are at attractive market values, we are able to realize gains. Terminating transactions also allows us to accelerate premium receipts and provides for additional growth capacity within our credit swap

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portfolio. Over our two years of operating history, we have terminated less than 1% of the credit swaps under which we had sold credit protection for credit considerations, and less than 10% for resizing considerations. We terminated \$223.4 million and \$405.0 million notional amount of credit swaps sold during the six months ended June 30, 2004 and 2003, respectively.

Where we have purchased credit protection as a short-term investment, early termination of the credit swaps is a fundamental part of the business strategy. We terminated \$189.0 million notional amount of credit swaps purchased in the six months ended June 30, 2004. The purchase of credit protection as a short-term investment was commenced after June 30, 2003 and therefore no terminations took place in the first half of 2003.

Net realized gains on the early termination of credit swaps were \$2.8 million and \$7.1 million for the six months ended June 30, 2004 and 2003, respectively. Net realized gains for the six months ended June 30, 2004 and 2003 are summarized below:

(\$ in thousands)	Six Months Ended June 30,	
	2004	2003
Realized gains on terminated credit swaps sold	\$ 2,109	\$ 7,729
Realized (losses) on terminated credit swaps sold	—	(214)
Realized (losses) on terminated credit swaps purchased to offset credit risk on certain credit swaps sold	(13)	(448)
Realized gains on terminated credit swaps purchased as short-term investments	693	—
Total Realized Gains on Credit Swaps	\$ 2,789	\$ 7,067

Net Unrealized Gains (Losses) on Credit Swaps

Net unrealized losses on credit swaps were \$(20.1) million for the six months ended June 30, 2004 as compared to net unrealized gains of \$31.4 million for the six months ended June 30, 2003. The change in unrealized gains (losses) on credit swaps reflects the change in the fair value of our credit swap portfolio and is primarily due to the increase in market credit swap premium levels experienced during the first six months of 2004. Given the breadth of the portfolio, changes in market credit swap premium levels affect its fair value. We believe credit swap premiums increased during the first six months of 2004 because of a market wide perception that premium levels had fallen too low and the fact that fewer credit swap issuers were willing, at those lower rates, to assume additional risk. See "—Critical Accounting Policies—Valuation of Credit Swaps" and "Risk Factors—Risks Related to our Business—Variations in credit swap premiums could cause our earnings to be inconsistent and our share price to fluctuate significantly". The unrealized gains (losses) on credit swaps sold and credit swaps purchased as short-term investments and for credit risk offset purposes for the six months ended June 30, 2004 and 2003 are summarized below:

(\$ in thousands)	Six Months Ended June 30,	
	2004	2003
Net unrealized gains (losses) on credit swaps sold	\$ (20,255)	\$ 31,375
Net unrealized gains on credit swaps purchased as short-term investments	137	—
Net unrealized gains (losses) on credit swaps purchased to offset credit risk on certain credit swaps sold	50	66
Net total Unrealized Gains (Losses) on Credit Swaps	\$ (20,068)	\$ 31,441

Interest Income Earned

We had interest income of \$1.4 million and \$1.3 million for the six months ended June 30, 2004 and 2003, respectively. The increase in the interest income is attributable to the growth in the balances of cash equivalents and short-term investments in the first six months of 2004, compared with 2003.

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Our cash, cash equivalents and short-term investments were approximately \$276.0 million and \$236.2 million as of June 30, 2004 and 2003, respectively. Average yields on the cash equivalent and short-term investments were 1.0% in the first six months of 2004 and 1.1% in the first six months of 2003, primarily due to a general decline in market interest rates over these periods.

Operating Expenses

Our operating expenses were \$11.2 million and \$11.1 million for the six months ending June 30, 2004 and 2003, respectively. Operating expenses for the six months ended June 30, 2004 and 2003 are summarized below:

(\$ in thousands)	Six Months Ended June 30,
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	2004	2003
Employee compensation	\$ 7,284	\$ 5,032
Brokerage expense	364	282
Excess-of-loss insurance premium	—	727
Administrative expenses	3,615	5,067
Total Operating Expenses	\$ 11,263	\$ 11,108
Number of full-time employees	31	27

The increase in employee compensation over these periods was primarily due to the increase in the number of employees as the business expanded its operations coupled with an increase in the levels of compensation. Brokerage expense relates to fees paid to credit swap brokers that we use on occasion to facilitate credit swap transactions. The increase in brokerage expense was primarily due to the increase in our volume of credit swaps. The excess-of-loss insurance premium expense relates to a surety policy to cover excess credit losses, which Primus Financial acquired in March 2002 and terminated in March 2003. Administrative expenses include professional fees, banking and rating agency charges and amortization and depreciation expenses. Administrative expenses were higher for the six month period ended June 30, 2003 compared to the six month period ended June 30, 2004 primarily as a result of higher professional fees which in turn were the result of the additional cost of auditing our first year of operations. Amortization and depreciation principally relates to the amortization of our internally developed software and the depreciation of our furniture and fixtures. Software amortization decreased by approximately \$399,000 for the first six months of 2004, compared with the first six months of 2003 as a result of the write-off of previously capitalized software that was no longer in active use by the company during 2003.

Income Taxes

Provisions for income taxes were \$117,000 and \$105,000 for the six months ended June 30, 2004 and 2003, respectively. As previously discussed, it is expected that only the income of Primus Asset Management and its subsidiary, Primus Re, are likely to be subject to United States federal, state and local income taxes. However, were Primus Barbados subject to income tax at a combined United States federal, New York State and New York City income tax rate of 46% on its United States GAAP income, then its income tax benefit would be approximately \$3.4 million and its income tax expense (excluding interest and penalties) would be approximately \$22.0 million for the six months ended June 30, 2004 and 2003, respectively. These figures assume that Primus Financial is not deemed to be making distributions to Primus Barbados, which distributions would subject Primus Barbados to the United States federal branch profits tax. If Primus Barbados qualifies for the benefits of the Barbados tax treaty with the United States, and is found to be subject to the branch profits tax on deemed distributions from Primus Financial, the Barbados tax treaty would reduce the rate at which the branch profits tax would apply from the 30% rate applicable in the absence of a tax treaty to a 5% rate. However, the United States and Barbados have recently executed a Second Protocol to amend the treaty, which is subject to ratification before becoming effective. If the Second Protocol becomes effective, Primus Barbados would not qualify for the treaty benefits discussed above, and, if found subject to the branch profits tax as a result of being found to be engaged in a trade or business in the

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United States and deemed to have received distributions from Primus Financial, would be subject to the branch profits tax at the rate of 30% on amounts deemed distributed. For more information, please see "Tax Considerations."

Results of Operations for the Years Ended December 31, 2003, 2002 and 2001

We were capitalized in March 2002 and started selling credit swaps in June 2002. Prior to March 2002, the company incurred development stage expenses, which are discussed further below. Since we were a development stage company prior to March 2002, comparisons of those periods to later periods are not relevant. We had net income (loss) of \$78.5 million, \$(3.1) million and \$(2.8) million for the years ended December 31, 2003, 2002 and 2001 respectively. The increase in net income in 2003 was driven by the growth in our credit swap portfolio, coupled with the appreciation in its value.

Net Credit Swap Revenue

Net credit swap revenue was \$103.3 million and \$14.8 million for the years ended December 31, 2003 and 2002, respectively. Net credit swap revenue includes:

- Net premiums earned;
- Net realized gains (losses) on credit swaps; and
- Net unrealized gains (losses) on credit swaps.

The table below shows the component parts of net credit swap revenue for the years ended December 31, 2003 and 2002.

(\$ in thousands)	Year Ended December 31,	
	2003	2002
Net premiums earned	\$ 38,958	\$ 12,131
Net realized gains on credit swaps	17,629	2,843
Net unrealized gains (losses) on credit swaps	46,739	(213)
Total Net Credit Swap Revenue	\$ 103,326	\$ 14,761

Net Premiums Earned

Net premiums earned were \$39.0 million and \$12.1 million for the years ended December 31, 2003 and 2002, respectively. Net premiums earned include:

- Premium income on credit swaps sold;
- Premium expense on credit swaps purchased as short-term investments; and
- Premium expense on credit swaps purchased to offset credit risk on certain credit swaps sold.

Credit swaps that we sold in 2002 generated \$28.5 million of the net premiums earned for the year ended December 31, 2003, as a full year's premiums were earned on those credit swaps and only a partial year of premiums was earned on the credit swaps we sold throughout 2003. The table below shows the component parts of net premiums earned for the years ended December 31, 2003 and 2002.

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(\$ in thousands)	Year Ended December 31,	
	2003	2002
Premium income on credit swaps sold	\$ 39,112	\$ 12,155
Premium expense on credit swaps purchased as short-term investments	(19)	—

Premium expense on credit swaps purchased to offset credit risk on certain credit swaps sold	(135)	(24)
Total Net Premiums Earned	\$ 38,958	\$ 12,131

The notional amounts outstanding of credit swaps we sold were \$6.4 billion and \$4.7 billion at December 31, 2003 and 2002, respectively. Premium income on credit swaps sold grew in 2003 as a result of the expansion in our credit swap portfolio and because premium income was only earned for a portion of 2002 as our credit swap activity began in June 2002.

The premium expense accrued on credit swaps purchased as short-term investments was \$19,000 for the year ended December 31, 2003. This activity was new in 2003, and we therefore incurred no credit swap premium expense in 2002. At December 31, 2003, the credit swap notional amount outstanding on credit swaps purchased as short-term investments was \$130.0 million.

The notional amounts of credit swaps that we had purchased for credit risk offset purposes were \$5.0 million and \$10.0 million at December 31, 2003 and 2002, respectively. The premium expense incurred as a result of our credit risk offset activity rose in 2003 because we had credit risk offset transactions in place for only a portion of 2002, whereas we had credit risk offset transactions in place throughout 2003.

Net Realized Gains (Losses) on Credit Swaps

Our business strategy is generally to hold swaps we sell until maturity. At the time we sell credit protection, we have no intention of terminating any transaction prior to maturity. However, as described in "—Overview—Revenues" above, there are circumstances in which we may terminate a credit swap prior to maturity, either as a result of credit considerations or to resize or rebalance our portfolio. We cannot identify at the outset of any credit swap transaction whether the credit swap will be terminated or otherwise disposed of prior to its maturity. If the credit swaps we terminate are at attractive market values, we are able to realize gains. Terminating transactions also allows us to accelerate premium receipts and provides for additional growth capacity within our credit swap portfolio. Over our two years of operating history, we have terminated less than 1% of the credit swaps, under which we had sold credit protection for credit considerations, and less than 10% for resizing considerations. Much of our resizing occurred during the second and third quarters of 2003, when market credit swap premium levels had dropped dramatically from their historic 2002 highs. We terminated \$977.0 million and \$130.0 million of credit swaps sold during the years ended December 31, 2003 and 2002, respectively. Net realized gains on the early termination of credit swaps were \$17.6 million and \$2.8 million for the years ended December 31, 2003 and 2002, respectively. Net realized gains increased from 2002 to 2003 as a result of an increased volume of early terminations and because the general increase in the fair value of credit swaps in 2003 enabled us to terminate transactions at higher gains. As of December 31, 2003, we had not incurred a credit event on any credit swap we had sold.

Net realized gains (losses) for the years ended December 31, 2003 and 2002 are summarized below:

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(\$ in thousands)	Year Ended December	
	31, 2003	2002
Realized gains on terminated credit swaps sold	\$ 18,313	\$ 3,145
Realized losses on terminated credit swaps sold	(264)	(302)

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Realized gains on terminated credit swaps purchased as short-term investments	28	—
Realized losses on terminated credit swaps purchased to offset credit risks on certain credit swaps sold	(448)	—
Total Realized Gains on Credit Swaps	\$ 17,629	\$ 2,843

Net Unrealized Gains (Losses) on Credit Swaps

Net unrealized gains on credit swaps were \$46.7 million for the year ended December 31, 2003, compared with a loss of \$213,000 for the year ended December 31, 2002. The increase in unrealized gains on credit swaps reflects the change in the fair value of our credit swap portfolio and is primarily due to the reduction in market credit swap premium levels experienced during 2003. We believe market credit swap premiums decreased in 2003 because there were fewer prominent bankruptcies and disclosures of financial irregularities and the global economy began to improve. See "—Critical Accounting Policies—Valuation of Credit Swaps" and "Risk Factors—Risks Related to our Business—Variations in credit swap premiums could cause our earnings to be inconsistent and our stock price to fluctuate significantly". The unrealized gains on credit swaps sold and credit swaps purchased as short-term investments and for credit risk offset purposes for the years ended December 31, 2003 and 2002 are summarized below:

(\$ in thousands)	Year Ended December 31,	
	2003	2002
Net unrealized gains on credit swaps sold	\$ 46,663	\$ 105
Net unrealized gains on credit swaps purchased as short-term investments	23	—
Net unrealized gains (losses) on credit swaps purchased to offset credit risk on certain credit swaps sold	53	(318)
Net total Unrealized Gains (Losses) on Credit Swaps	\$ 46,739	\$ (213)

Interest Income Earned

We had interest income of \$2.6 million, \$1.6 million and \$2,000 for the years ended December 31, 2003, 2002 and 2001, respectively. The increase in the interest income is attributable to the growth in the balances of cash equivalents and short-term investments during these periods. The average yields on the cash equivalent and short-term investments fell from 2.1% in 2001 to 1.3% in 2002 and to 1.1% in 2003, which reflects a general decrease in market interest rates over these periods.

Our cash, cash equivalents and short-term investments were approximately \$261.9 million, \$221.0 million and \$136,000 as of December 31, 2003, 2002 and 2001, respectively.

Operating Expenses

Our operating expenses were \$25.9 million and \$19.2 million for the years ending December 31, 2003 and December 31, 2002, respectively. Operating expenses for these years are summarized below:

(\$ in thousands)	Year Ended December	
	31,	
	2003	2002
Employee compensation	\$ 11,701	\$ 8,156
Brokerage expense	442	363
Excess-of-loss insurance premium	727	1,854
Administrative expenses	13,027	8,825
Total Operating Expenses	\$ 25,897	\$ 19,198
Number of full-time employees	29	19

The increase in employee compensation over these periods was primarily due to the increase in the number of employees as the business expanded its operations. Brokerage expense relates to fees paid to credit swap brokers that we use on occasion to facilitate credit swap transactions. The excess-of-loss insurance premium expense relates to a surety policy to cover excess credit losses, which Primus Financial acquired in March 2002 and terminated in March 2003. Administration expenses include professional fees, banking and rating agency charges and amortization and depreciation expenses. Amortization and depreciation principally relates to the amortization of our internally developed software and the depreciation of our furniture and fixtures. Software amortization increased by approximately \$3.2 million in 2003 as a result of the write-off of previously capitalized software that was no longer in active use by us. The 2002 amount discussed above includes \$4.3 million of development stage expenses that are discussed below.

