# XL Bermuda Ltd

Consolidated Financial Statements
for the Years Ended December 31,
2017 and 2016

XL CATLIN

April 27 2018

**Report of Independent Auditors**

**To the Shareholder of XL Bermuda Ltd**

We have audited the accompanying consolidated financial statements of XL Bermuda Ltd and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2017 and December 31, 2016, and the related consolidated statements of income, comprehensive income, shareholder's equity and cash flows for the years then ended.

**Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' responsibility**

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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**Opinion**
In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of XL Bermuda Ltd and its subsidiaries as of December 31, 2017 and December 31, 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

**Other Matter**
Accounting principles generally accepted in the United States of America require that the required supplemental information under Accounting Standards Update 2015-09, *Disclosure about Short-Duration Contracts* labelled as Unaudited within Note 10 on pages 55 to 63 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers Ltd.

**Chartered Professional Accountants**

# XL BERMUDA LTD
# CONSOLIDATED BALANCE SHEETS
# AS AT DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands, except share data)* | 2017 | 2016 |
|---|---|---|
| **ASSETS** | | |
| Investments: | | |
| Fixed maturities, at fair value (amortized cost: 2017, $29,645,663; 2016, $28,956,977) | $ 30,416,290 | $ 29,619,018 |
| Equity securities, at fair value (cost: 2017, $638,455; 2016, $995,934) | 713,967 | 1,036,655 |
| Short-term investments, at fair value (amortized cost: 2017, $801,210; 2016, $626,142) | 800,027 | 625,194 |
| Total investments available for sale | $ 31,930,284 | $ 31,280,867 |
| Fixed maturities, at fair value (amortized cost: 2017, $1,946,501; 2016, $1,548,178) | 2,006,385 | 1,617,014 |
| Short-term investments, at fair value (amortized cost: 2017, $14,969; 2016, $9,536) | 14,965 | 9,563 |
| Total investments trading | $ 2,021,350 | $ 1,626,577 |
| Investments in affiliates | 1,911,996 | 2,177,645 |
| Other investments | 1,163,863 | 1,164,547 |
| Total investments | $ 37,027,493 | $ 36,249,636 |
| Cash and cash equivalents | 3,273,315 | 3,341,679 |
| Restricted cash | 157,497 | 153,504 |
| Accrued investment income | 269,701 | 281,330 |
| Deferred acquisition costs and value of business acquired | 1,102,474 | 946,721 |
| Ceded unearned premiums | 2,198,217 | 1,687,864 |
| Premiums receivable | 6,934,482 | 5,522,976 |
| Reinsurance balances receivable | 930,114 | 577,479 |
| Unpaid losses and loss expenses recoverable | 7,247,723 | 5,491,297 |
| Receivable from investments sold | 201,515 | 128,411 |
| Amount due from Parent and affiliates | 68,004 | 82,958 |
| Goodwill and other intangible assets | 2,089,438 | 2,067,341 |
| Deferred tax asset | 332,024 | 310,542 |
| Other assets | 738,744 | 692,835 |
| **Total assets** | $ 62,570,741 | $ 57,534,573 |
| **LIABILITIES AND SHAREHOLDER'S EQUITY** | | |
| Liabilities: | | |
| Unpaid losses and loss expenses | $ 29,696,779 | $ 25,939,571 |
| Deposit liabilities | 1,042,677 | 1,116,233 |
| Future policy benefit reserves | 3,610,926 | 3,506,047 |
| Funds withheld on GreyCastle life retrocession arrangements (net of future policy benefit reserves recoverable: 2017, $3,191,584; 2016, $3,072,615) | 999,219 | 998,968 |
| Unearned premiums | 8,307,431 | 7,293,028 |
| Reinsurance balances payable | 3,706,116 | 2,451,717 |
| Payable for investments purchased | 332,142 | 226,009 |
| Deferred tax liability | 57,574 | 77,271 |
| Amount due to Parents and affiliates | 27,087 | 47,710 |
| Other liabilities | 952,773 | 1,158,877 |
| **Total liabilities** | $ 48,732,724 | $ 42,815,431 |
| Shareholders' Equity: | | |
| Ordinary shares, 15,000,000 authorized, par value $0.10; issued and outstanding (2017: 12,500,000 ; 2016: 12,500,000) | $ 1,250 | $ 1,250 |
| Additional paid in capital | 12,579,844 | 12,579,844 |
| Accumulated other comprehensive income | 741,922 | 541,900 |
| Retained earnings | (141,078) | 918,483 |
| Shareholders' equity attributable to XL Group Ltd | $ 13,181,938 | $ 14,041,477 |
| Non-controlling interest in equity of consolidated subsidiaries | 656,079 | 677,665 |
| **Total shareholders' equity** | $ 13,838,017 | $ 14,719,142 |
| **Total liabilities and shareholders' equity** | $ 62,570,741 | $ 57,534,573 |

See accompanying Notes to Consolidated Financial Statements

# XL BERMUDA LTD
# CONSOLIDATED STATEMENTS OF INCOME
# FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands)* | | 2017 | | 2016 |
|---|---|---|---|---|
| **Revenues:** | | | | |
| Net premiums earned | $ | 10,336,612 | $ | 9,777,934 |
| Net investment income: | | | | |
| Net investment income - excluding Life Funds Withheld Assets | | 688,284 | | 656,179 |
| Net investment income - Life Funds Withheld Assets | | 127,047 | | 154,751 |
| Total net investment income | | 815,331 | | 810,930 |
| Realized investment gains (losses): | | | | |
| Net realized gains (losses) on investments sold - excluding Life Funds Withheld Assets | | 132,788 | | 193,773 |
| Other-than-temporary impairments ("OTTI") on investments - excluding Life Funds Withheld Assets | | (12,988) | | (78,997) |
| OTTI on investments transferred to (from) other comprehensive income - excluding Life Funds Withheld Assets | | (359) | | 439 |
| Net realized gains (losses) on investments sold - Life Funds Withheld Assets | | 115,911 | | 152,589 |
| OTTI on investments - Life Funds Withheld Assets | | (1,434) | | (2,598) |
| Net unrealized gains (losses) on investments, trading securities ("Trading") - Life Funds Withheld Assets | | (14,805) | | 109,458 |
| Total net realized gains (losses) on investments, and net unrealized gains (losses) on investments, Trading | $ | 219,113 | $ | 374,664 |
| Net realized and unrealized gains (losses) on derivative instruments | | (41,732) | | 2,521 |
| Net realized and unrealized gains (losses) on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets | | (206,015) | | (540,090) |
| Income (loss) from investment affiliates | | 139,046 | | 70,758 |
| Fee income and other | | 48,647 | | 35,692 |
| **Total revenues** | $ | 11,311,002 | $ | 10,532,409 |
| **Expenses:** | | | | |
| Net losses and loss expenses incurred | $ | 8,001,920 | $ | 6,072,835 |
| Claims and policy benefits | | 39,189 | | 28,244 |
| Acquisition costs | | 1,788,140 | | 1,620,671 |
| Operating expenses | | 1,689,570 | | 1,961,366 |
| Foreign exchange (gains) losses | | 35,458 | | (8,146) |
| (Gain) Loss on sale of subsidiary | | — | | (7,088) |
| Interest expense | | 40,046 | | 69,121 |
| **Total expenses** | $ | 11,594,323 | $ | 9,737,003 |
| Income (loss) before income tax and income (loss) from operating affiliates | | (283,321) | | 795,406 |
| Income (loss) from operating affiliates | | 63,645 | | 44,397 |
| Provision (benefit) for income tax | | 59,070 | | 42,380 |
| **Net income (loss)** | $ | (278,746) | $ | 797,423 |
| Non-controlling interests | | (30,815) | | (50,783) |
| **Net income (loss) attributable to XL Bermuda Ltd** | $ | (309,561) | $ | 746,640 |