From 1998 to March 13, 2002, we were engaged in creating our operating technology platform, raising capital and establishing the basis for our AAA/Aaa counterparty credit ratings. We primarily incurred employee compensation, administrative and software development expenses. During this period, we were funded by external sources. See "—Liquidity and Capital Resources". Development-stage expenses were \$4.3 million in 2002, \$2.8 million in 2001, \$3.1 million in 2000 and \$1.0 million in 1999. These expenses included \$3.5 million in salaries and benefits, \$2.2 million in legal fees, \$2.9 million in professional fees, \$733,000 in technology and data feeds and \$1.8 million of all other expenses. The \$11.7 million total includes expense items incurred in the years 1998, 1999 and 2000 totaling \$207,000, \$1.0 million and \$2.8 million, respectively. The total expense amount from those years equals \$4.0 million.

Income Taxes

Benefits (provisions) for income taxes were \$172,000 and \$(254,000) for the years ending December 31, 2003 and 2002, respectively. Primus Guaranty had a net deferred tax asset fully offset by a valuation allowance of \$5.9 million and \$4.5 million as of December 31, 2003 and 2002, respectively. The change in the deferred tax asset and valuation allowance between 2002 and 2003 results from Primus Asset Management's estimated net operating loss. As previously discussed, it is expected that only the income of Primus Asset Management and its subsidiary, Primus Re, are likely to be subject to United States federal, state and local income taxes. However, were Primus Barbados subject to income tax at a combined United States federal, New York State and New York City income tax rate of 46% on its United States GAAP income, then its income tax expense (excluding interest and penalties) would be approximately \$37.0 million for 2003 and \$80,000 for 2002. These figures assume that Primus Financial is not deemed to be making distributions to Primus Barbados, which distributions would subject Primus Barbados to the United States federal branch profits tax. If Primus Barbados qualifies for the benefits of the Barbados tax treaty with the United States, and is found to be subject to the branch profits tax on deemed distributions from Primus Financial, the Barbados tax treaty would reduce the rate at which the branch profits tax would apply from the 30% rate applicable in the absence of a tax treaty to a 5% rate. However, the United States and Barbados have recently executed a Second Protocol to amend the treaty, which is subject to ratification before becoming effective. If the Second Protocol becomes effective, Primus Barbados would not qualify for the treaty benefits discussed above, and, if found subject to the branch profits tax as a result of being found to be engaged in a trade or business in the United States and deemed to have received

distributions from Primus Financial, would be subject to the branch profits tax at the rate of 30% on amounts deemed distributed. For more information, please see "Tax Considerations."

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Contractual Obligations

Primus Financial has leased its premises at 360 Madison Avenue, New York, New York from Madison 45 LLC at a fixed yearly rental (subject to certain escalations specified in the lease) until August 1, 2012. There are no material restrictions imposed by the lease agreement. The lease is categorized as an operating lease and future payments under the lease are as follows:

Contractual Obligations	Total	Payment due by period			More than 5 years
		Less than 1 year	1-3 years	3-5 years	
Property Lease	\$ 6,481,475	\$ 720,495	\$ 1,494,580	\$ 1,512,444	\$ 2,753,956

We have no other material long-term contractual obligations.

Liquidity and Capital Resources

Prior to commencement of operations (March 14, 2002), we were provided advances by Jay H. Shidler, a shareholder who continues to be a shareholder and director of Primus Guaranty. These advances were primarily to pay operating expenses prior to the commencement of operations. Mr. Shidler was subsequently reimbursed for the advances. See "Certain Relationships and Related Transactions". On the commencement date, we were capitalized with \$155.0 million from the issuance of our Series A preferred shares to two subsidiaries of XL Capital Ltd, or XL, Transamerica Life Insurance Company, a subsidiary of AEGON USA, CalPERS/PCG Corporate Partners Fund, LLC and Radian Group Inc., or Radian. Concurrently with that issuance, Primus Financial obtained a \$115.0 million excess-of-loss insurance policy from Radian Reinsurance, Inc. The policy was provided to cover credit losses in excess of Primus Financial's cash capital. Primus Financial terminated this policy in March 2003.

Primus Financial issued \$110.0 million of PFP Cumulative Preferred Stock on December 19, 2002 in two series, Series I and Series II, to a trust. In conjunction with the receipt of the securities, the trust issued \$100.0 million of Money Market Preferred™ Securities Custodial Receipts, or MMP Receipts, in two series, Series A and Series B, to various institutional investors in a private placement. The trust also issued \$10.0 million of Variable Inverse Preferred™ Securities Custodial Receipts that were retained by Primus Financial. One series pays distributions every 28 days based on an auction rate set on the prior business day and the other series makes payments quarterly, based on an auction rate, which is currently set annually. After December 19, 2012, Primus Financial may redeem the securities, in whole or in part, on any distribution date at \$1,000 per share plus accumulated and unpaid dividends. However, Primus Financial is not required to redeem the securities, nor is it required to establish a sinking fund. For the year ended December 31, 2003, Primus Financial made net distributions to the trust's MMP Receipts in an amount equal to \$1.9 million.

Additionally, as required by our operating guidelines, Primus Financial maintains a \$37.5 million liquidity facility with Harris Trust and Savings Bank, or Harris Trust. The purpose of the liquidity facility is to provide Primus Financial with cash in the event it is obligated to purchase a Reference Entity's debt obligation as the result of a credit event and could not liquidate its investments to do so on a timely basis. The liquidity facility requires that Primus Financial have United States government securities available to pledge as collateral on any advances made under the facility. The facility is renewable on an annual basis at the option of Primus Financial or Harris Trust and has been extended through March 2005. There have been no credit events to date and there have been no borrowings under the facility.

We receive cash from the receipt of credit swap premiums, the net proceeds from the early termination of credit swaps, interest income earned on our investment portfolio and capital raising activities. Cash has been used to pay our operating expenses, administrative expenses, premiums on credit swaps we have purchased and preferred share distributions.

Primus Financial, in order to support its AAA/Aaa ratings, is required to maintain capital in an amount determined by the capital models it has agreed upon with S&P and Moody's. The capital

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required is primarily a function of its credit swap portfolio characteristics, Primus Financial's operating expenses and its tax position. Retained cash flow and proceeds from financings are utilized to increase our capital resources to support our credit swap business.

With our current capital resources and anticipated future credit swap premium receipts and interest income, we believe we have sufficient liquidity to pay our operating expenses and preferred distributions over at least the next twelve months.

Our cash, cash equivalents and short-term investments were approximately \$276.0 million and \$236.2 million as of June 30, 2004 and 2003, respectively. Cash flows provided by (used in) operating activities, investing activities and financing activities were \$14.6 million and \$15.3 million for the periods ended June 30, 2004 and 2003, respectively.

Our cash, cash equivalents and short-term investments were approximately \$261.9 million, \$221.0 million and \$136,000 as of December 31, 2003, 2002 and 2001, respectively. Cash flows provided by (used in) operating activities, investing activities and financing activities were \$36.9 million, \$220.8 million and \$2,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

Primus Financial issued \$75.0 million of subordinated deferrable interest notes on July 23, 2004. This issuance increased the capital resources of Primus Financial, which will help facilitate the expansion of its credit swap activity. The net proceeds will be invested in accordance with our investment guidelines. Given that the interest rate for the notes will be reset periodically, we anticipate that the interest cost of the debt, net of interest income on the invested proceeds, should be less than 0.50% per annum in normal circumstances. Primus Financial may issue an additional \$75.0 million of subordinated deferrable interest notes prior to the end of 2004.

In connection with the issuance of the Series A preferred shares in March 2002, we issued warrants to Radian enabling them to purchase 1,061,059 common shares at an exercise price of \$5.18 per share. On May 15, 2004, Radian exercised these warrants as a result of which we received \$5.5 million.

We expect that the proceeds of this offering will help us to continue to implement our business strategy. We expect our existing capital base and the associated earnings, along with proceeds of this offering and additional debt financing by Primus Financial, including the possible additional subordinated note issuance described above, will be sufficient to operate our business. However, there can be no assurance that we will not need to raise additional capital in the future.

Additional Information

United States GAAP applicable to derivative contracts requires us to account for the credit swaps that we buy or sell at fair value. The fair value of credit swaps is primarily determined by market credit swap premium levels. Premium levels, in turn, are driven by a number of factors, including the number and size of market participants willing to buy or sell credit protection at any given time and the market's perception of credit risk over the life of a particular credit swap. The latter is in turn a function of macroeconomic factors such as the overall state of the economy, corporate profitability and financial leverage and geopolitical concerns. As a general matter, given our strategy of holding credit swaps sold until maturity, we do not seek to manage our overall exposure to market credit swap premium levels by terminating credit swaps prior to their maturity. Accordingly, we expect fluctuations in the fair value of our credit swap portfolio as a result of changes in credit swap premiums over time. These period-to-period changes in value have no ultimate effect on our business, our performance or cash flow. However, reflecting our credit swap portfolio at fair value produces significant changes in our revenue and net income from period to period as the market values of our credit swaps fluctuate.

Despite our strategy of holding credit swaps sold to maturity, we occasionally dispose of credit swaps prior to maturity, but only in circumstances where we believe that the underlying risk related to the credit swap has increased beyond our risk tolerance or where we would seek to rebalance our portfolio and create greater capacity for other credit swaps. Under United States GAAP, the full amount of any realized gains and losses on the termination of credit swaps is included in our revenue immediately.

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In managing our business and assessing its growth and profitability from a strategic and financial planning perspective, we believe it is appropriate to consider both our United States GAAP financial results as well as the impact on those results of fair value accounting and the termination of credit swaps. Therefore, we evaluate what our economic results would have been if we excluded from revenue the amounts of any unrealized gains and losses on our portfolio of credit swaps sold, and any realized gains from terminations of credit swaps sold prior to maturity, although we amortize those gains over the remaining original lives of the terminated contracts, except for credit swaps purchased as investments. In the years ended December 31, 2003 and 2002, we realized \$18.3 million and \$3.1 million of gains, respectively, from the early termination of credit swaps sold. The amortized gains for those years were \$2.9 million and \$53,000, respectively. In the six month periods ended June 30, 2004 and 2003, we realized \$2.1 million and \$7.7 million of gains from the early termination of credit swaps sold. The amortized gains for those periods were \$2.9 million and \$0.7 million respectively. At June 30, 2004, amortization of gains from all credit swaps terminated prior to that date will be recognized in 2004 as \$5.8 million; in 2005 as \$5.5 million; in 2006 as \$5.5 million; in 2007 as \$3.6 million; and in 2008 as \$0.2 million. The amortized gains we recognized for the six months ended June 30, 2004 were \$2.9 million, versus the \$0.7 million recognized for the six months ended June 30, 2003.

Our board of directors also uses these results in assessing our management's performance and determining their compensation.

Market and Counterparty Risk

Market risk represents the potential for losses that may result from changes in the value of a financial instrument as a consequence of market conditions. Our primary market risk is increasing or decreasing market credit swap premium levels, which increase or decrease the fair value of our credit swap portfolio. See "—Critical Accounting Policies—Valuation of Credit Swaps" and "Risk Factors—Risks Related to our Business—Variations in credit swap premiums could cause our earnings to be inconsistent and our stock price to fluctuate significantly." Market credit swap premium levels change as a result of specific events or news related to a Reference Entity, such as a change in a credit rating by S&P and Moody's. Additionally, market credit swap premium levels can vary as a result of changes in market sentiment. As a general matter, given our strategy of holding credit swaps sold until maturity, we do not seek to manage our overall exposure to market credit swap premium levels, and we expect fluctuations in the fair value of our credit swap portfolio as a result of these changes. In cases where we purchase credit swaps as short-term investments, we incur the cost of paying premiums until we terminate the purchased credit protection. We undertake these transactions in the expectation that the market credit swap premium level for the Reference Entity will rise subsequent to our purchase of protection, but any gains realized upon termination may not suffice to offset the premium expense we have incurred while holding the purchased credit protection. Indeed, the market credit swap premium level for the Reference Entity may fall and we may incur termination losses as well as premium expense as a result. The fair value of our credit swaps purchased will be affected by market credit swap premium levels, which will affect our net income. Currently, we purchase a limited amount of credit protection, relative to the size of our portfolio of credit swaps sold, and the cost of purchased credit protection does not materially impact our overall operating margin. The notional amount outstanding on credit swaps we purchased as short-term investments was \$217.1 million at June 30, 2004.

We face other market risks, which are likely to have a lesser impact upon our net income than those associated with market credit swap premium level risk. These other risks include interest rate risk associated with market interest rate movements. These movements may affect the value of our credit swap portfolio as our pricing model includes an interest rate component, which is used to discount future expected cash flows. Interest rate movements may also affect the carrying value of our investments. The PFP Cumulative Preferred Stock pays distributions that are based upon the auction rate preferred market. A difference between the rates we pay in the auction rate preferred market and the interest rates we receive on our investments may result in an additional cost to our company. Assuming that auction results with respect to the PFP Cumulative Preferred Stock reflect prevailing short-term interest rates, each 25 basis point increase or decrease in the level of those rates would

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increase or decrease Primus Financial's annual distribution cost by approximately \$125,000 for each of the Series A and Series B MMP Receipts, but would not affect distributions on the Series B MMP Receipts until after January 20, 2005 when such MMP Receipts may revert to a 28-day auction cycle. Conversely, since almost all of our \$272.5 million cash balance is invested in short-term assets, in the event of such an increase in short-term interest rates, we would earn additional interest income. We also have some exposure to currency rates as we have sold Euro-denominated credit swaps. To date, we have kept the premiums received from these transactions in Euro-denominated cash accounts. The value of the cash Euro balances is translated into United States dollars at current spot rates. Changes in the value of the Euro compared with the United States dollar may have an impact on our net income. We do not hedge any interest rate or currency market risks.