See accompanying Notes to Consolidated Financial Statements

# XL BERMUDA LTD
# CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
# FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Net income (loss) attributable to ordinary shareholder** | $ (309,561) | 746,640 |
| Change in net unrealized gains (losses) on investments - excluding Life Funds Withheld Assets, net of tax | 181,711 | (58,217) |
| Change in adjustments related to future policy benefit reserves, net of tax | 27,184 | 62,294 |
| Change in net unrealized gains (losses) on investments - Life Funds Withheld Assets, net of tax | (51,983) | (4,502) |
| Change in net unrealized gains (losses) on affiliate and other investments, net of tax | (5,013) | (57,854) |
| Change in OTTI losses recognized in other comprehensive income, net of tax | 2,415 | 3,670 |
| Change in underfunded pension liability, net of tax | 2,531 | (246) |
| Foreign currency translation adjustments, net of tax | 43,177 | 95,960 |
| **Comprehensive income (loss)** | $ (109,539) | 787,745 |

See accompanying Notes to Consolidated Financial Statements

## XL BERMUDA LTD
## CONSOLIDATED STATEMENTS OF SHAREHOLDER'S EQUITY
## FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Ordinary Shares:** | | |
| Balance – beginning of year | $ 1,250 | $ 1,000 |
| Issuance of ordinary shares | — | 250 |
| **Balance – end of year** | $ 1,250 | $ 1,250 |
| **Additional Paid in Capital:** | | |
| Balance – beginning of year | $ 12,579,844 | $ 13,488,503 |
| Increase in equity of subsidiary | — | 1,341 |
| Return of Capital | — | (910,000) |
| **Balance – end of year** | $ 12,579,844 | $ 12,579,844 |
| **Accumulated Other Comprehensive Income (Loss):** | | |
| Balance – beginning of year | $ 541,900 | $ 500,795 |
| Change in net unrealized gains (losses) on investments - excluding Life Funds Withheld Assets, net of tax | 181,711 | (58,217) |
| Change in adjustments related to future policy benefit reserves, net of tax | 27,184 | 62,294 |
| Change in net unrealized gains (losses) on investments - Life Funds Withheld Assets, net of tax | (51,983) | (4,502) |
| Change in net unrealized gains (losses) on affiliate and other investments, net of tax | (5,013) | (57,854) |
| Change in OTTI losses recognized in other comprehensive income, net of tax | 2,415 | 3,670 |
| Change in underfunded pension liability, net of tax | 2,531 | (246) |
| Foreign currency translation adjustments, net of tax | 43,177 | 95,960 |
| **Balance – end of year** | $ 741,922 | $ 541,900 |
| **Retained Earnings (Deficit):** | | |
| Balance – beginning of year | $ 918,483 | $ 521,843 |
| Net income (loss) attributable to ordinary shareholders | (309,561) | 746,640 |
| Dividends on ordinary shares | (750,000) | (350,000) |
| **Balance – end of year** | $ (141,078) | $ 918,483 |
| **Non-controlling Interest in Equity of Consolidated Subsidiaries:** | | |
| Balance – beginning of year | $ 677,665 | $ 632,883 |
| Non-controlling interests – contributions | 59,583 | 47,524 |
| Non-controlling interests – distributions | (26,092) | (9,028) |
| Non-controlling interests – redeemed | (43,704) | — |
| Non-controlling interests | (10,557) | 7,308 |
| Non-controlling interest share in change in accumulated other comprehensive income (loss) | (816) | (1,022) |
| **Balance – end of year** | $ 656,079 | $ 677,665 |
| **Total Shareholder's Equity** | $ 13,838,017 | $ 14,719,142 |

See accompanying Notes to Consolidated Financial Statements

# XL BERMUDA LTD
# CONSOLIDATED STATEMENTS OF CASH FLOWS
# FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Cash flows provided by (used in) operating activities:** | | |
| Net income (loss) | $ (278,746) | $ 797,423 |
| **Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:** | | |
| Total net realized (gains) losses on investments and net unrealized (gains) losses on investments, trading | (219,750) | (378,540) |
| Net realized and unrealized (gains) losses on derivative instruments | 41,732 | (2,521) |
| Net realized and unrealized (gains) losses on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets | 206,015 | 540,090 |
| Amortization of premiums (discounts) on fixed maturities | 156,855 | 193,482 |
| (Income) loss from investment fund and operating affiliates | (122,487) | (67,802) |
| Loss (gain) on sale of subsidiaries | — | (7,088) |
| Depreciation and amortization | 90,952 | 114,020 |
| Accretion of deposit liabilities | 29,243 | 43,984 |
| **Changes in:** | | |
| Unpaid losses and loss expenses | 2,881,359 | 1,073,313 |
| Future policy benefit reserves | (235,328) | (162,096) |
| Funds withheld on GreyCastle life retrocession arrangements, net | (281,136) | (223,516) |
| Unearned premiums | 733,182 | 436,106 |
| Premiums receivable | (1,200,673) | (1,084,432) |
| Unpaid losses and loss expenses recoverable | (1,575,046) | (360,223) |
| Amounts due from parent and affiliates | (5,669) | (57,899) |
| Ceded unearned premiums | (430,213) | 70,529 |
| Reinsurance balances receivable | (327,462) | (174,126) |
| Deferred acquisition costs and value of business acquired | (118,566) | (62,926) |
| Reinsurance balances payable | 1,120,507 | 398,738 |
| Deferred tax asset – net | (59,498) | (41,641) |
| Derivatives | (18,856) | 119,038 |
| Other assets | (68,370) | (17,549) |
| Other liabilities | (235,142) | (78,896) |
| Other | 68,574 | (72,498) |
| **Total adjustments** | $ 430,223 | $ 197,547 |
| **Net cash provided by (used in) operating activities** | $ 151,477 | $ 994,970 |
| **Cash flows provided by (used in) investing activities:** | | |
| Proceeds from sale of fixed maturities and short-term investments | $ 15,527,115 | $ 12,443,102 |
| Proceeds from redemption of fixed maturities and short-term investments | 3,332,898 | 3,750,469 |
| Proceeds from sale of equity securities | 756,872 | 848,779 |
| Purchases of fixed maturities and short-term investments | (19,073,441) | (14,923,187) |
| Purchases of equity securities | (326,610) | (1,103,447) |
| Proceeds from sale of affiliates | 593,539 | 397,091 |
| Purchases of affiliates | (176,034) | (681,385) |
| Purchase of subsidiaries, net of acquired cash | — | (92,893) |
| Proceeds from sale of subsidiaries, net of cash sold | — | 22,998 |
| Change in restricted cash | (3,993) | 1,488 |
| Other, net | (70,645) | 201,219 |
| **Net cash provided by (used in) investing activities** | $ 559,701 | $ 864,234 |