Counterparty risk represents the potential for loss should one or more of our counterparties be unable to meet its obligations due to bankruptcy or a similar event, which could adversely affect our results of operations. Our

counterparties generally have investment grade credit ratings. At June 30, 2004, the notional and fair value amount of credit swaps outstanding with respect to our counterparties that had credit ratings of below investment grade were \$6.0 million and \$27,000, respectively. The premiums on these transactions were fully prepaid by the counterparties.

New Accounting Pronouncements

The Financial Accounting Standards Board, or FASB, issued FASB Interpretation 45, or FIN 45, in November 2002. FIN 45 provides accounting and disclosure requirements for certain guarantees, which encompass credit swaps. The accounting provisions of FIN 45, which are effective for certain guarantees issued or modified beginning January 1, 2003, will not have an effect on the consolidated financial statements as we record credit swaps at fair value. The disclosure provisions of FIN 45 require that we disclose (1) the nature of the credit swap portfolio, (2) the approximate term, (3) how the credit swaps arose, (4) the events requiring us to perform under the credit swap, (5) the maximum potential amount of undiscounted future payments, and (6) the current carrying amount of the credit swap.

In January 2003, the FASB issued Interpretation 46, or FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." The Interpretation defines "variable interests" and specifies the circumstances under which consolidation of special purpose entities will be dependent upon such interests. In December 2003, the FASB issued FASB Interpretation 46 (revised December 2003), or FIN 46R, which effectively modified and clarified certain provisions of FIN 46, as originally issued, and modified the effective date for certain entities.

We adopted the provisions of FIN 46R in 2003. FIN 46 was effective immediately for Variable Interest Entities, or VIEs, created after January 31, 2003. The provisions of FIN 46, as revised, were adopted as of December 31, 2003, for our interests in all VIEs. The result was the derecognition of the MMP Receipts issued by the trust and the recognition of the PFP Cumulative Preferred Stock issued by Primus Financial to the trust. As encouraged by FIN 46R, we have restated our prior year's financial statements to conform to the treatment. The adoption of FIN 46R had no impact on our financial condition or the results of operations.

In April 2003, the FASB issued SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". SFAS 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS 133. This statement amends SFAS 133 for decisions made as part of the Derivatives Implementation Group and clarifies under what circumstances a contract with an initial net investment meets the characteristic of a derivative and when a derivative contains a financing component that warrants special reporting in the statement of cash flows. SFAS 149 is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. SFAS 149 did not have a material impact on our financial statements.

In May 2003, the FASB issued SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." SFAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity.

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SFAS 150 requires that an issuer classify a financial instrument that is within its scope as a liability when that financial instrument embodies an obligation of the issuer. This statement was effective immediately for financial instruments entered into or modified after May 31, 2003, and to all other existing instruments at the beginning of the first interim period beginning after June 15, 2003. SFAS 150 did not have an impact on our financial statements.

INDUSTRY OVERVIEW

Overview of Credit Swaps

A credit swap is a financial instrument used to transfer the credit risk of a Reference Entity from one party to another for a given period of time. In a standard credit swap contract, one party, which we refer to as the protection buyer, purchases credit protection from another party, which we refer to as the protection seller, for an amount equal to the notional amount of a senior obligation (e.g., bond or loan) of a Reference Entity. For this protection, the protection buyer pays a credit swap premium to the protection seller. The premium is generally paid quarterly in arrears, but may be paid in full upfront in the case of a transaction with a short maturity. Generally, if a credit event occurs during the term of the credit swap, the protection seller pays the protection buyer the notional amount and takes delivery of the Reference Entity's obligation. Credit swaps are generally unconditional, irrevocable and noncancellable.

The basic transaction structure for credit swaps is as follows:

Credit events stipulated in credit swaps vary by transaction, but generally include: (1) bankruptcy, (2) failure to pay the underlying debt obligation, (3) repudiation of the debt obligation or moratorium on the payment of interest and principal on the debt obligation (generally for sovereign Reference Entities) and (4) restructuring of a debt obligation resulting in one or more material changes to an obligation. Credit events are subject to various minimum amounts and cure periods.

Upon the occurrence of a credit event, there are two methods to settle the transaction. Physical settlement is the predominant form of settlement. It requires the protection buyer to deliver the notional amount of the Reference Entity obligation to the protection seller in return for the notional amount paid in cash. Under the cash settlement method, payment is made by the protection seller to the protection buyer equal to the notional amount less the market value of the Reference Entity obligation. The market value is determined by referencing dealer quotes or observable market prices over a period of time after the credit event has occurred.

Credit Swap Characteristics

Credit swaps have several distinct structural features that make them particularly suitable for credit risk management applications.

- Credit swaps are documented using standard forms of contracts developed by ISDA. The overall agreement defining the relationship between the parties is the ISDA master agreement, supplemented by a schedule of negotiated terms, and a master confirmation for credit swaps and/or specific confirmations for each transaction. The forms are generally accepted throughout the financial marketplace. This form of documentation standardization has significantly increased the liquidity of credit swaps.

- Credit swaps define, separate, and isolate the credit risk from the other risks (e.g., interest rate risk) of an underlying obligation, allowing for a practical mechanism to manage credit risk efficiently (i.e., buy credit protection). The Reference Entity whose credit risk is being transferred need neither be a party to, nor be aware of, a credit swap transaction because the credit swap is not "attached" to the underlying obligation.
- For some (but not all) of the credit swaps we enter into, there is a secondary trading market. This market involves principally the debt of better-known Reference Entities whose securities are more actively traded. Trading in the secondary market is accomplished by unwinding the credit swap (with the counterparty's consent), assigning the credit swap (in whole or in part) to a third party (with the counterparty's consent) or offsetting the risk of the credit swap position by buying credit swap protection. A protection buyer or seller (including our company) can transfer all or part of the risk of default by a Reference Entity using any of the aforementioned methods. Generally, the accounting treatment for protection buyers and sellers depends of the role of such party in purchasing or selling credit protection. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes appearing elsewhere in this prospectus for more information regarding our accounting treatment for our credit swap business.
- Credit swaps can be custom-tailored to cover only a portion of the period during which a debt obligation is outstanding. Counterparties can thereby hedge specific investments in their portfolios against credit risks in ways that are not otherwise readily available in the capital markets.

Credit swaps and the credit protection that they provide are treated by commercial banks as on-balance sheet equivalents for regulatory capital and economic capital purposes. Credit swaps have been recognized by regulatory authorities in many jurisdictions as a means of reducing a financial institution's risk in computing compliance with regulatory capital requirements. For a bank, this reduces its regulatory capital requirement and can improve its returns on regulatory and economic capital. The Basel II accord (an effort by international banking supervisors to improve the consistency of capital regulations) currently under consideration should serve to further enhance the regulatory capital advantages of credit swaps affected with counterparties such as us. Since credit swaps are market sensitive instruments whose value is dynamic, they are efficient and effective tools for hedging against changes in credit spreads of underlying cash instruments as well as default risk.

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Growth in the Credit Swap Market

The credit swap market has developed from a small, niche segment of the capital markets to a global market that is rapidly growing with diversified product applications and a wide range of participants. Total notional outstanding of the global credit swap market (excluding asset swaps) has grown from approximately \$180.0 billion at December 31, 1997 to \$3.6 trillion as of December 31, 2003, according to the British Bankers Association and ISDA.

Credit Swaps Outstanding, 1997 – 2003

(\$ in billions)

Source: for 1997-2000: British Bankers Association and for 2001-2003: ISDA Market Survey

According to *The Future of Credit Derivatives* (March, 2004) by McKinsey & Company, growth in the number of market participants and market volume is forecast to continue at its current rapid pace, and is being driven primarily by the significant contribution that credit swaps are making to efficient risk management and rational credit pricing. Credit swaps have also been employed in structured products that allow investors to assume different levels of risk with respect to portfolios of underlying Reference Entities.

Industry Participants

Participants in the credit swap market have grown and diversified to include a wide range of financial institutions. Commercial banks are the most active participants in the credit swap market.

Commercial banks, the first major users of credit swap protection, use credit swaps to manage the regulatory and economic capital required to support their credit origination and lending operations. Active credit risk management allows financial institutions and corporations to continuously evaluate their portfolios of credit risk against regulatory and economic guidelines and to rebalance their portfolios based on the various trade-offs among client demands, capital requirements and risk-adjusted returns.

Non-bank participants in the credit swap market have expanded rapidly to include insurance companies, investment funds and industrial corporations.

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Credit Swap Market Participants, December 31, 2002

The following chart illustrates the activity of participants in the credit swap market, measured by credit swaps outstanding.

Source: Risk Magazine 2003 Credit Derivatives Survey

Structured Products

The application of credit swaps has evolved over time, from single Reference Entities to baskets of Reference Entities, or portfolio credit swaps, to credit swap indices.

Portfolio credit swaps redistribute the credit risk of a credit swap portfolio across different tranches. Each tranche represents a different level of risk of loss, with some tranches assuming the first losses and others assuming further losses. Primary examples of portfolio credit swaps include synthetic collateralized debt obligations, or synthetic CDOs, and single tranche transactions.

- Synthetic CDOs involve the structuring and selling of a fully capitalized transaction that matches the notional amount of the underlying credit swaps with income bearing securities. Synthetic CDOs are generally structured by dealers and sold to investors through private offerings.
- Single tranche transactions are issuances in which there is only one piece of the capitalization structure placed with an investor. These transactions are generally structured by dealers and

custom tailored for their investors. Dealers and their investors negotiate the Reference Entities to be included in the underlying credit swap portfolio, and the risk position the investor would like to assume against that portfolio.

Credit swap indices enable participants to either sell or buy credit protection against the credit risk of a credit swap portfolio. In the past few years, several indices have been developed by leading global financial institutions to offer participants a diverse, liquid vehicle for assuming or hedging exposure to different credit markets. These vehicles have increased liquidity in the credit swap market and become industry benchmarks.

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BUSINESS

Overview

Our principal business is selling credit protection under which we assume the risk of default on investment grade credit obligations. The protection we sell takes the form of a credit swap. In exchange for a fixed quarterly premium we agree, upon a default or other credit event affecting a Reference Entity, to pay a counterparty a notional amount against delivery of the Reference Entity's debt obligation.

Primus Financial has the highest counterparty credit ratings offered by S&P (AAA) and Moody's (Aaa) and is managed by an experienced team of professionals who have expertise in credit analysis, trading, risk management and market analysis.

Currently, each of Primus Financial's credit swaps relates to a single specified Reference Entity. In the future, Primus Financial also intends to enter into credit swaps under which it will sell credit protection on a portfolio of obligations of different Reference Entities, most of which will be investment grade. In these transactions, Primus Financial will undertake the risk of loss in the portfolio up to certain levels. For example, out of a portfolio of one hundred named Reference Entities, Primus Financial may assume the risk of loss arising from a default or credit event occurring with respect to more than seven, but not more than ten, of the named Reference Entities. Unrelated other parties would be assuming or retaining the risk of losses in the portfolio below and above the tranche of risk assumed by Primus Financial.

In addition, through our subsidiary Primus Re, we offer financial guaranty insurance products and, through our subsidiary Primus Asset Management, we offer asset management services. Our financial guaranty insurance and asset management business leverages our expertise in credit analysis and quantitative risk assessment. We will evaluate opportunities to make strategic acquisitions to accelerate our entry into related businesses.

From our first sale of a credit swap in June 2002 through June 30, 2004, we have sold credit swaps referencing \$11.2 billion (in notional amount) of debt obligations, of which \$8.7 billion (in notional amount) remained outstanding at June 30, 2004.

Competitive Strengths

We believe we are well-positioned to continue to compete effectively in the credit swap market. The following are our competitive strengths:

Highest Available Counterparty Credit Ratings. Primus Financial has a AAA ("extremely strong") counterparty credit rating from S&P and a Aaa ("exceptional") counterparty credit rating from Moody's, the highest of their respective twenty-one rating levels. These ratings are based on an analysis of the risks of Primus Financial's business of selling credit swaps in relation to its capital. We believe that financial strength of a counterparty is an important consideration for buyers of credit swaps. Primus Financial's ratings provide it with a competitive advantage that affords access to a broader universe of potential counterparties and a greater capacity to incur credit risk than would be the case for other financial institutions with lower counterparty credit ratings. In addition, our financial strength allows us to finance our operations at a relatively lower cost than other financial institutions with lower credit ratings. At June 30, 2004, Primus Financial had total capital resources of \$253.2 million.

Experienced Management Team with Strong Market Relationships. Our management team has an average of 24 years of industry experience with strong and long-standing market relationships with most of the principal participants and counterparties in the credit swap market. This has allowed us to become widely accepted as a professional credit swap investor and counterparty. We believe these relationships will allow us to continue to expand our presence in the credit markets. Prior to joining us, each of those individuals was a managing director or held an equivalent position at leading financial institutions. The team is led by our Chief Executive Officer, Thomas Jasper, who has over 20 years' experience in the financial and capital markets and who was a founder and former Co-Chairman of ISDA.

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Disciplined Underwriting and Risk Management. We underwrite credit risks through proprietary credit analysis that allows us to sell credit protection on Reference Entities that we believe offer attractive risk-adjusted returns. Primus Financial's experienced credit staff manages the underwriting process and actively monitors the on-going risk profile of our portfolio. Our underwriting process has allowed us to create a portfolio of Reference Entities whose quality and diversity are designed to mitigate our exposure to losses. We actively monitor fundamental credit information and market indicators regarding these Reference Entities and take action to limit or remove our exposure to a Reference Entity when we believe its risk of default exceeds acceptable levels. Because of our low number of employees, determining and limiting our exposure to a Reference Entity can be done more quickly than might otherwise be the case at a larger financial institution.

Efficient and Scalable Operations. We believe that our scalable operations enable us to leverage our management's expertise and provide opportunities to realize increased profitability as our business grows and matures. Our relatively low number of employees, our narrow focus and our relatively low ratio of employees to senior employees both allow and require our senior employees to direct the great majority of their efforts toward our credit swap business, rather than the administrative, managerial and cross-selling tasks that occupy a large portion of many senior employees' time at larger, diversified financial institutions.