See accompanying Notes to Consolidated Financial Statements

# XL BERMUDA LTD
# CONSOLIDATED STATEMENTS OF CASH FLOWS
# FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Cash flows provided by (used in) financing activities:** | | |
| Dividends paid on ordinary shares | (750,000) | (350,000) |
| Distributions to non-controlling interests | (65,678) | (51,852) |
| Contributions from non-controlling interests | 59,583 | 47,524 |
| (Distribution)/Contribution to/from Parent Company | | (910,000) |
| Repurchase of preference shares | (45,581) | — |
| Deposit liabilities | (34,565) | (69,482) |
| **Net cash provided by (used in) financing activities** | $ (836,241) | $ (1,333,810) |
| Effects of exchange rate changes on foreign currency cash | 56,699 | (57,742) |
| Increase (decrease) in cash and cash equivalents | $ (68,364) | $ 467,652 |
| Cash and cash equivalents – beginning of period | 3,341,679 | 2,874,027 |
| Cash and cash equivalents – end of period | $ 3,273,315 | $ 3,341,679 |
| | | |
| Net taxes paid | $ 30,955 | $ 81,315 |

See accompanying Notes to Consolidated Financial Statements

## 1. General

XL Bermuda Ltd (the “Company” or “XLB”) was formed June 2016 under the laws of Bermuda as the result of the amalgamation of two Bermuda operating entities, XL Insurance (Bermuda) Ltd and XL Re Ltd and is registered as a Class 4E insurer. The Company’s ultimate parent is XL Group Ltd ("XL"), a Bermuda exempted company.

On July 25, 2016, XL Group plc, an Irish public limited company ("XL-Ireland"), and XL completed a scheme of arrangement under Irish law (the "Scheme of Arrangement") that effected a transaction (the "Redomestication") that resulted in the shareholders of XL-Ireland becoming shareholders of XL and XL-Ireland becoming a subsidiary of XL.

In connection with the Redomestication, on August 3, 2016, XL-Ireland distributed the ordinary shares of XLIT Ltd. (formerly XL Capital Ltd.), a Cayman Islands exempted company ("XL-Cayman"), to XL (the “Distribution”), which was recorded on the share register of XL-Cayman on August 4, 2016. As a result of the Distribution, XL-Cayman is now a direct, wholly-owned subsidiary of XL. It is anticipated that XL-Ireland will be liquidated (via a solvent members voluntary liquidation which was initiated on August 2, 2016) by the end of 2018.

The Company and its operating subsidiaries are a leading provider of insurance and reinsurance coverages to industrial, commercial and professional firms, insurance companies and other enterprises on a worldwide basis. The Company and its various subsidiaries operate globally in 29 countries, through the Company's two business operations: Insurance and Reinsurance.

### Insurance Operations

The Company’s insurance operations are organized to pair our global industry and product expertise with a strong regional presence and local infrastructure that includes decision makers familiar with local needs and market dynamics. It includes three business groups: North America, International and Global Lines.

North America provides primary and excess casualty, environmental liability, professional liability, property, excess and surplus lines, U.S. program/facilities and construction business.

International provides property, primary and excess casualty, environmental liability, professional liability, construction, mergers & acquisitions and structured risk solutions.

Global Lines includes the following lines of business: aviation & satellite, marine (including North America inland marine), fine art & specie, private clients, equine, livestock & aquaculture, energy, crisis management, political risk, credit & bond, London wholesale property & casualty and life, accident & health

### Reinsurance Operations

The Company’s Reinsurance operations are structured into five business groups mainly based on region: Bermuda; North America; London; EMEA; and Latin America, Asia Pacific & Credit ("LAC").

The Reinsurance operations provide casualty, property risk, property catastrophe, specialty, and other reinsurance lines on a global basis with business being written on both a proportional and non-proportional treaty basis, and also on a facultative basis.

### Run-Off Life Operations

The Company ceased writing new life reinsurance in 2009 and since that time have been managing the run-off of the life reinsurance operations ("Run-Off Life Operations"). On May 30, 2014, XLB completed a transaction with GreyCastle Holdings Ltd ("GreyCastle") that resulted in sale of the Company's wholly-owned subsidiary, XL Life Reinsurance (SAC) Ltd ("XLLR"), to GreyCastle (subsequent to the transaction, XLLR changed its name to GreyCastle Life Reinsurance (SAC) Ltd ("GCLR")). As a result of the transaction, the Company has ceded the majority of the life reinsurance business to GCLR via 100% quota share reinsurance (the "GreyCastle Life Retro Arrangements"). This transaction covers a substantial portion of XLB's life reinsurance reserves. During 2015, the Company entered into another reinsurance agreement (the "U.S. Term Life Retro Arrangements") ceding the majority of the remaining life reinsurance business.

## 2. Significant Accounting Policies

### (a) Basis of Preparation and Consolidation

These consolidated financial statements include the accounts of the Company and all of its subsidiaries. These consolidated financial statements have been prepared in conformity with GAAP. To facilitate period-to-period comparisons, certain reclassifications have been made to prior year consolidated financial statement amounts to conform to the current year presentation. There was no effect on net income from this change in presentation.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company's most significant areas of estimation include:

- unpaid losses and loss expenses and unpaid losses and loss expenses recoverable;
- future policy benefit reserves;
- valuation and other-than-temporary impairments of investments;
- income taxes;
- reinsurance premium estimates; and
- carrying value of goodwill and intangible assets.

While management believes that the amounts included in the consolidated financial statements reflect the Company's best estimates and assumptions, actual results could differ materially from these estimates.

### (b) Fair Value Measurements

*Financial Instruments Subject to Fair Value Measurements*

Accounting guidance over fair value measurements requires that a fair value measurement reflect the assumptions market participants would use in pricing an asset or liability based on the best information available. Assumptions include the risks inherent in a particular valuation technique (such as a pricing model) and/or the risks inherent in the inputs to the model. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the "exit price"). Instruments that the Company owns ("long positions") are marked to bid prices and instruments that the Company has sold but not yet purchased ("short positions") are marked to offer prices. Fair value measurements are not adjusted for transaction costs.

*Basis of Fair Value Measurement*

Fair value measurements accounting guidance also establishes a fair value hierarchy that prioritizes the inputs to the respective valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). An asset or liability's classification within the fair value hierarchy is based on the lowest level of significant input to its valuation. The three levels of the fair value hierarchy are described further below:

- **Level 1** - Quoted prices in active markets for identical assets or liabilities (unadjusted); no blockage factors.
- **Level 2** - Other observable inputs (quoted prices in markets that are not active or inputs that are observable either directly or indirectly)-include quoted prices for similar assets/liabilities (adjusted) other than quoted prices in Level 1; quoted prices in markets that are not active; or other inputs that are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.
- **Level 3** - Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Unobservable inputs reflect the reporting entity’s own assumptions about the assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose values are determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Details on assets and liabilities that have been included under the requirements of authoritative guidance on fair value measurements to illustrate the bases for determining the fair values of these items held by the Company are included in each respective section of this note.

Fair values of investments and derivatives are based on published market values if available, estimates of fair values of similar issues, or estimates of fair values provided by independent pricing services and brokers. Fair values of financial instruments for which quoted market prices are not available or for which the Company believes current trading conditions represent distressed markets are based on estimates using present value or other valuation techniques. The fair values estimated using such techniques are significantly affected by the assumptions used, including the discount rates and the estimated amounts and timing of future cash flows. In such instances, the derived fair value estimates cannot be substantiated by comparison to independent markets and are not necessarily indicative of the amounts that would be realized in a current market exchange.

**(c) Investments**

*Investments - Available For Sale*

Investments that are considered available for sale ("AFS") (comprised of fixed maturities, equity securities and short-term investments) are carried at fair value. The fair values for AFS investments are generally sourced from third parties. The fair values of fixed income securities are based upon quoted market values where available, "evaluated bid" prices provided by third party pricing services ("pricing services") where quoted market values are not available, or by reference to broker or underwriter bid indications where pricing services do not provide coverage for a particular security. To the extent the Company believes current trading conditions represent distressed transactions, the Company may elect to utilize internally generated models.

It is common industry practice to utilize pricing services as a source for determining the fair values of investments where the pricing services are able to obtain sufficient market-corroborating information to allow them to produce a valuation at a reporting date. In addition, in the majority of cases, although a value may be obtained from a particular pricing service for a security or class of similar securities, these values are corroborated against values provided by other pricing services. The pricing services use market approaches to valuations using primarily Level 2 inputs in the vast majority of valuations, or some form of discounted cash flow analysis, to obtain investment values for a small percentage of fixed income securities for which they provide a price. Standard inputs to the valuations provided by the pricing services listed in approximate order of priority for use when available include: reported trades, benchmark yields, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data. The pricing services may prioritize inputs differently on any given day for any security, and not all inputs listed are available for use in the evaluation process on any given day for each security evaluation; however, the pricing services also monitor market indicators, customer feedback through a price challenge process and industry and economic events. Information of this nature is a trigger to acquire further corroborating market data. When these inputs are not available, they identify "buckets" of similar securities (allocated by asset class types, sectors, sub-sectors, contractual cash flows/structure, and credit rating characteristics) and apply some form of matrix or other modeled pricing to determine an appropriate security value that represents their best estimate as to what a buyer in the marketplace would pay for a security in a current sale. Prices provided by independent pricing services and independent broker quotes can vary widely even for the same security. The use of different methodologies and assumptions may have a material effect on the estimated fair value amounts. While the Company receives values for the majority of the investment securities it holds from pricing services, it is ultimately management's responsibility to determine whether the values received and recorded in the financial statements are representative of appropriate fair value measurements.

Broker/dealer quotations are used to value fixed maturities where prices are unavailable from pricing services due to factors specific to the security such as limited liquidity, lack of current transactions, or trades only taking place in privately negotiated transactions. These are considered Level 3 valuations, as significant inputs utilized by brokers may be difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification.

Equity securities include investments in open-end mutual funds, exchange-traded funds and shares of publicly traded companies. The fair value of equity securities is based upon quoted market values (Level 1), or monthly net asset value statements provided by the investment managers upon which subscriptions and redemptions can be executed (Level 2).

Short-term investments include investments due to mature within one year from the date of purchase and are valued using the same external factors and in the same manner as fixed income securities.

Changes in the value of investments available for sale are reflected as unrealized gains or losses on investments, and are included in "accumulated other comprehensive income (loss)", on a net of tax basis.

All investment transactions are recorded on a trade date basis. Realized gains and losses on sales of equities and fixed income investments are determined on a first-in, first-out basis.

Investment income is recognized when earned, and includes interest and dividend income together with the amortization of premium and discount on fixed maturities and short-term investments, and is recorded net of related investment expenses. Amortization of discounts on fixed maturities includes amortization to expected recovery values for investments that have previously been recorded as other-than-temporarily impaired. For mortgage-backed securities, and any other holdings for which there is a prepayment risk, prepayment assumptions are evaluated and revised as necessary. Prepayment fees or call premiums that are payable to the Company only when a security is called prior to its maturity are earned when received and reflected in net investment income.

*Investments -Trading*

Investments for which the Company has elected the fair value option are classified as "trading". Trading securities are carried at fair value. All trading securities are held in support of the GreyCastle Life Retro Arrangements, as defined in Note 1. Thus, changes in the fair value of trading securities are included in "Net unrealized gains (losses) on investments, trading securities - Life Funds Withheld Assets," and interest and dividend income from trading securities are included as a component of "Net investment income - Life Funds Withheld Assets".

*Investments Related to Life Retrocession Arrangements written on a Funds Withheld Basis*

Designated investments that support the GreyCastle Life Retro Arrangements, which were written on a funds withheld basis ("Life Funds Withheld Assets") and entered into in connection with the sale of XLB's life reinsurance subsidiary are classified as either available for sale or trading. Investment results for these assets - including interest income, unrealized gains and losses, and gains and losses from sales - are passed directly to the reinsurer pursuant to a contractual arrangement that is accounted for as a derivative.

Changes in the fair value of the embedded derivative associated with the GreyCastle Life Retro Arrangements are recorded in "Net realized and unrealized gains (losses) on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets" on the Consolidated Statements of Income. The fair value of the embedded derivative is included within "Funds withheld on life retrocession arrangements, net of future policy benefit reserves recoverable" on the Consolidated Balance Sheets.

*Investments In Affiliates*

Investments in which the Company has significant influence over the operating and financial policies of the investee are classified as investments in affiliates on the Company's Consolidated Balance Sheets and are accounted for under the equity method of accounting. Under this method, the Company records its proportionate share of income or loss from such investments in its results for the period as well as its portion of movements in certain of the investee shareholders' equity balances. When financial statements of the affiliate are not available on a timely basis to record the Company's share of income or loss for the same reporting periods as the Company, the most recently available financial statements are used. This lag in reporting is applied consistently. Distributions received from affiliates representing returns on invested capital are recorded as operating cash flows, while distributions representing returns of invested capital or proceeds upon sale of all or a portion of an affiliate are recorded as investing cash flows.

The Company generally records its hedge fund and private investment affiliates on a one-month and three-month lag, respectively, and its operating affiliates on a three-month lag. Significant influence is considered on a case-by-case basis. Investments in affiliates are not subject to fair value measurement guidance as they are not considered to be fair value measured investments under GAAP. However, impairments associated with investments in affiliates that are deemed to be other-than-temporary are calculated in accordance with fair value measurement guidance and appropriate disclosures included within the financial statements during the period the losses are recorded.

*Other Investments*

Contained within this asset class are equity interests in investment funds, limited partnerships and unrated tranches of collateralized debt obligations for which the Company does not have sufficient rights or ownership interests to follow the equity method of accounting. Also included within other investments are structured transactions, which are carried at amortized cost.

Fair values for other investments, principally other direct equity investments, investment funds and limited partnerships, are primarily based on the net asset value provided by the investment manager, the general partner or the respective entity, recent financial information, available market data and, in certain cases, management judgment. These entities generally carry their trading positions and investments, the majority of which have underlying securities valued using Level 1 or Level 2 inputs, at fair value as determined by their respective investment managers; accordingly, these investments are generally classified as Level 2. Investments for which fair value is estimated using net asset value per share as a practical expedient are excluded from the fair value hierarchy. Private equity investments are classified as Level 3. The net unrealized gain or loss on investments, net of tax, is included in "Accumulated other comprehensive income (loss)." Any unrealized loss in value considered by management to be other-than-temporary is charged to income in the period in which such determination is made.