Business Strategy

The major elements of our strategy are:

Continue to Expand our Credit Swap Business. We intend to leverage our competitive strengths to:

- continue to build a diversified credit risk portfolio;
- sell credit swaps referencing portfolios containing obligations of multiple Reference Entities;
- expand the number and depth of our counterparty relationships;

- actively manage the credit risk in our portfolio; and
- increase and efficiently utilize our capital resources to support our growth.

Maintain Primus Financial's AAA/Aaa Ratings. We believe that having the highest counterparty credit ratings from S&P and Moody's gives Primus Financial the ability to attract large and growing amounts of business with a wide range of counterparties and the ability to select Reference Entities along the full spectrum of investment grade credits.

Pursue Opportunities in Complementary Businesses. We intend to diversify our sources of revenue by expanding into complementary businesses. Primus Asset Management recently entered into an agreement under which it would act as an investment advisor with respect to a credit swap portfolio for a third-party special purpose vehicle. We are pursuing additional investment opportunities in the credit swap market, such as selling credit swaps referencing a broader range of obligations. As we continue to increase the breadth and volume of our services, we plan to selectively add personnel to support our activities. We will evaluate opportunities to make strategic acquisitions to accelerate our entry into related businesses.

Corporate Structure

We are a Bermuda company that was incorporated in 1998. Bermuda has a stable legal and regulatory environment and has been an internationally recognized domicile for insurers and other financial companies for many years. Bermuda has adopted corporate, insurance, tax and exchange control laws, among others, that have attracted many companies with international operations to incorporate in Bermuda. See "—Certain Bermuda Law Considerations" for additional information on Bermuda's legal environment. Bermuda does not tax such companies on their income from sources outside Bermuda. See "Tax Considerations—Taxation of Shareholders—Bermuda Taxation" and "Tax Considerations—Taxation of Primus Guaranty and its Subsidiaries—Bermuda Taxation" for additional information. Primus Financial is organized in Delaware and is our principal operating subsidiary. We own all of the voting securities of Primus Financial through two intermediate holding companies. The

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first, Primus Group Holdings, a Delaware company, was formed to hold our United States assets. We formed and interposed Primus Barbados between Primus Guaranty and Primus Group Holdings because Barbados has a tax treaty with the United States and Bermuda has no relevant tax treaty. If distributions from our United States subsidiaries are found to be subject to a branch profits tax and Primus Barbados qualifies for the benefits of the tax treaty, the distributions may be subject to a 5% branch profits tax instead of the 30% branch profits tax that would apply to distributions to corporations organized under the laws of countries without an applicable United States tax treaty, including Bermuda. However, the United States and Barbados have recently executed a Second Protocol to amend the treaty, which is subject to ratification before becoming effective. If the Second Protocol becomes effective, Primus Barbados would not qualify for the treaty benefits discussed above. See "Tax Considerations—Taxation of Primus Guaranty and its Subsidiaries—Barbados Taxation" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements appearing elsewhere in this prospectus for more information regarding the impact on our results of operations of Primus Guaranty being incorporated in Bermuda. We also have a Bermuda registered insurer, Primus Re, that offers financial guaranty insurance protection to companies that prefer insurance products to credit swaps. We incorporated Primus Re in Bermuda to take advantage of Bermuda as an internationally recognized domicile for insurers. We are currently owned primarily by XL, Transamerica Life Insurance Company, an indirect wholly-owned subsidiary of AEGON, N.V., a Netherlands based holding company, CalPERS/PCG Corporate Partners Fund, LLC, Radian and our management. Executives of our institutional shareholders serve on our board of directors and provide us valuable assistance and expertise in conducting and

expanding our business. The chart below shows the ownership structure of the group.

Primus Financial

Primus Financial is a AAA/Aaa rated provider of credit protection with respect to investment grade Reference Entities. It sells credit protection to selected counterparties through credit swaps. We believe that Primus Financial can generate attractive risk-adjusted returns by selling credit protection

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at credit swap premiums that exceed the predicted credit losses and operating expenses. Primus Financial may also purchase credit swap protection from counterparties on a limited basis when it believes that credit swap premiums are particularly low relative to the risk of a Reference Entity. See "Industry Overview—Overview of Credit Swaps".

As of June 30, 2004, Primus Financial had \$253.2 million of capital resources to support its AAA/Aaa counterparty ratings. This capital consists of \$109.0 million of paid-in capital, which was contributed to Primus Financial by Primus Guaranty, \$98.5 million of net proceeds from the issuance of PFP Cumulative Preferred Stock issued on December 19, 2002 and retained cash flow of \$45.7 million. Primus Financial completed the issuance of \$75.0 million of subordinated deferrable interest notes on July 23, 2004 and may issue an additional \$75.0 million of subordinated deferrable interest notes prior to the end of 2004. The credit swaps in our portfolio had an average maturity of 2.8 years at June 30, 2004. To date, Primus Financial had not suffered a credit loss. However, many of Primus Financial's credit swaps are relatively new and the underlying Reference Entities may not have had time to exhibit problems.

Credit Review and Approval Procedures

Primus Financial subjects each of the Reference Entities rated investment grade by both S&P and Moody's and for which we are considering selling credit protection to a standardized credit review and approval procedure that evaluates, assesses and documents the underlying credit risk of a particular Reference Entity. This procedure is an essential component in determining whether we will sell protection on that Reference Entity and results in the assignment of an independent rating, or a Primus Rating, credit decision and position limit for each such entity. Quantitative inputs that support Primus Financial's credit decisions include the following:

- S&P and Moody's ratings and history;
- industry and company specific analyses and research by major investment and commercial banks;
- financial statement analysis of the Reference Entity;
- credit risk models based on the value of the Reference Entity's assets;
- financial market indicators including bond spreads, stock prices and credit swap premiums; and
- current news on the Reference Entity and its industry.

Primus Financial's credit approval process benefits from the fact that the typical investment grade Reference Entity is a public company which has a current rating and rating history, financial performance history and substantial company and third-party information on financial status and future business prospects. Primus Financial's experienced management professionals are responsible for its credit review and approval procedures. The approach to conducting a credit review results in the designation of a Primus Rating for all approved Reference Entities and is designed to generate consistent credit profiles and flag inconsistencies or issues that require further analysis. This iterative credit review process is also designed to result in judgments that take advantage of all the available information in the

marketplace. After the initial review, all Reference Entities whose risks have been reviewed and a limit approved are periodically monitored.

Credit and Risk Management Policies and Oversight

Policies governing the credit and risk management processes are set by the board of directors of Primus Financial through its Credit and Portfolio Risk Committee, or CPRC. The responsibilities of the CPRC include: (1) at least annually reviewing and approving the credit-related policies and procedures of Primus Financial; (2) reviewing changes to its operating guidelines and our capital models; and (3) reviewing capital levels and portfolio optimization strategies.

Primus Financial's Pricing and Portfolio Management Committee, or PPMC, provides oversight of Primus Financial's portfolio and implements the policies and procedures set by the board of Primus Financial and the CPRC. The PPMC (1) reviews market conditions with a view to providing guidance

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on portfolio priorities, (2) reviews deteriorating credits and proposed hedging or terminating strategies and (3) periodically directs in-depth reviews by industry sector, the results of which are reported to the CPRC.

Transaction Pricing and Execution

Investment activity is limited to Reference Entities approved by, and position limits determined by, Primus Financial's credit professionals. Operating within those constraints, Primus Financial's trading and investment professionals make investment decisions based on their view of risk-adjusted returns available in the market.

Primus Financial's counterparties are primarily major global financial institutions that act in their capacities as dealers and credit portfolio managers. Primus Financial receives bids and offers for the purchase or sale of credit swaps on a daily basis. These bids and offers are communicated directly by its counterparties, or through Primus Financial's access to messages broadcast by brokers to such brokers' subscribers. Primus Financial may also initiate a bid or offer in the same ways. Primus Financial receives pricing transparency and transaction opportunities from its counterparties on a daily basis.

The premiums that Primus Financial receives in connection with its transactions are largely determined by market conditions affecting credit markets, and particularly credit swap markets, both generally and with respect to particular Reference Entities. Primus Financial's decision to effect a particular transaction, and at a particular price within the confines of the current market range, is determined by a number of considerations including a comparative analysis of risk-adjusted returns for different Reference Entities, availability of capacity in particular Reference Entities and with particular counterparties, and the near-term outlook for credit swap prices.

Credit Swap Portfolio

As of June 30, 2004, our credit swaps sold portfolio totaled \$8.7 billion (in notional amount) which had a weighted average credit rating of A/A3 (S&P/Moody's), and represented 453 Reference Entities spread across 40 industries in 22 countries. The percentages of our credit swaps that were denominated in United States dollars and Euros at June 30, 2004 were 76% and 24%, respectively. Reference Entities that were domiciled in the United States and outside the United States comprised 51% and 49%, respectively, of our credit swap portfolio at June 30, 2004.

Additionally, since Primus Financial's inception there has been no credit event on any credit swap we have sold. However, many of Primus Financial's credit swaps are relatively new and the underlying Reference Entities may not have had time to exhibit problems.

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The following charts provide a summary of our portfolio as of June 30, 2004:

Portfolio Distribution by S&P Rating

Portfolio Distribution by S&P Industry

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Risk Management

Primus Financial monitors the Reference Entities in its credit swap portfolio on an ongoing basis. As part of the monitoring process, there is a continual review of the Reference Entities' credit ratings, financial reporting and modeling analyses. Additionally, each Reference Entity in Primus Financial's credit swap portfolio is reviewed at least quarterly, at which point its Primus Rating is reconfirmed. If Primus Financial determines that the risk of a default or other credit event of a Reference Entity exceeds acceptable levels, Primus Financial can reduce or eliminate its credit exposure by buying credit protection against that Reference Entity or by terminating its credit swaps referencing that Reference Entity.

From time to time, Primus Financial enters into transactions designed to reduce its risk positions. These include unwinding credit swaps, assigning credit swaps to third parties (with a novation of its obligations) or purchasing credit swaps that offset the risk of its positions. Risk reducing transactions may be motivated by credit considerations or by expectations regarding future price movements.

Operating Guidelines

Primus Financial's operating guidelines have been negotiated with S&P and Moody's and specify various structural, portfolio and capital constraints with which Primus Financial must comply to maintain its highest counterparty credit ratings including: (1) maximum credit exposure limits to industries, countries and Reference Entities; (2) credit ratings requirements of Reference Entities that are referenced in the credit swaps sold by Primus Financial; and (3) maximum length of exposure to any single Reference Entity.

As stipulated in Primus Financial's operating guidelines, upon the occurrence of certain events Primus Financial must temporarily cease entering into new credit swaps until such event is cured. Events that would cause Primus Financial to cease entering into new credit swaps include a capital shortfall under the operating guidelines, the bankruptcy or other analogous event of Primus Financial, a violation of the operating guidelines that is not cured within ten days upon the occurrence of a capital shortfall and 30 days in all other circumstances or a downgrade of Primus Financial

to A ("strong") or A2 ("good financial security") or below by S&P or Moody's. If an event causing the cessation of new credit swaps is not cured, Primus Financial will not enter into new credit swaps and will runoff its outstanding portfolio of credit swaps.

As required by the operating guidelines, Primus Financial has obtained a \$37.5 million liquidity facility from Harris Trust to provide it with additional liquidity, if necessary, to accommodate the timely purchase of a physically settled deliverable obligation upon the occurrence of a credit event. The liquidity facility has a maturity of one year and may be extended for successive one-year periods upon the request of Primus Financial and with the consent of Harris Trust. The current maturity date of the liquidity facility is March 13, 2005. Primus Financial intends to request an extension of this facility at each annual maturity date so long as it is required to do so by the operating guidelines. Primus Financial's borrowings under the liquidity facility are secured by the investment assets of Primus Financial.

Capital Models and Verification Process

We have developed customized capital models that are cash flow-based simulations of portfolio performance. There is a unique capital model for each of S&P and Moody's. Under its operating guidelines, Primus Financial is required to have an external auditor (currently Ernst & Young LLP) provide to S&P and Moody's an agreed-upon procedures report on a weekly basis. The procedures, which are specified by the rating agencies, consist of testing the application of Primus Financial's operating guidelines with respect to its credit swap portfolio. Agreed-upon procedures reports of this kind are generally required by the rating agencies for companies whose credit ratings depend upon their continued compliance with operating guidelines. Primus Financial intends to continue to hold sufficient capital resources to maintain its AAA/Aaa ratings.

Primus Financial uses our customized capital models to determine the sufficiency of its capital resources to meet the AAA/Aaa requirements of S&P and Moody's. The sufficiency of capital

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resources is in part determined by: (1) the notional amount of each credit swap in the portfolio; (2) the term of each credit swap; (3) the credit risk of each underlying Reference Entity; (4) credit swap premiums; (5) industry concentrations within the portfolio; and (6) Primus Financial's operating expenses and tax status.

Counterparties

Strengthening and expanding relationships with our counterparties is an important element of our business. We have expanded the number of counterparties to whom we sell credit swaps from 20 at December 31, 2002 and 31 at December 31, 2003, to 34 at June 30, 2004, primarily consisting of major global financial institutions. Primus Financial's top counterparty and top five counterparties represented 21% and 59% of Primus Financial's credit swap portfolio outstanding, respectively. The following counterparties each accounted for more than 10% of our consolidated net premium earned for the fiscal year ended December 31, 2003: A, \$5.5 million; B, \$4.8 million; C, \$4.4 million; and D, \$4.2 million. Three of these counterparties are affiliates of underwriters of this offering.

We enter into an ISDA master agreement with each of our counterparties. As of June 30, 2004, we did not have any counterparties with whom we had not yet executed ISDA master agreements. These agreements govern the terms of the credit swap transactions we enter into. The ISDA master agreement does not obligate us to sell or our counterparties to buy credit swaps. The ISDA master agreement does allow us to conduct many separate transactions with a counterparty on an efficient basis, each subject only to a specific confirmation. Our master agreement does not

prohibit our counterparties from purchasing credit swaps from other entities nor does it limit our ability to transact business with other counterparties.

Bankruptcy Remoteness and Governance of Primus Financial

We have structured Primus Financial so that it should not be consolidated with Primus Guaranty or any of its affiliates in the event of its or their bankruptcy. This is an element necessary to maintain Primus Financial's highest counterparty credit ratings from the rating agencies. Components of this bankruptcy remote structure include (1) a board of directors that includes two independent directors who are neither directors nor employees of Primus Financial or its affiliates and (2) a requirement that all agreements with any affiliated company are on an arm's-length basis.

Primus Asset Management

We provide, through Primus Asset Management, credit risk investment advisory and asset management services to Primus Financial and also offer such services to third parties. We advise our clients on the evaluation, selection and pricing of all risks for credit protection, as well as monitor a client's credit exposure and make recommendations as to hedging their credit risks. In addition, we will also advise a client with respect to loss mitigation in the event of any credit events. Primus Asset Management is paid by Primus Financial on a cost plus basis. Advisory engagements from third parties will generate fees based on a percentage of the amount of notional assets under management, plus contingent fees based on performance.

Recently, Primus Asset Management entered into an agreement under which it would act as an investment advisor with respect to a credit swap portfolio for a third-party special purpose vehicle. This arrangement is still in its preliminary stages and there can be no assurance that the special purpose vehicle will be funded and launched.

Primus Re

Primus Re is a Bermuda company registered as a Class 3 insurer under the Bermuda Insurance Act 1978, as amended, and related regulations, or the Bermuda Insurance Act, and operates as a financial guaranty insurance company prepared to act as a non-rated seller of credit swaps and financial guaranty insurance to the market. Financial guaranty insurance is a contract in which an insurance company receives a fee to provide credit protection on a debt instrument and therefore provides a transfer of risk economically similar to a credit swap.

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Primus Re's business is to act as a conduit, or transformer, between parties interested in buying or selling protection in insurance form and other parties interested in assuming the opposite risk position in the form of credit swaps. Primus Re generates revenue by charging a higher insurance premium for protection sold than the swap premium it pays for the offsetting protection it purchases. Primus Re had conducted limited activities through June 30, 2004.

Investments

Our investment portfolio has been invested in short-term government securities, money-market instruments and other investment grade securities. Primus Financial has engaged Harris Investment Management to assist in the management of its fixed income portfolio and to act as its custodian to hold its securities portfolio. The operating guidelines limit Primus Financial's investments primarily to United States government and agency securities, maturing

within three years.

Technology

Our scalable platform was built specifically to effect transactions in credit swaps and manage the resulting risks. It processes and records all of our transactions, and immediately generates confirming documentation as trades are input, thereby reducing the risk of disputes and facilitating our acceptance by counterparties as a professional market participant. Most constraints on our portfolio, including the operating guidelines and limits set by our credit professionals, are maintained in the platform, so that non-conforming transactions cannot be processed and compliance with all constraints can be monitored on a real-time basis. The platform contains extensive databases regarding Reference Entities, credit swap prices and other information required to generate financial and management reports. Our technology has been protected from failure through a variety of security measures, and through the use of fault tolerant hardware at a separate location with fully redundant communication and power back-ups. The platform is designed to permit the parallel processing of third party portfolios managed by Primus Asset Management, alongside Primus Financial's portfolio. The technology allows us to expand our activities at relatively low incremental cost and it helps us to control efficiently and evaluate our business and to ensure compliance with rating agency requirements.

Certain Bermuda Law Considerations

As a holding company, Primus Guaranty is not subject to Bermuda insurance regulations. However, the Bermuda Insurance Act regulates the insurance business of Primus Re, which is registered under that Act. In this section, when we refer to Primus Guaranty, we are referring solely to Primus Guaranty, Ltd. and not to any of its consolidated operations. Certain significant aspects of the Bermuda insurance regulatory framework and other relevant matters of Bermuda law are set forth below:

Certain Bermuda Law Considerations. Primus Guaranty and Primus Re have been designated as non-residents for exchange control purposes by the Bermuda Monetary Authority, or BMA. Common shares may be offered or sold in Bermuda only in compliance with the provisions of the Investment Business Act, which regulates the sale of securities in Bermuda. Primus Guaranty and Primus Re are each required to obtain the prior permission of the BMA for the issuance and transferability of their shares. We have received consent from the BMA for the issue and free transferability of the common shares offered pursuant to this prospectus, as long as the shares of Primus Guaranty are listed on an appointed stock exchange (including the NYSE), to and among persons who are non-residents of Bermuda for exchange control purposes.

Primus Guaranty and Primus Re have each been incorporated in Bermuda as an "exempted company." Under Bermuda law, exempted companies are companies formed for the purpose of conducting business outside Bermuda from a principal place in Bermuda. As a result, they are exempt from Bermuda laws restricting the percentage of share capital that may be held by non-Bermudians, but they may not participate in certain transactions, including: (1) the acquisition or holding of land in Bermuda (except as may be required for their business and held by way of lease or tenancy for terms

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of not more than 50 years or which is used to provide accommodation or recreational facilities for their officers and employees and held with the consent of the Bermuda Minister of Finance, for a term not exceeding 21 years) without the express authorization of the Bermuda legislature; (2) the taking of mortgages on land in Bermuda to secure an

amount in excess of BD\$50,000 without the consent of the Bermuda Minister of Finance; (3) the acquisition of any bonds or debentures secured by any land in Bermuda, other than certain types of Bermuda government securities; or (4) the carrying on of business of any kind in Bermuda, except in furtherance of their business carried on outside Bermuda (and certain other limited circumstances) or under license granted by the Bermuda Minister of Finance.

We must comply with the provisions of the Bermuda Companies Act regulating the payment of dividends, and making distributions from contributed surplus and repurchases of shares. A company shall not declare or pay a dividend, or make a distribution out of contributed surplus, if there are reasonable grounds for believing that: (a) the company is, or would after the payment be, unable to pay its liabilities as they become due; or (b) the realizable value of the company's assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts. Under the Bermuda Companies Act, when a Bermuda company issues shares at a premium (that is for a price above the par value), whether for cash or otherwise, a sum equal to the aggregate amount or value of the premium on those shares must be transferred to an account called "the share premium account." The provisions of the Bermuda Companies Act relating to the reduction of the share capital of a company apply as if the share premium account were paid-up share capital of that company, except for certain matters such as premium arising on a particular class of shares which may be used in paying up unissued shares to be issued to shareholders as fully paid bonus shares. The paid-up share capital may not be reduced if on the date the reduction is to be effected there are reasonable grounds for believing that the company is, or after the reduction would be, unable to pay its liabilities as they become due. Similarly, no purchase by a company of its own shares may be effected if, on the date on which the purchase is to be effected, there are reasonable grounds for believing that the company is, or after the purchase would be, unable to pay its liabilities as they become due.

Exempted companies, such as Primus Guaranty and Primus Re, must comply with Bermuda resident representation provisions under the Bermuda Companies Act. Under Bermuda law, non-Bermudians (other than spouses of Bermudians, or holders of a permanent resident's certificate, or holders of a working resident's certificate) may not engage in any gainful occupation in Bermuda without an appropriate governmental work permit. A work permit may be granted or extended upon showing that, after proper public advertisement, no Bermudian (or spouse of a Bermudian, or holder of a permanent resident's certificate, or holder of a working resident's certificate) is available who meets the minimum standards reasonably required by the employer. The current policy of the Bermuda government is to place a six-year term limit on individuals with work permits, subject to certain exemptions for key employees. There are employee protection laws and social security laws in Bermuda that will apply if we ever have employees based in Bermuda.

The Bermuda Insurance Act. The Bermuda Insurance Act imposes on insurance companies certain solvency and liquidity standards; certain restrictions on the declaration and payment of dividends and distributions; certain restrictions on the reduction of statutory capital; and certain auditing and reporting requirements and also the need to have a principal representative and a principal office (as understood under the Bermuda Insurance Act) in Bermuda. Primus Re's principal representative is currently Marsh Management Services (Bermuda) Ltd. The Bermuda Insurance Act grants to the BMA the power to cancel licenses, supervise, investigate and intervene in the affairs of insurance companies and in certain circumstances share information with foreign regulators. The Bermuda Insurance Act distinguishes between insurers carrying on long-term business and insurers carrying on general business. There are four classifications of insurers carrying on general business, with Class 4 insurers subject to the strictest regulation and Class 3 insurers subject to the next strictest regulation. Primus Re is registered as a Class 3 insurer and is regulated as such under the Bermuda Insurance Act. Class 3 insurers are authorized to carry on general insurance business (as understood under the Bermuda Insurance Act), subject to conditions attached to their license and to compliance

with minimum capital and surplus requirements, solvency margin, liquidity ratios and other requirements imposed by the Bermuda Insurance Act.

As a Class 3 insurer (1) Primus Re is required to maintain the general business solvency margin which is a minimum solvency margin equal to the greatest of: (A) \$1,000,000; (B) 20% of net premiums written up to \$6,000,000 plus 15% of net premiums written over \$6,000,000; or (C) 15% of loss and other insurance reserves; (2) at any time Primus Re fails to meet its general business solvency margin it must, within 30 days after becoming aware of that failure or having reason to believe that such failure has occurred, file with the BMA a written report containing particulars of the circumstances leading to the failure and of the manner and time within which it intends to rectify the failure; (3) Primus Re is prohibited from declaring or paying any dividends at any time it is in breach of its general business solvency margin or the required minimum liquidity ratio, or if the declaration or payment of such dividends would cause it to fail to meet such margin or ratio, and if it has failed to meet its minimum solvency margin or minimum liquidity ratio on the last day of any financial year, Primus Re will be prohibited, without the approval of the BMA, from declaring or paying any dividends during the next financial year; and (4) Primus Re is prohibited, without the prior approval of the BMA, from reducing by 15% or more its total statutory capital (which includes contributed surplus, paid in capital and share premium) as set out in its previous year's financial statements. Primus Re is required annually to file statutorily mandated financial statements and returns, audited by an independent auditor approved by the BMA, together with an annual loss reserve opinion of a BMA approved loss reserve specialist.

Primus Re, Ltd. Act 2000. Primus Re has obtained private Bermuda legislation, entitled the "Primus Re, Ltd. Act 2000", or Private Act, from the Bermuda Legislature that enables it to operate separate accounts (as defined in the Private Act), subject to the provisions of the Private Act. The expected result is that the assets of one separate account are protected from the liabilities of other accounts, with the result that only the assets of a particular separate account may be applied to the liabilities of that separate account. Pursuant to the Private Act, the assets and liabilities of a separate account are treated as a separate fund from Primus Re's own general assets and liabilities or the assets and liabilities arising from any other separate accounts, and, in an insolvency proceeding pursuant to Bermuda law, it is expected that a liquidator will be bound to respect the sanctity of such separate accounts. There are no Bermuda court decisions on the efficacy of separate accounts.

Competition

The business of selling credit protection in the form of credit swaps is highly competitive. Competition is based on many factors, including the general reputation, service and perceived financial strength of the protection seller, the pricing of the credit swap protection (i.e., the premium to be paid by the protection buyer for the credit swap) and other terms and conditions of the credit swap. While there are many participants in the credit swap industry, we believe that Primus Financial is well-positioned as a AAA/Aaa rated (S&P/Moody's) company dedicated to providing credit swap protection to credit swap dealers and credit portfolio managers. Unlike other participants in the credit swap market, our business model is based on the persistent differential between returns available from credit swap premiums and the underlying risk, combined with our efficient operating and capital structure.

Credit Ratings

Ratings by independent agencies are an important factor in establishing the competitive position of counterparties in the credit swap market and are important to our ability to sell credit swaps. Rating organizations continually review the financial positions of counterparties in the credit swap market, including us. S&P maintains a letter scale rating system ranging from "AAA" ("extremely strong") to "CC" ("currently highly-vulnerable"). Moody's maintains a letter scale rating system ranging from "Aaa" ("exceptional") to "C" ("lowest rated"). Primus Financial has been rated "AAA" ("extremely strong") by S&P, which is the highest of twenty-one rating levels, and "Aaa" ("exceptional") by Moody's, which is also the highest of twenty-one rating levels. The objective of

S&P's and Moody's rating systems is to assist counterparties by providing an opinion of a counterparty's financial strength and ability to meet ongoing obligations to its counterparties. These ratings reflect S&P's and Moody's opinions of our ability to pay a counterparty upon a credit event and are not applicable to the common shares offered in this prospectus and are not a recommendation to buy, sell or hold our common shares. These ratings are subject to periodic review by, and may be revised downward or revoked at the sole discretion of, S&P and Moody's.

Credit Swap Documentation

The overall trading relationship between parties to a credit swap is typically governed by an ISDA master agreement that sets the general and ongoing legal and credit terms between the parties and contains express provisions for netting of payment obligations. One of the principal benefits of using ISDA documentation is the ease of completing individual credit swaps with counterparties.

The ISDA master agreement consists of a printed form that includes typical contract terms such as representations and warranties, covenants, events of default and remedies after default and a schedule of elections and modifications to the printed form. The ISDA master agreement is designed to allow Primus Financial and a counterparty to document all of their credit swap transactions under a single agreement.

Individual credit swap transactions are documented under separate confirmations that set forth the particular terms of such transaction. Each confirmation supplements and is subject to the ISDA master agreement.

Potential Conflicts with Certain Shareholders

Certain of our existing shareholders engage in commercial activities and enter into transactions or agreements with us or in competition with us, which may give rise to conflicts. Some of our existing shareholders or their affiliates may in the future sponsor other entities engaged in the credit swap or financial guaranty business, some of which may compete with us. Certain of our existing shareholders and their affiliates have also entered into agreements with and made investments in numerous companies that may compete with us. Our existing shareholders may also pursue acquisition opportunities that may be complementary to our business, and as a result, those acquisition opportunities may not be available to us.

Our board of directors does, however, monitor transactions with our principal shareholders and their affiliates to ensure that such transactions are conducted on an arm's-length basis. Additionally, our directors have customarily recused themselves when transactions with our shareholders with whom they are associated are discussed or approved by the board of directors, a practice which we anticipate will continue. Our directors who are associated with our principal shareholders have been made aware of their fiduciary duties to us and our other shareholders.

Employees

As of June 30, 2004, we had 31 employees, none of whom is located in Bermuda or Barbados. None of our employees is party to a collective bargaining agreement or represented by any labor organization. We consider our relations with our employees to be good.

Properties

Primus Financial occupies approximately 12,000 square feet in New York, New York under a lease that expires in 2012. We believe our space is adequate for our current needs and that suitable additional or substitute space will be available to accommodate foreseeable expansion of our operations. We do not lease or own real property in Bermuda or Barbados.