Overseas deposits include investments in private funds related to Lloyd's syndicates in which the underlying instruments are primarily fixed maturities. The funds themselves do not trade on an exchange and therefore are not included within available for sale securities. Also included in overseas deposits are restricted balances held by Lloyd's syndicates for solvency purposes which are primarily invested in cash and cash equivalents. Given the restricted nature of these balances, they are included in other investments on the Consolidated Balance Sheets. Each of these investment types is considered a Level 2 valuation.

The Company has historically participated in structured transactions. These have included providing cash loans supporting project finance transactions and providing liquidity facility financing to structured project deals. The Company also invested in a payment obligation with an insurance company. The Company's policy is to value such transactions at amortized cost. For further details see Note 8, "Fair Value Measurements" and Note 6, "Other Investments."

**(d) Premiums and Acquisition Costs**

Insurance premiums written are recorded in accordance with the terms of the underlying policies. Reinsurance premiums written are recorded at the inception of the policy and are estimated based upon information received from ceding companies and any subsequent differences arising on such estimates are recorded in the period they are determined. For multi-year reinsurance treaties which are payable in annual installments, generally, only the initial annual installment is included as premiums written at policy inception due to the ability of the reinsured to commute or cancel coverage during the term of the policy. The remaining annual installments are included as premiums written at each successive anniversary date within the multi-year term.

Premiums are generally earned on a pro-rata basis over the period the coverage is provided. Unearned premiums represent the portion of premiums written applicable to the unexpired terms of policies in force. Net premiums earned are presented after deductions for reinsurance ceded, as applicable. Premiums receivable are reported net of commissions payable and allowance for estimated uncollectible amounts.

Reinstatement premiums are recognized at the time a loss event occurs where coverage limits for the remaining life of the contract are reinstated under pre-defined contract terms and are fully earned when recognized.

Life and annuity premiums from long duration contracts that transfer significant mortality or morbidity risks are recognized as revenue and earned when due from policyholders. Life and annuity premiums from long duration contracts that do not subject the Company to risks arising from policyholder mortality or morbidity are accounted for as investment contracts and presented within deposit liabilities.

The Company has periodically written retroactive loss portfolio transfer contracts. These contracts are evaluated to determine whether they meet the established criteria for reinsurance accounting, and, if so, at inception, written premiums are fully earned and corresponding losses and loss expense recognized. The contracts can cause significant variances in gross premiums written, net premiums written, net premiums earned, and net incurred losses in the years in which they are written. Reinsurance contracts sold not meeting the established criteria for reinsurance accounting are recorded using the deposit method.

Acquisition costs, which vary with and are directly related to the acquisition of policies, consist primarily of: a) commissions paid to brokers and cedants, and b) premium-related taxes are deferred and amortized over the period during which the premiums are earned. Acquisition costs are shown net of contractual commissions earned on reinsurance ceded. Future earned premiums, the anticipated losses and other costs (and in the case of a premium deficiency, investment income) related to those premiums, are also considered in determining the level of acquisition costs to be deferred.

**(e) Reinsurance**

In the normal course of business, the Company seeks to reduce the potential amount of loss arising from claims events by reinsuring certain levels of risk assumed in various areas of exposure with other insurers or reinsurers. Reinsurance premiums ceded are expensed (and any commissions recorded thereon are earned) on a monthly pro-rata basis over the period the reinsurance coverage is provided. Ceded unearned reinsurance premiums represent the portion of premiums ceded applicable to the unexpired term of policies in force. Reinstatement premiums ceded are recognized at the time a loss event occurs where coverage limits for the remaining life of the contract are reinstated under pre-defined contract terms and are fully earned when recognized. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Provisions are made for estimated unrecoverable reinsurance.

The Company enters into ceded reinsurance agreements with other companies in the normal course of business. All premium and loss-related balances related to reinsurance agreements are reported on a gross basis within XLB's Consolidated Balance Sheets, with the exception of the GreyCastle Life Retro Arrangements, which were written on a funds withheld basis. The future policy benefit reserves recoverable related to these retrocession arrangements are netted against the funds withheld liability owing to the counterparty on the Consolidated Balance Sheets due to the contractual right of offset.

**(f) Fee Income and Other**

Fee income and other includes fees received for insurance, loss prevention consulting services and product structuring services provided and is earned over the service period of the contract. Any adjustments to fees earned or the service period are reflected in income in the period when determined.

**(g) Other-Than-Temporary Impairments ("OTTI") of Available for Sale Securities**

The Company's process for identifying declines in the fair value of investments that are other-than-temporary involves consideration of several factors. The primary factors include (i) an analysis of the liquidity, business prospects and financial condition of the issuer, including consideration of credit ratings, (ii) the significance of the decline, (iii) an analysis of the collateral structure and other credit support, as applicable, of the securities in question, and (iv) for debt securities, whether the Company intends to sell such securities. In addition, the authoritative guidance requires that OTTI for certain asset-backed and mortgage-backed securities be recognized if the fair value of the security is less than its discounted cash flow value and there has been a decrease in the present value of the expected cash flows since the last reporting period. Where the Company's analysis of the above factors results in the Company's conclusion that declines in fair values are other-than-temporary, the cost of the security is written down to discounted cash flow, and a portion of the previously unrealized loss is therefore realized in the period such determination is made.

With respect to equity securities and other investments carried at fair value, we generally impair a security if its fair value is 50% or lower than its amortized cost or if the security is in a loss position for 11 or more consecutive months.

If the Company intends to sell an impaired security, or it is more likely than not that it will be required to sell the security before recovery of its amortized cost basis, the impairment is other-than-temporary and is recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost.

In instances in which the Company determines that a credit loss exists but the Company does not intend to sell the security, and it is not more likely than not that the Company will be required to sell the security before the anticipated recovery of its remaining amortized cost basis, the OTTI is separated into (1) the amount of the total impairment related to the credit loss and (2) the amount of the total impairment related to all other factors (i.e. the noncredit portion). The amount of the total OTTI related to the credit loss is recognized in earnings and the amount of the total OTTI related to all other factors is recognized in accumulated other comprehensive loss. The total OTTI is presented in the Consolidated Statements of Income with an offset for the amount of the total OTTI that is recognized in accumulated other comprehensive income (loss). Absent the intent or requirement to sell a security, if a credit loss does not exist, any impairment is considered to be temporary.

The noncredit portion of any OTTI losses on securities classified as available for sale is recorded as a component of other comprehensive income (loss) with an offsetting adjustment to the carrying value of the security. The fair value adjustment could increase or decrease the carrying value of the security.

In periods subsequent to the recognition of an OTTI loss, the other-than-temporarily impaired debt security is accounted for as if it had been purchased on the measurement date of the OTTI at an amount equal to the previous amortized cost basis less the credit-related OTTI recognized in earnings. For debt securities for which credit-related OTTI is recognized in earnings, the difference between the new cost basis and the cash flows expected to be collected is accreted into interest income over the remaining life of the security in a prospective manner based on the estimated amount and timing of future estimated cash flows.