Legal Proceedings

We are not party to nor currently aware of any pending or threatened litigation.

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MANAGEMENT

Directors, Executive Officers and Other Key Employees

Set forth below is information concerning our directors, executive officers and other key employees.

Name	Age	Position
Executive Officers		
Thomas W. Jasper	56	Chief Executive Officer and Director
Richard Claiden	52	Chief Financial Officer
Zachary Snow	53	General Counsel
Other Key Employees		
Candace Lau-Hansen	40	Global Head of Marketing
Alec C. Rainsby	43	Chief Technology and Operations Officer
Hilmar Schaumann	41	Chief Trading and Investment Officer
Charles Truett	60	Chief Risk Officer
Directors		
Michael P. Esposito, Jr.	64	Chairman of the Board of Directors
Frank P. Philipps	57	Director
Thomas J. Hartlage	52	Director
Robert R. Lusardi	47	Director
Jay H. Shidler	58	Director

Thomas W. Jasper has been our Chief Executive Officer since March 2001 and a director since March 2002. Mr. Jasper joined our company in October 1999 as a consultant to assist us in our formation. Prior to joining our company, Mr. Jasper served for 17 years as a key executive of Salomon Brothers Inc. and its successor, Salomon Smith Barney Holdings, Inc. In 1982, Mr. Jasper created Salomon's interest rate swap business. While at Salomon, in 1984 Mr. Jasper co-founded ISDA, served as its first Co-Chairman, and worked to establish ISDA as the world's preeminent swap association. Mr. Jasper became the Chief Operating Officer of Salomon's non-Japan Asian business in 1994. In 1997, after the acquisition of Salomon Brothers Inc. by The Travelers Group, Inc., Mr. Jasper created the Global Treasury business plan and structure for the merged firm. Mr. Jasper continued as the Global Treasurer of Salomon Smith Barney until late 1998. Mr. Jasper serves on the boards of directors of Phoenix House Foundation, the

Wellspring Foundation and the executive board of the Cox School of Business at Southern Methodist University. Mr. Jasper holds a Bachelor of Arts degree from Southern Methodist University and an M.B.A. from the University of Texas.

Richard Claiden has been our Chief Financial Officer since October 2003. Prior to joining our company, from 2000 to 2003, Mr. Claiden was a Managing Director and from 2001 to 2003 Head of Operational Risk at the investment banking division of JPMorgan Chase. From 1994 to 1999, Mr. Claiden held numerous executive positions at the Canadian Imperial Bank of Commerce. Mr. Claiden holds a Bachelor of Science degree in Economics from London University and holds a Master of Arts in Accounting and Finance from Lancaster University. He is a fellow of the Institute of Chartered Accountants (U.K.).

Zachary Snow has been our General Counsel since May 2002. Prior to joining our company, Mr. Snow served for three years as Executive Vice President and General Counsel of Bridge Information Systems, a leading provider of financial market information. In 2001, he assumed global responsibility for human resources and corporate communications and was named co-Chief Executive Officer in connection with Bridge Information Systems' reorganization proceeding under Chapter 11. He also served as interim President and Chief Executive Officer of the Bridge Information Systems' broker-dealer and related subsidiaries. Prior to that, Mr. Snow served nineteen years (1979-99) in the legal department of Salomon Brothers Inc and its successor, Salomon Smith Barney, Inc., becoming a

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managing director in 1990 and head of the United States legal department in 1993. While employed by Salomon, Mr. Snow served as Chairman of the Fixed Income Committee of the National Association of Securities Dealers Regulation, Inc. and of the Derivative Products Committee of the Securities Industry Association. Mr. Snow has served as Chairman of the Board of Directors of Corlears School and of the Battery Dance Company. Mr. Snow holds a Bachelor of Arts degree from Princeton University and a J.D. from Harvard Law School.

Candace Lau-Hansen has been our Global Head of Marketing since January 2003. Prior to joining our company, Ms. Lau-Hansen spent eleven years at JPMorgan Chase, where she was a Managing Director in the Structured Credit Products and Financial Institutions Groups. From 2000 to 2001, Ms. Lau-Hansen was Global Head of Reinsurance Sales, managing a global team of structured credit sales people covering the reinsurance industry. Prior to that position, from 1996 to 2001, she was the North America/Bermuda Reinsurance Team Leader within JPMorgan Chase's Financial Institutions Group. From 1992 through 1996, Ms. Lau-Hansen managed the Chase Manhattan Bank's relationships with insurance companies in the Northeast United States. Ms. Lau-Hansen holds a Bachelor of Arts degree from Yale University.

Alec C. Rainsby has been our Chief Technology and Operations Officer since March 2002 and has been Chief Technology Officer since March 2000. Prior to joining our company, from June 1993 to March 2000, Mr. Rainsby was a Managing Director in the Debt Markets Technology group of Merrill Lynch. In 1998, Mr. Rainsby created a technology strategy and implementation plan for the Global Debt Markets business and went on to develop a technical architecture group and operating model. During his tenure at Merrill Lynch, Mr. Rainsby managed over 80 professionals, with responsibility for application development, maintenance, hotline support and database administration. Prior to Merrill Lynch, Mr. Rainsby worked at Prudential Securities from 1987 to 1993 where he served in the Financial Strategies Group dealing primarily with mortgage and asset backed securities. Mr. Rainsby holds a Bachelor of Science degree in management science from the London School of Economics.

Hilmar Schaumann has been our Chief Trading and Investment Officer since May 2002. Prior to joining our company, Mr. Schaumann held positions in the global derivatives markets with Deutsche Bank and Swiss Re Financial Products Corporation for 12 years. As a Director at Swiss Re Financial Products in New York, Mr. Schaumann established the firm's credit derivatives trading and structuring group. At Deutsche Bank, where he worked in its London and Frankfurt offices, Mr. Schaumann traded fixed income products on an arbitrage basis and structured derivatives solutions for clients, which included the development of exotic derivatives. Mr. Schaumann has been involved with the ISDA Credit Derivatives Market Practice Committee and was a member of the first "Group of Six" that drafted the Modified Restructuring definition. Mr. Schaumann holds a Master of Science in Mathematics from the University of Hannover. He also attended the Program for Management Development at Harvard Business School.

Charles Truett has been our Chief Risk Officer since August 2001. Prior to joining our company, Mr. Truett spent 31 years with Bank of America and Continental Bank. From 1994 to 1998, Mr. Truett was Bank of America's Senior Credit Officer for its derivatives and securities businesses throughout North and South America and, during this time, also served as Chief Credit Officer and member of the Board of Directors of BA Securities, Inc. From 1998 to 2000, Mr. Truett was the Senior Credit Officer for Latin America at Bank of America during which time he developed and implemented credit systems to automate the credit approval and file processes. From 2000 to May 2001, Mr. Truett was based in Hong Kong as Bank of America's Senior Risk Management executive for Asia. Mr. Truett holds a Bachelor of Science degree in management science from the Case Institute of Technology and holds an M.B.A. from the University of Chicago.

Michael P. Esposito, Jr. has been the Chairman of our Board of Directors since March 2002. He has been non-executive Chairman of the Board of Directors of XL Capital Ltd (NYSE: XL), a provider of insurance and reinsurance coverage and financial products and services, since 1995 and a director since 1986. He is also a director of the general partner of XL Capital Principal Partners I, L.L.C. Since 1995 he has served as a director of Forest City Enterprises, Inc. (NYSE: FCY), a real estate development and management firm and since 1997 as a director of Annuity and Life Re

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(Holdings), Ltd. (NYSE: ANR), an insurance company. Mr. Esposito served as Co-Chairman of the Board of Directors of Inter-Atlantic Capital Partners, Inc., an investment banking firm, from 1998 to 2000, having previously served as Vice Chairman from 1994 to 1998. Mr. Esposito served as Executive Vice President and Chief Corporate Compliance, Control and Administration Officer of The Chase Manhattan Corporation from 1992 to 1995, having previously served as Executive Vice President and Chief Financial Officer from 1987 to 1992.

Frank P. Filippis has been a director of our company since March 2002. In June 1999, he was elected Chairman and Chief Executive Officer of Radian Group Inc. (NYSE: RDN) and its principal subsidiary, Radian Guaranty, Inc. (collectively, Radian Group), which were formed through a merger of Amerin and Commonwealth Mortgage Assurance Company, or CMAC. Radian Group provides private mortgage insurance coverage on residential mortgage loans. From January 1995 to June 1999, he served as Chairman, President and Chief Executive Officer of CMAC. In 1995, he was elected President and a Director of CMAC Investment Corporation (NYSE: CMT), and in January 1996, he was elected Chief Executive Officer of CMAC Investment Corporation. Mr. Filippis originally joined CMAC in 1992 as Senior Vice President and Chief Financial Officer and became Executive Vice President and Chief Operating Officer in 1994. He has been a director of Impac Mortgage Holdings, Inc. (NYSE: IMH), a mortgage real estate investment trust, since November 1995. He has been a director of Radian Group since May 1995.

Thomas J. Hartlage has been a director of our company since March 2002. Since 1990, Mr. Hartlage has been employed in a variety of capacities at subsidiaries of AEGON N.V. (NYSE: AEG), an insurance company, including having responsibilities for strategic planning and product and market development. Since 2001, he has been president of AEGON Structured Products, Inc., a unit of AEGON Institutional Markets focused on building and developing structured transaction business in the capital markets sector. Mr. Hartlage has more than 25 years of experience in the financial services sector. Mr. Hartlage is a chartered financial analyst (CFA).

Robert R. Lusardi has been a director of our company since March 2002. Since July 2000, he has served as Chief Executive for Financial Products and Services of XL Capital Ltd (NYSE: XL), a provider of insurance and reinsurance coverage and financial products and services. From February 1998 until March 2001, he also served as Chief Financial Officer of XL. Mr. Lusardi has been an Executive Vice President of XL since 1998 and serves as a director and/or officer of a number of XL entities, including the general partner of XL Capital Principal Partners I, L.L.C. From 1980 until 1998, Mr. Lusardi was an investment banker at Lehman Brothers where he ultimately served as a Managing Director and headed the insurance and asset management investment banking practice. He is Chairman of the Board of Pareto Partners, a London-based investment management concern. He is also a Director of FSA International Ltd., a financial guaranty company. Mr. Lusardi holds a Bachelor of Arts, Master of Arts degree in Engineering and Economics from Oxford University and an M.B.A. from Harvard University.

Jay H. Shidler is the founder and former Chairman of the Board of our company. Mr. Shidler has been a director of our company since its formation in June 1998. He is the founder and managing partner of The Shidler Group, a private firm investing in the start-up and early stage funding of companies in the finance, insurance, and real estate industries. A nationally acknowledged expert in the field of real estate investment and finance, Mr. Shidler is the founder and Chairman of the Board of Directors of Corporate Office Properties Trust (NYSE: OFC) and founder and Chairman of the Board of First Industrial Realty Trust (NYSE: FR). He serves on the boards of directors of several private companies and charitable organizations, including The Shidler Family Foundation.

The following individuals will become directors of Primus Guaranty upon completion of this offering:

Duncan E. Goldie-Morrison, 49, will become a director of our company upon the closing of this offering. Mr. Goldie-Morrison is President of Ritchie Capital Management, a multi-strategy hedge fund in Geneva, Illinois. Between 1993 and 2003, he was Managing Director, Head of Global Markets Group and Head of Asia at Bank of America. He was responsible for the origination, syndication, sales, trading and research components of the bank's debt businesses. He was also responsible for

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interest rate, credit and commodity derivatives and foreign exchange. Additionally, he managed the company's businesses in Asia and Latin America. He was a member of Bank of America's Management Operating Committee, the Asset and Liability Committee and the Trading Risk Committee. Mr. Goldie-Morrison serves on the board of directors of ICAP, plc (London Stock Exchange: IAPL), the world's largest voice and electronic interdealer broker. Mr. Goldie-Morrison was an ISDA board member for four years and a board member and executive committee member of the Bond Market Association. He was also a member of Duke University's Capital Markets Center Advisory Board.

James K. Hunt, 52, will become a director of our company upon the closing of this offering. Mr. Hunt founded and has been Managing Partner of Bison Capital Asset Management, LLC, a private equity firm, since 2001. From 2001 to 2002, Mr. Hunt also served as an outside consultant to SunAmerica Investments, Inc., a company specializing in

retirement savings solutions. From 1990 to 2000, he was employed by SunAmerica Inc. where he became President of SunAmerica Corporate Finance and Executive Vice President of SunAmerica Investments, Inc., which subsequently became a unit of AIG SunAmerica. During his tenure at SunAmerica, he was also President and Chief Executive Officer of the Anchor Pathway Funds and SunAmerica Series Trust with assets exceeding \$26 billion. Mr. Hunt serves on the board of directors of Falcon Financial Investment Trust (Nasdaq: FLCN), a specialty finance company focused solely on the business of originating and servicing loans to automotive dealers in the United States. Since March 2002, Mr. Hunt has served as a director of Primus Financial. Mr. Hunt holds a Bachelor of Business Administration degree in economics from the University of Texas at El Paso and an M.B.A. in finance and accounting from the University of Pennsylvania's Wharton Graduate School of Business.

John A. Ward, III, 58, will become a director of our company upon the closing of this offering. Mr. Ward was the Chairman of the Board of Directors and Chief Executive Officer of American Express Bank from January 1996 until September 2000, and President of Travelers Cheque Group from April 1997 until September 2000. Mr. Ward joined American Express following a 27-year career at Chase Manhattan Bank, during which he held various senior posts in the United States, Europe and Japan. His last position at Chase was that of Chief Executive Officer of ChaseBankCard Services, which he held from 1993 until 1995. Presently, Mr. Ward serves as a director of Rewards Network Inc. (AMEX: IRN), a loyalty and rewards marketing company, and Coactive Marketing Group, Inc. (NasdaqSC: CMKG), a marketing, sales promotion and interactive media services and e-commerce provider company. Since March 2002, Mr. Ward has served as a director of Primus Financial.

Board Composition

Upon closing of this offering, our board of directors will consist of nine members. Our Bye-laws provide for a staggered board of directors.

Directors are elected for three-year terms as follows:

- Messrs. Michael P. Esposito, Jr., Duncan E. Goldie-Morrison and Thomas W. Jasper have been designated Class I directors whose terms will expire at the 2007 annual meeting of shareholders;
- Messrs. Thomas J. Hartlage, Frank P. Philipps and James K. Hunt have been designated Class II directors whose terms will expire at the 2006 annual meeting of shareholders; and
- Messrs. Robert Lusardi, Jay H. Shidler and John A. Ward, III have been designated Class III directors whose terms will expire at the 2005 annual meeting of shareholders.

In addition, in order to ensure compliance with the independence requirements of the NYSE, the composition of the board of directors may change prior to and following the offering. It is our intention to be in full and timely compliance with all applicable rules of the NYSE and applicable law, including with respect to the independence of our directors. We intend to comply with the requirements of the Sarbanes-Oxley Act of 2002 and the NYSE rules which require that our audit committee be composed of at least three independent directors.

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Committees of the Board of Directors

Our board of directors has the power to appoint committees to perform certain management and administration functions. Our board of directors currently has an audit committee, a compensation committee and a finance and

investment committee. We believe that the members of the audit and compensation committees are, and the nominating and corporate governance committee that we will establish upon the closing of this offering will be, "independent" directors under the standards applicable to members of those committees imposed by the regulations of the Securities and Exchange Commission, or SEC, for audit committees and the NYSE's listing standards for audit, compensation and nominating/corporate governance committees.

Audit Committee

The audit committee, on behalf of our board of directors, recommends to the shareholders the appointment and termination of an independent public accounting firm to be engaged to audit our financial statements, discusses with the independent auditors their independence, reviews and discusses the audited financial statements with the independent auditors and management and recommends to our board of directors whether the audited financials should be included in our future Annual Reports on Form 10-K to be filed with the SEC. The audit committee will consist of three members, all of whom will be independent directors within one year following the completion of this offering. We anticipate that Messrs. Goldie-Morrison, Hartlage and Ward will be members of this committee following completion of the offering. Mr. Hartlage is an executive of Transamerica Life Insurance Company, which beneficially owned approximately 17.2% of our voting shares outstanding as of June 30, 2004.

Compensation Committee

The compensation committee reviews and either approves, on behalf of our board of directors, or recommends to the board of directors for approval (1) the annual salaries and other compensation of our executive officers and (2) individual share and option grants. The compensation committee also provides assistance and recommendations with respect to our compensation policies and practices and assists with the administration of our compensation plans. We anticipate that Messrs. Esposito, Filippis and Hunt will be members of this committee upon completion of the offering. Mr. Esposito is non-executive Chairman of XL, which beneficially owned approximately 45.3% of our voting shares outstanding as of June 30, 2004. Mr. Filippis is Chairman and Chief Executive Officer of Radian, which owned approximately 14.6% of our voting shares outstanding as of June 30, 2004.

Finance and Investment Committee

The finance and investment committee reviews and either approves, on behalf of our board of directors, or recommends to the board of directors for approval, our capital management policies including reviewing and recommending actions with respect to strategic investments, new business initiatives, and reviewing our investment guidelines and performance. We anticipate that Messrs. Goldie-Morrison, Lusardi and Shidler will be members of this committee upon completion of the offering. Mr. Lusardi is an Executive Vice President of XL (and serves as a director and/or officer of a number of XL entities), which beneficially owned approximately 45.3% of our voting shares outstanding as of June 30, 2004.

Nominating and Corporate Governance Committee

Upon the completion of this offering, we will establish a nominating and corporate governance committee. The nominating and corporate governance committee will be responsible for the oversight of, and will assist our board of directors in, developing and recommending corporate governance practices and selecting the director nominees to stand for election at annual meetings of our shareholders. We anticipate that Messrs. Esposito, Filippis and Hunt will be members of this committee following completion of the offering.

Compensation Committee Interlocks and Insider Participation

No interlocking relationship exists between our board of directors or compensation committee and the board of directors or compensation committee of any other entity, nor has any interlocking relationship existed in the past.

Compensation of Directors

For the year ended December 31, 2003, Messrs. Ward and Hunt each received compensation of \$31,000 for serving on the board of directors of Primus Financial and are reimbursed for reasonable expenses incurred in attending meetings of the board of directors of Primus Financial or such board's committees. For the year ended December 31, 2003, the other individuals serving on our board of directors who were not our employees did not receive any compensation so long as they were affiliated with institutions that had a financial interest in us.

After completion of this offering, we intend to pay each of our non-employee directors in the following manner:

- an annual \$30,000 award of common shares;
- an annual retainer of \$30,000, paid half in cash, half in common shares;
- a fee of \$1,000 per board of directors or committee meeting attended;
- an additional annual retainer of \$10,000 for the chairman of the audit committee; and
- an additional annual retainer of \$5,000 for the chairman of each other committee.

The common shares referred to above will be fully vested, although such common shares will not be delivered to the director until the director leaves board service. We intend to reimburse promptly all directors for reasonable expenses incurred to attend meetings of our board of directors or committees.

We have been advised by Mr. Hartlage that, consistent with his employer's corporate practice, Mr. Hartlage will cede any compensation paid to him as a director to Transamerica Life Insurance Company.

Executive Compensation

The following table sets forth all compensation received for services rendered during the year ended December 31, 2003 by our chief executive officer and our two other executive officers whose annual salary and bonus exceeded \$100,000 in such fiscal year. These three officers are referred to as the "named executive officers" in this prospectus. The compensation described in this table does not include medical, group life insurance or other benefits which are available generally to all of our salaried employees.

Summary Compensation Table

Name and Principal Position	Annual Compensation		Long-Term Compensation				
	Salary (\$)	Bonus (\$)	Other Annual Compensation (\$)	Restricted Share Award(s) (\$) ⁽¹⁾	Securities Awards Underlying Options/SARs (#)	Payouts LTIP Payouts (\$)	All Other Compensation (\$)
Thomas W. Jasper Chief Executive Officer	\$ 450,000	\$ 781,395	—	\$ 358,526	61,250	—	—
Richard Claiden	48,526	50,000	—	368,060 ⁽³⁾	18,750	—	—

Chief Financial Officer⁽²⁾

Zachary Snow	316,667	325,500	—	139,466	25,000	—	—
General Counsel							

(1) There was no public trading market for our common shares as of the grant date of these awards. Accordingly, these values have been calculated on our board of directors' determination of the fair market value of the underlying shares as of the grant date of \$9.76 per share. The restricted share awards granted for 2003, in the form of restricted share units, vest in equal installments on the first three anniversary dates of the grant date, February 15, 2004.

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(2) Mr. Claiden commenced employment on October 23, 2003. His salary and bonus, if annualized, would have been greater than \$100,000.

(3) Includes a restricted share award for 2003 and an award of 50,000 restricted share units, valued at \$6.93 per share, granted upon Mr. Claiden's employment date, October 23, 2003, which vests in equal installments on the first three anniversary dates of the grant date.

Option Grants in the Last Fiscal Year

The following table sets forth information regarding options we granted during the fiscal year ended December 31, 2003 to the named executive officers. Potential realizable values are net of exercise price before taxes, and are based on the assumption that our common shares appreciate at the annual rate shown, compounded annually, from the date of grant until the expiration of the ten-year term. These numbers are calculated based on SEC requirements and do not reflect our projection or estimate of future share price growth.

Name	Number of Securities Underlying Options Granted	Individual Grants			Potential Realizable Value at Assumed Annual Rates of Share Price Appreciation for Option Term	
		Percent of Total Options Granted to Employees During the Fiscal Year Ended December 31, 2003	Exercise Price Per Share (\$/Sh)	Expiration Date ⁽¹⁾	5% (\$)	10% (\$)
Thomas W. Jasper	61,250	19.0%	\$ 9.76	2/15/14	\$ 375,878	\$ 952,549
Richard Claiden	18,750	5.8%	9.76	2/15/14	115,067	291,603
Zachary Snow	25,000	7.8%	9.76	2/15/14	153,417	388,789

⁽¹⁾The options were granted on February 15, 2004 and vest in equal installments on the first four anniversaries of such date.

Aggregated Option Exercises in Last Fiscal Year and Fiscal Year End Option Values

The following table sets forth information on unexercised options to purchase our common shares granted to the named executive officers and held by them as of December 31, 2003. No options were exercised during fiscal year 2003.

Name	Shares Acquired on Exercise (#)	Value Realized (\$)	Number of Securities Underlying Unexercised Options at December 31, 2003		Value of Unexercised In-The-Money Options at December 31, 2003 (\$) ⁽¹⁾	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Thomas W. Jasper	—	—	—	111,250	—	\$ 668,825
Richard Claiden	—	—	—	18,750	—	88,875
Zachary Snow	—	—	—	50,000	—	307,750

(1) There was no public trading market for our common shares as of December 31, 2003. Accordingly, as permitted by the rules of the SEC, these values have been calculated based on an assumed initial public offering price of \$14.50 per share, the midpoint of the range set forth on the cover page of this prospectus, less the applicable exercise price per share, multiplied by the underlying common shares.

Share Option and Other Benefit Plans

Stock Incentive Plan

Our Stock Incentive Plan, or the Incentive Plan, provides equity incentives to our employees who are in a position to contribute to our long-term success. The Incentive Plan permits the grant of options in the form of incentive stock options and non-qualified stock options, common shares (restricted and unrestricted) and restricted share units, or RSUs.

The total number of common shares that have been reserved for issuance pursuant to awards under the Incentive Plan is equal to 1,393,652, plus the number of common shares or share units

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awarded to employees outside of the Incentive Plan that are forfeited or reacquired by us at a price that is less than fair market value (up to a maximum of 587,500). The Incentive Plan's share limit is not affected by any RSUs that are granted or subsequently forfeited or cancelled under the Incentive Plan pursuant to bonus awards granted under our Annual Performance Bonus Plan, or the Bonus Plan.

Our chief executive officer, Mr. Jasper, is the plan administrator and, in general (except where the compensation committee of our board of directors has retained discretion), has sole discretion, power and authority to interpret and administer the Incentive Plan. All grants made under the Incentive Plan are approved by our compensation committee.

Unless otherwise determined by the plan administrator, the options granted under the Incentive Plan will carry per share exercise prices that are equal to the fair market value of our common shares on the dates of grant, vest over four years from the date of grant and expire ten years following the dates of grant, subject to earlier expiration upon, or after a specified period following, termination of employment. For the fiscal year ended December 31, 2003, Messrs.

Jasper, Claiden and Snow were awarded options under the Incentive Plan for 61,250, 18,750 and 25,000 common shares, respectively, at an exercise price per share of \$9.76, and for the fiscal year ended December 31, 2002, Messrs. Jasper and Snow were awarded options under the Incentive Plan relating to 50,000 and 25,000 common shares, respectively, at an exercise price of \$6.93.

The plan administrator is also permitted to award restricted and unrestricted common shares which represent the right of a participant to receive delivery of a specified number of our common shares at a future date, or upon the occurrence of a future event. The non-cash portion of annual bonus awards made pursuant to the Bonus Plan are made in the form of RSUs under the Incentive Plan that vest over three years from the date of grant.

All unvested awards become (1) fully vested upon a termination of the grantee's employment by reason of the grantee's death, disability or retirement, (2) fully vested immediately prior to a sale of our company and (3) vested as to 50% of the common shares not then vested upon this initial public offering. 237,910 restricted share units and 234,294 options will vest upon completion of this initial public offering.

The Incentive Plan permits the plan administrator to make an equitable adjustment to the number, kind and exercise price per share of awards in the event of our recapitalization, reorganization, merger, spin-off, share exchange, dividend of common shares, liquidation, dissolution or other similar transaction or events. In addition, the plan administrator may make adjustments in the terms and conditions of any awards in recognition of any unusual or nonrecurring events. The plan administrator may, at any time, alter, amend, suspend or discontinue the Incentive Plan.

2004 Stock Incentive Plan

We have adopted a new 2004 Stock Incentive Plan, or 2004 Plan, to replace the Incentive Plan, although awards already granted under the Incentive Plan will remain outstanding in accordance with their terms. The 2004 Plan generally is to be administered by the compensation committee of our board of directors, except that the full board may act at any time to administer the plan, and authority to administer any aspect of the 2004 Plan may be delegated to our chief executive officer or any other person. The 2004 Plan allows the plan administrator to grant awards of our common shares or the right to receive or purchase our common shares (including options to purchase shares, restricted shares and share units, bonus shares, performance shares, and share appreciation rights) to our employees, directors or other persons or entities providing significant services to us or our subsidiaries, and further provides the plan administrator the authority to reprice outstanding share options or other awards. The actual terms of an award, including the number of common shares relating to the award, any exercise or purchase price, any vesting, forfeiture or transfer restrictions, the time or times of exercisability for, or delivery of, common shares, are to be determined by the plan administrator and set forth in a written award agreement with the participant.

The aggregate number of our common shares for which awards may be granted under the 2004 Plan cannot exceed 12% of the number of our common shares issued and outstanding at the time any

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award is granted. Awards made under the 2004 Plan that have been forfeited (including our repurchase of common shares subject to an award for the price, if any, paid to us for such common shares, or for their par value), cancelled or have expired, will not be treated as having been granted for purposes of the preceding sentence. Unless otherwise provided in an award agreement, all unvested awards become fully vested, and all performance conditions will lapse, upon a termination of the grantee's employment by reason of the grantee's death, disability or retirement, except that certain performance-based awards will only vest based on the number of days completed in the applicable

performance period (as of the date of termination).

The 2004 Plan permits the plan administrator to make an equitable adjustment to the number, kind and exercise price per share of awards in the event of our recapitalization, reorganization, merger, spin-off, share exchange, dividend of common shares, liquidation, dissolution or other similar transaction or events. In addition the plan administrator may make adjustments in the terms and conditions of any awards in recognition of any unusual or nonrecurring events. Our board of directors may, at any time, alter, amend, suspend or discontinue the 2004 Plan. The 2004 Plan will automatically terminate ten years after it has been most recently approved by our shareholders.

Annual Performance Bonus Plan

Our Bonus Plan is maintained in order to tie a portion of each participant's compensation to our financial success and to attract, retain and motivate persons of outstanding ability to exert their best efforts on our behalf. Our chief executive officer, Mr. Jasper, has been designated by our board of directors as plan administrator and in general (except where our compensation committee has retained discretion) has sole discretion, power and authority to interpret and administer the Bonus Plan.