With respect to securities where the decline in value is determined to be temporary and the security's amortized cost is not written down, a subsequent decision may be made to sell that security and realize a loss. Subsequent decisions on security sales are made within the context of overall risk monitoring, changing information, market conditions generally and assessing value relative to other comparable securities. We have outsourced a significant portion of the day-to-day management of the Company's investment portfolio to third party investment manager service providers. While these investment manager service providers may, at a given point in time, believe that the preferred course of action is to hold securities with unrealized losses that are considered temporary until such losses are recovered, the dynamic nature of the portfolio management may result in a subsequent decision to sell the security and realize the loss, based upon a change in market and other factors described above. The Company believes that subsequent decisions to sell such securities are consistent with the classification of the Company's portfolio as available for sale.

There are risks and uncertainties associated with determining whether declines in the fair value of investments are other-than-temporary. These include subsequent significant changes in general economic conditions as well as specific business conditions affecting particular issuers, subjective assessment of issue-specific factors (seniority of claims, collateral value, etc.), future financial market effects, stability of foreign governments and economies, future rating agency actions and significant disclosure of accounting, fraud or corporate governance issues that may adversely affect certain investments. In addition, significant assumptions and management judgment are involved in determining if the decline is other-than-temporary. If management determines that a decline in fair value is temporary, then a security's value is not written down at that time. However, there are potential effects upon the Company's future earnings and financial position should management later conclude that some of the current declines in the fair value of the investments are other-than-temporary declines.

**(h) Derivative Instruments**

The Company recognizes all derivatives as either assets or liabilities on the Consolidated Balance Sheets and measures those instruments at fair value. Except for the embedded derivative associated with the GreyCastle Life Retro Arrangements discussed above within (c) "Investments Related to Life Retrocession Arrangements written on a Funds Withheld Basis,"the changes in fair value of derivatives are shown in the Consolidated Statements of Income as "net realized and unrealized gains (losses) on derivative instruments," unless the derivatives are designated as hedging instruments. The accounting for derivatives that are designated as hedging instruments is discussed below. Changes in the fair value of derivatives may create volatility in the Company's results of operations from period to period. Amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) are offset against net fair value amounts recognized in the Consolidated Balance Sheets for derivative instruments executed with the same counterparty under the same netting arrangement to the extent that the Company intends to settle the amounts on a net basis.

Derivative contracts can be exchange-traded or over-the-counter ("OTC"). Exchange-traded derivatives (futures and options) typically fall within Level 1 of the fair value hierarchy, depending on whether they are deemed to be actively traded or not. OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources where an understanding of the inputs utilized in arriving at the valuations is obtained. Where models are used, the selection of a particular model to value an OTC derivative depends upon the contractual terms and specific risks inherent in the instrument as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, interest rate swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment. Such instruments comprise the majority of derivatives held by the Company and are typically classified within Level 2 of the fair value hierarchy.

Certain OTC derivatives trade in less liquid markets with limited pricing information, or required model inputs that are not directly market corroborated, which causes the determination of fair value for these derivatives to be inherently more subjective. Accordingly, such derivatives are classified within Level 3 of the fair value hierarchy. The valuations of less standard or less liquid OTC derivatives are typically based on Level 1 and/or Level 2 inputs that can be observed in the market, as well as unobservable Level 3 inputs. Level 1 and Level 2 inputs are regularly updated to reflect observable market changes. Level 3 inputs are changed only when corroborated by evidence such as similar market transactions, pricing services and/or broker or dealer quotations. The Company conducts its non-hedging derivatives activities in three main areas: investment related derivatives, credit derivatives and other non-investment-related derivatives.

The Company uses derivative instruments, primarily interest rate swaps, to manage the interest rate exposure associated with certain assets and liabilities. These derivatives are recorded at fair value. On the date the derivative contract is entered into, the Company may designate the derivative as: a hedge of the fair value of a recognized asset or liability ("fair value" hedge); a hedge of the variability in cash flows of a forecasted transaction or of amounts to be received or paid related to a recognized asset or liability ("cash flow" hedge); or a hedge of a net investment in a foreign operation. Alternatively, the Company may not designate any hedging relationship for a derivative contract.

*Fair Value Hedges*

Changes in the fair value of a derivative that is designated and qualifies as a fair value hedge, along with the changes in the fair value of the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings (through "net realized and unrealized gains and losses on derivative instruments"), with any differences between the net change in fair value of the derivative and the hedged item representing the hedge ineffectiveness. Periodic derivative net coupon settlements are recorded in net investment income, with the exception of hedges of Company-issued debt, which are recorded in interest expense. The Company may designate fair value hedging relationships where interest rate swaps are used to hedge the changes in the fair value of certain fixed rate liabilities and fixed maturity securities due to changes in the designated benchmark interest rate.

*Cash Flow Hedges*

Changes in the fair value of a derivative that is designated and qualifies as a cash flow hedge are recorded in accumulated other comprehensive income ("AOCI") and are reclassified into earnings when the variability of the cash flow of the hedged item impacts earnings. Gains and losses on derivative contracts that are reclassified from AOCI to current period earnings are included in the line item in the consolidated statements of operations in which the cash flows of the hedged item are recorded. Any hedge ineffectiveness is recorded immediately in current period earnings as "net realized and unrealized gains and losses on derivative instruments." Periodic derivative net coupon settlements are recorded in net investment income. The Company may designate cash flow hedging relationships where interest rate swaps are used to mitigate interest rate risk associated with anticipated issuances of debt or other forecasted transactions.

*Hedges of the Net Investment in a Foreign Operation*

Changes in the fair value of a derivative used as a hedge of a net investment in a foreign operation, to the extent effective as a hedge, are recorded in the foreign currency translation adjustments account within AOCI. Cumulative changes in fair value recorded in AOCI are reclassified into earnings upon the sale or complete or substantially complete liquidation of the foreign entity. Any hedge ineffectiveness is recorded immediately in current period earnings as "net realized and unrealized gains and losses on derivative instruments."

*Hedge Documentation and Effectiveness Testing*

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated changes in value or cash flow of the hedged item. At hedge inception, the Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking each hedge transaction. The documentation process includes linking derivatives that are designated as fair value, cash flow, or net investment hedges to specific assets or liabilities on the balance sheet or to specific forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. In addition, certain hedging relationships are considered highly effective if the changes in the fair value or discounted cash flows of the hedging instrument are within a ratio of 80-125% of the inverse changes in the fair value or discounted cash flows of the hedged item. Hedge ineffectiveness is measured using qualitative and quantitative methods. Qualitative methods may include comparison of critical terms of the derivative to the hedged item. Depending on the hedging strategy, quantitative methods may include the "Change in Variable Cash Flows Method," the "Change in Fair Value Method," the "Hypothetical Derivative Method" or the "Dollar Offset Method."

*Discontinuance of Hedge Accounting*

The Company discontinues hedge accounting prospectively when: it determines that the derivative is no longer highly effective in offsetting changes in the fair value or cash flows of a hedged item; the derivative is dedesignated as a hedging instrument; or the derivative expires or is sold, terminated or exercised. When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective fair-value hedge, the derivative continues to be carried at fair value on the balance sheets with changes in its fair value recognized in current period earnings through "net realized and unrealized gains and losses on derivative instruments." When hedge accounting is discontinued because the Company becomes aware that it is not probable that the forecasted transaction will occur, the derivative continues to be carried on the balance sheets at its fair value, and gains and losses that were accumulated in AOCI are recognized immediately in earnings.