The Bonus Plan provides that each year our chief executive officer will identify the Bonus Plan participants and specify the target bonuses for each participant. Participants who are designated by our chief executive officer as "key executives" will generally have target bonuses that average 1.25 times salary. For all other participants, target bonuses will generally average 0.75 times salary. Key executives will be guaranteed a minimum bonus, typically 0.5 times salary and their bonuses will be capped, typically at two times salary. Target bonuses are reviewed each year in light of both our performance and updated information on market comparables.

As soon as practicable at the end of each fiscal year, the bonus pool with respect to such year will be determined at the discretion of our chief executive officer, subject to the approval of our compensation committee. In general, if our financial performance is deemed satisfactory, the bonus pool will equal the budgeted bonus accrual. The bonus pool may be larger or smaller, depending upon our actual results. The allocation of our bonus pool among eligible participants will be determined by our chief executive officer, with approval of our compensation committee. Such awards will be based upon individual performance (subject to the predetermined guarantees and caps). A specified portion of a participant's bonus, up to 30%, is payable in the form of RSUs under the Incentive Plan. Payment of the cash portion of each participant's bonus will generally be distributed as soon as practicable following allocation of the bonus pool each year. Generally, participants must be employed with us on the date of distribution of the bonus pool in order to be eligible to receive an award. For the fiscal year ended December 31, 2003, Messrs. Jasper, Claiden and Snow were awarded cash bonuses of \$781,395, \$50,000 and \$325,500, respectively, and non-cash bonuses in the form of RSUs under the Incentive Plan relating to 36,742, 2,192 and 14,293 common shares, respectively, and for the fiscal year ended December 31, 2002, Messrs. Jasper and Snow were awarded cash bonuses of \$750,000 and \$337,500, respectively, and non-cash bonuses in the form of RSUs under the Incentive Plan relating to 36,043 and 16,219 common shares, respectively.

Severance Plan

We have adopted a severance plan for our senior executive officers (other than our chief executive officer) and certain other designated key employees, which will provide for severance benefits based upon length of service for terminations of employment occurring outside the context of a change in control of our company, and an enhanced level of severance for terminations of

employment occurring in connection with a change in control of our company that may occur following consummation of this offering. Generally, severance payable outside the context of a change in control will equal one month of base pay, bonus (based on the average of the cash bonuses paid in the previous 3 years), and reimbursement of Consolidated Omnibus Budget Reconciliation Act, or COBRA, premiums for each full year of completed service, with a minimum severance of two months and a maximum severance of 12 months, as well as a pro rata annual bonus. Severance payable for terminations occurring during an 18 month period following a change in control will include base pay, bonus (based on the highest cash bonus paid in the previous 3 years), and reimbursement of COBRA premiums for a specified severance period (generally 18 months for members of our management committee and 12 months for others), as well as accelerated vesting of outstanding share-based awards (on a prorated basis for performance-based share awards) and a pro rata annual bonus. If any payments under the plan or otherwise are subject to the "golden parachute" excise tax, we will pay participants an amount sufficient to negate the impact of this tax, unless the tax can be eliminated by a 10% or less reduction of the amounts payable. Any severance payable pursuant to this plan will be offset by severance payable under any applicable employment agreement. Employees are required to sign a non-compete agreement as a condition to participation in this plan. Our board may amend or terminate this plan, or remove or add designated participants, on 12 months' notice to any participants affected by the change provided that no changes adverse to participants could be made during the 18 month period following a change in control. For purposes of the plan, a change in control is defined as (i) an acquisition by any person or group of a beneficial interest of at least 30% (50% if such person owned our shares immediately prior to this offering) of the voting power, (ii) a change in the composition of a majority of the board not approved by incumbents, or (iii) any reorganization, merger or sale of assets or similar transaction where shareholders immediately prior to such transaction cease to own at least 50% of voting stock of the resulting corporation.

401(k) Plan

We offer our employees the opportunity to make contributions to a 401(k) plan, and provide a company match of 50% of the first \$6,000 contributed by each employee each year to the plan.

Employment Agreements

Thomas W. Jasper. Mr. Jasper's current employment agreement expires in March 2005. We have entered into a new employment agreement with him which will become effective upon completion of this offering and which will replace his current agreement. The new employment agreement will provide for the following: a base salary of \$500,000; an annual bonus opportunity targeted at 150% of base salary, with the actual bonus based primarily upon achievement of performance goals established annually by the compensation committee; and termination benefits consisting of a payment equal to five times Mr. Jasper's annual base salary then in effect, a prorated annual bonus, continued health benefits for two years and full or partial accelerated or continuing vesting of his unvested incentive equity awards, payable upon a termination of employment by us other than for "cause" or by Mr. Jasper for "good reason". It will also provide for a payment sufficient to negate the impact of any "golden parachute" excise tax, unless that tax can be eliminated by a 10% or less reduction of the payments to which Mr. Jasper is otherwise entitled. For example, if Mr. Jasper's employment were terminated without cause at a time when his rate of base salary was \$500,000, he would be entitled to a cash severance payment of \$2.5 million, plus a prorated bonus that would depend upon the point in time during the year that the termination occurred and our actual performance during such year. He would also be entitled to the benefits and equity vesting described above. We can terminate Mr. Jasper's employment without any termination obligation on any anniversary of this offering, starting with the third anniversary, by providing him at least six months notice. However, where such notice is provided after a "change in control" (which is defined in the same way as in our Severance Plan described above) and the termination is to be effective on any anniversary of this offering occurring within 18 months after such change in control, the contractual termination benefits described above will be payable. The new employment agreement also contains a prohibition on Mr. Jasper's competing with us for the one year period following termination of his employment if he is entitled to

his contractual termination benefits, or otherwise if we elect to pay him 2.5 times his annual base salary and continue to vest certain of his equity awards for one year. If we terminate Mr. Jasper's employment other than for cause on the third or any subsequent anniversary of this offering, his equity awards will continue to vest on their original vesting schedule as long as Mr. Jasper does not engage in any competitive activities during the vesting period.

In addition, Mr. Jasper has been granted incentive equity awards in connection with, and conditioned upon completion of, this offering for a total of 157,500 common shares, one-half of which is in the form of an option to purchase common shares that will vest over four years of service, and one-half of which is in the form of performance common shares. All of the performance common shares will be paid if a targeted level of performance is achieved for the period commencing January 1, 2004 and ending December 31, 2006, between 50% and 100% of the performance common shares will be paid if actual performance for a period is at least equal to a threshold level of performance but less than target, and up to 150% of the performance common shares will be paid if actual performance exceeds target. No performance common shares will be paid if actual performance is not at least equal to the threshold level of performance. During our developmental stage, Mr. Jasper received fully vested grants of 437,500 common shares; he also has received share option awards and RSU awards pursuant to our Incentive Plan and Bonus Plan which are described above. Upon a change in control, if these or other equity awards are not continued, assumed or substituted in the transaction, they will vest in full immediately prior to the change in control.

Richard Claiden. We are party to an employment agreement with Mr. Claiden, pursuant to which he is entitled to receive an annual base salary of \$250,000 and a discretionary annual merit bonus payable in cash and RSUs. In respect of 2003, Mr. Claiden received a bonus in cash and RSUs under our Bonus Plan and an award of options under our Incentive Plan, all of which are described above. For 2004, the target amount of his bonus is \$250,000. Upon joining us, he received an award of 50,000 RSUs that vest in three equal installments in 2004, 2005 and 2006. One-half of any RSUs that are unvested at the time of this offering will become vested at such time. In addition, all unvested RSUs will vest upon a sale of our company. In the event of Mr. Claiden's termination of employment, any RSUs that have not yet vested will be forfeited, unless his termination is by reason of his death or disability, in which case all unvested RSUs will vest.

Zachary Snow. We are party to an employment agreement with Mr. Snow, pursuant to which he is paid annually a base salary that is currently \$350,000. Mr. Snow received awards under our Incentive Plan and Bonus Plan that are described above. In connection with the commencement of his employment, Mr. Snow received 75,000 restricted common shares on June 7, 2002. One-third of these shares vest on each of the first three anniversaries of his hire date. One-half of any shares not yet vested will vest upon completion of this offering. His employment agreement expires on May 6, 2005. In the event that Mr. Snow's employment is terminated prior to expiration of his employment agreement (a) by us other than for "cause" (as defined in his agreement with us), or (b) by Mr. Snow for "good reason" (as defined in his agreement with us), Mr. Snow will be entitled to receive severance payments and benefits consisting of: (i) continued base salary at a rate of 200% of his base salary and continued health coverage, in each case for a period equal to the lesser of (x) 12 months, or (y) the remaining term of his agreement (i.e., from the date of termination until May 6, 2005); and (ii) a prorated portion of his annual bonus and share award, paid when bonuses are normally paid. If Mr. Snow terminates his employment for good reason, he will also be entitled to immediate vesting of all outstanding share and option awards. In the event his employment is terminated as a result of his disability or upon the expiration of the term of the agreement, Mr. Snow is only entitled to receive a prorated portion of his annual bonus. If his employment is terminated by us for cause or by him not for good reason, Mr. Snow cannot compete with us for 12 months. Upon any other termination of his employment, Mr. Snow's non-competition period will correspond to the period during which he is receiving any severance payments or benefits described in clause (i)

above. We may extend the non-competition period for up to 12 months if we provide notice and continue the payment of severance during this period.

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IPO Awards

The board of directors has approved the grant of equity incentive awards in connection with, and conditioned on completion of, this offering. Specifically, the board of directors authorized the grant of options and performance common shares in the aggregate amount up to 2.4% of common shares outstanding upon consummation of this offering. The cost of the awards in connection with this offering will be recognized over the vesting period for the awards in accordance with FAS 123. The cost of options will be recognized ratably between the closing date of the offering and December 31, 2007. The cost of the performance common shares will be recognized ratably between the closing date of the offering and December 31, 2006. The expense associated with the performance shares will be adjusted over the vesting period to reflect the projected actual award, which is based upon our aggregate performance in the years 2004, 2005 and 2006. The board of directors delegated to the compensation committee decisions regarding the terms and conditions of such awards, including the employees to whom such awards are to be granted and the performance factors required to earn such common shares. The compensation committee has determined that 50% of the equity incentive awards will be option grants which will vest annually over four years and 50% will be performance common shares. All of the performance common shares will be paid if a targeted level of performance is achieved for the period commencing January 1, 2004 and ending December 31, 2006, between 50% and 100% of the performance common shares will be paid if actual performance for a period is at least equal to a threshold level of performance but less than target, and up to 150% of the performance common shares will be paid if actual performance exceeds target. The targeted levels of performance are (1) an average return on equity of 15% and (2) a 65% compound annual growth rate in economic results. The awards will be made at the initial public offering price per share. Thomas Jasper, Richard Claiden and Zachary Snow have been granted 157,500, 37,500 and 37,500 equity incentive awards, respectively.

We have also granted each of our non-employee directors 1,562 common shares, conditioned upon completion of this offering. Mr. Esposito and Mr. Lusardi have waived their respective rights to these common shares. Mr. Hartlage has advised us that, consistent with his employer's corporate practice, he will cede beneficial ownership of these common shares to Transamerica Life Insurance Company.

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PRINCIPAL AND SELLING SHAREHOLDERS

The following table and accompanying footnotes show information regarding the beneficial ownership of our common shares before and after this offering by:

- each person who is known by us to own beneficially more than 5% of our common shares;
- each member of our board of directors and each of our executive officers;

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- all members of our board of directors and our executive officers as a group; and
- each selling shareholder.

The percentage ownership before the offering is based on 33,634,978 common shares outstanding as of September 23, 2004, and reflects a one for eight reverse share split that we intend to effect immediately prior to the completion of this offering (with fractional shares satisfied in cash). The percentage ownership before the offering assumes conversion of all outstanding shares of Series A preferred shares, but assumes that no exercise of outstanding warrants and options has occurred. Percentage ownership after the offering is based on common shares outstanding immediately after the closing of this offering.

For purposes of the table below, we deem common shares subject to options or warrants that are currently exercisable or exercisable within 60 days of September 23, 2004 to be outstanding and to be beneficially owned by the person holding the options or warrants for the purpose of computing the percentage ownership of that person but we do not treat them as outstanding for the purpose of computing the percentage ownership of any other person. Except as otherwise noted, the persons or entities in this table have sole voting and investing power with respect to all of the common shares beneficially owned by them, subject to community property laws, where applicable. Except as otherwise set forth below, the street address of the beneficial owner is c/o Primus Asset Management, Inc., 360 Madison Avenue, 23rd Floor, New York, New York 10017.

Name of Beneficial Owner	Shares Beneficially Owned Prior to Offering		Maximum Number of Shares Offered in this Offering	Percentage Ownership After this Offering	Maximum Number of Shares Being Sold in the Over-Allotment Option, if Any	Shares Beneficially Owned After the Offering if the Underwriters' Over-Allotment Option is Exercised in Full	
	Number of Shares	Percent				Number of Shares	After Offering
Beneficial Owners owning greater than 5% of the shares:							
BlackRock Capital Ltd	15,893,509	45.3%(1)	573,335	34.7%	740,557	14,579,617	33.0%
Transamerica Life Insurance Company (an indirectly wholly-owned subsidiary of PRUDENTIAL FINANCIAL GROUP, N.V., a Netherlands domiciled holding company)	5,791,505	17.2%(2)	208,920	13.1%	269,855	5,314,292	12.4%
BlackRock PERS/PCG Corporate Partners Fund, LLC	5,791,505	17.2%(3)	208,920	13.0%	269,855	5,312,730	12.4%
BlackRock Canadian Group Inc.	4,922,062	14.6%(4)	177,556	11.1%	229,343	4,515,163	10.6%
Executive Officers:							
Thomas W. Jasper	519,929	1.5%(5)	0	1.4%	0	599,635	1.4%
Richard Snow	86,656	*%(6)	0	*%	0	121,083	*%
Richard Claiden	0	*%	0	*%	0	35,471(7)	*%
Non-Executive Directors:							
Michael P. Esposito, Jr.	0	*%	0	*%	0	0(8)	*%
Frank P. Filippis	0	*%	0	*%	0	1,562(9)	*%
William E. Goldie-Morrison	0	*%	0	*%	0	1,562(10)	*%
Thomas J. Hartlage	0	*%	0	*%	0	0(11)	*%
James K. Hunt	0	*%	0	*%	0	1,562(12)	*%

Robert R. Lusardi

0 *%