**(i) Cash and Cash Equivalents**

*Cash Equivalents*

Cash equivalents include fixed interest deposits placed with a maturity of under 90 days when purchased. Bank deposits are not considered to be fair value measurements and as such are not subject to the authoritative guidance on fair value measurement disclosures. Money market funds are classified as Level 1, as these instruments are considered actively traded; however, certificates of deposit are classified as Level 2.

*Restricted Cash*

Restricted cash represents cash and cash equivalents that the Company is a) holding for the benefit of a third party and is legally or contractually restricted as to withdrawal or usage for general corporate purposes; and b) not replaceable by another type of asset other than cash or cash equivalents, under the terms of the Company's contractual arrangements with such third parties. Restricted cash includes cash and cash equivalents held pursuant to the terms of the Company's contractual obligations relating to the GreyCastle Life Retro Arrangements described in Note 1.

**(j) Foreign Currency Revaluation and Translation**

Monetary assets and liabilities denominated in currencies other than the functional currency of the applicable Company subsidiaries in which those monetary assets and liabilities reside are revalued into the appropriate functional currency at prevailing balance sheet-date exchange rates. Revenues and expenses denominated in currencies other than the functional currency of the applicable Company subsidiaries in which those revenues and expenses reside, are valued at the exchange rates on the dates on which those underlying revenue and/or expense transactions occur. The net effect of these revaluation adjustments are recognized in the Consolidated Statements of Income as part of "Foreign exchange (gains) losses".

Assets and liabilities of foreign operations whose functional currency is not the U.S. dollar are then translated into the Company's U.S. reporting currency at prevailing balance sheet-date exchange rates, while revenue and expenses of such foreign operations are translated into the Company's U.S. reporting currency at monthly average exchange rates during the year. The net effect of these translation adjustments, as well as any gains or losses on intercompany balances for which settlement is not planned or anticipated in the foreseeable future, net of applicable deferred income taxes, are included in the Consolidated Balance Sheets as part of "Accumulated other comprehensive income."

**(k) Goodwill, Intangibles and Other Long-Lived Assets**

The Company has recorded goodwill in connection with various acquisitions in prior years. Goodwill represents the excess of the purchase price over the fair value of the net assets acquired. In accordance with GAAP, the Company tests goodwill for potential impairment annually as of June 30, and between annual tests if an event occurs or circumstances change that may indicate that the potential exists for the fair value of a reporting unit to be reduced to a level below its carrying amount. The Company tests for impairment at the reporting unit level in accordance with the authoritative guidance on intangibles and goodwill. The Company has organized its goodwill into two reporting units, reflecting its two operations.

The Company's indefinite-lived intangible assets consist primarily of Lloyd's syndicate capacity plus acquired insurance and reinsurance licenses. These assets are deemed to have indefinite useful lives and are therefore not subject to amortization. In accordance with GAAP, the Company tests non-amortized intangible assets for potential impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. If the carrying value of a non-amortized intangible asset is in excess of its fair value, the asset must be written down to its fair value through the recognition of an impairment charge to earnings.

All of the Company's depreciable or amortizable intangible and other long-lived assets such as trade names, distribution networks, premises, equipment, agency relationships, and acquired or internally-developed software, are carried at net book value, and are depreciated or amortized on a straight-line basis over their estimated useful lives. The amortization periods approximate the period over which the Company expects to generate future net cash inflows from the use of these assets. All of these assets are subject to impairment testing in accordance with authoritative guidance for the impairment or disposal of long-lived assets when events or conditions indicate that the carrying value of an asset may not be fully recoverable from future cash flows. See Note 9, "Goodwill and Other Intangible Assets" for further information.

**(l) Variable Interest Entities ("VIEs")**

Investments or other interests that absorb portions of an entity's expected losses or receive portions of the entity's expected residual returns are called variable interests. Entities in which the equity investors, as a group, do not have the characteristic of a controlling financial interest, or that do not have sufficient equity at risk to allow them to finance their own activities without additional financial support are referred to as VIEs.

A VIE must be consolidated by its primary beneficiary, which is the variable interest holder that is determined to have the controlling financial interest in the entity. This is the entity that has both: a) the power to direct the VIE's activities that most significantly impact its economic performance, and b) the obligation to absorb losses or receive benefits of the VIE that could potentially be significant to it. Refer to Note 16, "Variable Interest Entities," for further discussion of the Company's interests in VIEs.

**(m) Non-controlling Interests**

Non-controlling shareholders' interests are presented separately in the Company's Consolidated Balance Sheets and Consolidated Statements of Shareholders' Equity as required under GAAP. The net loss (income) attributable to non-controlling interests is presented separately in the Company's Consolidated Statements of Comprehensive Income. Refer to Note 16, "Variable Interest Entities," and Note 19, "Share Capital," for further discussion of non-controlling interests in the Company.

**(n) Losses and Loss Expenses**

Unpaid losses and loss expenses include reserves for reported unpaid losses and loss expenses and for losses incurred but not reported. The reserve for reported unpaid losses and loss expenses for the Company's property and casualty ("P&C") operations is established by management based on claims reported from insureds or amounts reported from ceding companies, and represent the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company.

The reserve for losses incurred but not reported is estimated by management based on loss development patterns determined by reference to the Company's underwriting practices, the policy form, type of program and historical experience. The Company's actuaries employ a variety of generally accepted methodologies to determine estimated ultimate loss reserves, including the "Bornhuetter-Ferguson incurred loss method" and frequency and severity approaches.

Certain workers' compensation and certain U.K. bodily injury liabilities are considered fixed and determinable and are discounted.

Management believes that the reserves for unpaid losses and loss expenses are sufficient to cover losses that fall within coverages assumed by the Company. However, there can be no assurance that losses will not exceed the Company's total reserves. The methodology of estimating loss reserves is periodically reviewed to ensure that the assumptions made continue to be appropriate and any adjustments resulting from such reviews are reflected in income in the year in which the adjustments are made.

**(o) Deposit Liabilities**

Contracts entered into by the Company that are not deemed to transfer significant underwriting risk and/or timing risk are accounted for as deposits, whereby liabilities are initially recorded at an amount equal to the assets received. The Company uses a portfolio rate of return of equivalent duration to the liabilities in determining risk transfer. An initial accretion rate is established based on actuarial estimates whereby the deposit liability is increased to the estimated amount payable over the term of the contract.

The deposit accretion rate is the rate of return required to fund expected future payment obligations (this is equivalent to the "best estimate" of future cash flows), which are determined actuarially based upon the nature of the underlying indemnifiable losses. Accretion of the liability is recorded as interest expense.

The Company periodically reassesses the estimated ultimate liability. Any changes to this liability are reflected as adjustments to interest expense to reflect the cumulative effect of the period the contract has been in force, and by an adjustment to the future accretion rate of the liability over the remaining estimated contract term.

**(p) Future Policy Benefit Reserves**

The Company estimates the present value of future policy benefits related to long duration contracts using assumptions for investment yields, mortality, and expenses, including a provision for adverse deviation.

The assumptions used to determine future policy benefit reserves are best estimate assumptions that are determined at the inception of the contracts and are locked-in throughout the life of the contract unless a premium deficiency develops. As the experience on the contracts emerges, the assumptions are reviewed. If such review would produce reserves in excess of those currently held, then the locked-in assumptions will be revised and a claim and policy benefit is recognized at that time. The Company includes the cost of reinsurance in its premium deficiency considerations.

Certain life insurance and annuity contracts provide the holder with a guarantee that the benefit received upon death will be no less than a minimum prescribed amount. The contracts are accounted for in accordance with GAAP, which requires that the best estimate of future experience be combined with actual experience to determine the benefit ratio used to calculate the policy benefit reserve.

**(q) Income Taxes**

The Company accounts for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, we determine deferred tax assets and liabilities on the basis of the differences between the financial statement and tax bases of assets and liabilities by using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

The Company recognizes deferred tax assets to the extent that we believe that these assets are more likely than not to be realized. In making such a determination, we consider all available positive and negative evidence, including future reversals of existing temporary differences, projected future taxable income, tax planning strategies, and taxable income in prior years that may be available for carryback. A valuation allowance will be established for any portion of a deferred tax asset that we believe will not be realized, and the impact will be included in the provision for income taxes.

The Company records uncertain tax positions in accordance with ASC 740 on the basis of a two- step process in which (1) we determine whether it is more likely than not that the tax positions will be sustained on the basis of the technical merits of the position and (2) for those tax positions that meet the more likely than not recognition threshold, we recognize the largest amount of tax benefit that is more than 50 percent likely to be realized upon settlement with the tax authority.

The Company recognizes interest and penalties on underpaid tax as a component of income tax expense.

The Company's investment income is allocated to applicable branch operations and is taxable in certain jurisdictions. The method of allocating this income may be different for tax reporting as compared to GAAP. The Company records the tax effects of this allocation entirely through operations.

**(r) Recent Accounting Pronouncements**

**Recently Issued Accounting Standards Adopted in 2017**

*ASU 2016-17 Interests Held through Related Parties That Are under Common Control*

In October 2016, the FASB issued an accounting standards update concerning the evaluation of indirect interests held through related parties during the assessment of variable interest entities ("VIEs"). When identifying the primary beneficiary of a VIE, this update requires a reporting entity that acts as the single decision maker of that VIE to include, on a proportionate basis, those interests held through related parties under common control when assessing whether it holds a variable interest in that VIE. This is a change from previous GAAP, which required such indirect interests to be included in their entirety during this assessment. In the event that a reporting entity is not considered to be the primary beneficiary of the VIE following this assessment, the update does not change the requirement to assess whether the entity and its related parties under common control as a group possess the characteristics of a primary beneficiary. The guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments in this update were to be applied retrospectively to all periods since Accounting Standards Update 2015-02 was adopted, which for the Company was the first quarter of 2016. The Company adopted this guidance in 2017. There were no changes to the identified primary beneficiaries of any VIEs in which the Company holds an interest, and thus no impact on the Company's financial position, results of operations or cash flows.

*ASU 2017-04 Simplifying the Test for Goodwill Impairment*

In January 2017, the FASB issued an accounting standards update concerning impairment testing of goodwill. The main provision of this guidance removes the existing "Step 2" analysis required under previous GAAP. The previous GAAP required an entity to perform procedures to determine the fair value at the impairment testing date of its assets and liabilities (including unrecognized assets and liabilities) following the procedures that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Instead, under the revised guidance, an entity's annual goodwill impairment review should include a "quantitative impairment test" in which it should compare the fair value of a reporting unit with its carrying amount. If the carrying amount exceeds the fair value, then the entity should record an impairment charge for this difference, limited to the total goodwill allocated to the reporting unit (an entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary). The update should be applied on a prospective basis. This guidance is effective for goodwill impairment testing performed in fiscal years beginning after December 15, 2019 bur early adoption was permitted for goodwill impairment tests performed on testing dates after January 1, 2017. The Company elected to early adopt this guidance during the first quarter of 2017. While the guidance changed the Company's goodwill impairment testing procedures, there was no impact on the Company's financial position, results of operations or cash flows.

**Recently Issued Accounting Standards Not Yet Adopted**

*ASU 2016-01 Recognition and Measurement of Financial Assets and Financial Liabilities*

In January 2016, the FASB issued an accounting standards update concerning the accounting for financial instruments. The guidance retains the basic existing framework for accounting for financial instruments under GAAP, while achieving limited convergence with IFRS in this area. The guidance: (1) requires equity investments (except consolidated entities and those accounted for under the equity method of accounting) to be measured at fair value with changes in fair value recognized in net income; (2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (3) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for non-public business entities; (4) eliminates the requirement to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost on the balance sheet; (5) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (6) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial statements; (7) requires separate presentation of financial assets and financial liabilities by measurement category and form of asset in the financial statements; and (8) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to AFS securities in combination with the entity's other deferred tax assets. The guidance will be effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Adoption should be applied by means of a cumulative effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption, except the amendments related to impairment of equity securities without readily determinable fair values. The Company will adopt this guidance as of January 1, 2018. As of that date, accumulated unrealized gains and losses relating to investments in equity securities and certain of our other investments, net of tax, which are included in accumulated other comprehensive income, will be classified to retained earnings. At December 31, 2017 the amount subject to reclassification is a net unrealized gain of $235.2 million, less deferred tax of $12.1 million. Adoption of this update will also have an effect on results of operations going forward, as mark to market movements on equity securities will prospectively impact net income; however, it will not have a material impact on the Company's cash flows

*ASU 2016-02 Leases*

In February 2016, the FASB issued an accounting standards update concerning the accounting for leases. The most significant change to existing GAAP created by this standard will be the lessee recognition of lease assets and lease liabilities for those leases classified as operating. The core principle of this guidance stipulates that a lessee should recognize in the statement of financial position, initially measured at the present value of the lease payments, both a liability for contractual payments due under the lease, and an asset representing its right to use the underlying leased asset for the lease term ("right-of-use asset"). For financing leases, interest on the lease liability should be recognized separately from the amortization of the right-of-use asset in the statement of comprehensive income. Additionally, as regards the presentation of financing lease activities within the statement of cash flows, repayments of the principal portion of the lease liability should be classified within financing activities, while payments of interest on the lease liability should be classified within operating activities. For operating leases, a single net lease cost should be recognized over the lease term, generally on a straight-line basis, and all cash payments related to the lease should be classified within operating activities in the statement of cash flows. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities, and therefore recognize lease expense for such leases on a straight-line basis over the lease term. The guidance will be effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients that entities may elect to apply. An entity that elects to apply the practical expedients will substantively continue to account for leases that commence before the effective date in accordance with existing GAAP, except that a right-of-use asset and a lease liability must be recorded for all operating leases at each reporting date based on the present value of the remaining minimum rental payments that were previously tracked and disclosed. The Company is currently evaluating the impact of this guidance, but expects that it will have an effect on the Company's financial condition as new assets and liabilities related to operating leases are likely to be recorded as a result of adoption. See Note 18(d), "Commitments and Contingencies - Properties," for further information regarding the company's lease commitments. The Company does not expect this new guidance to have a material impact on the Company's results of operations or cash flows.

*ASU 2016-13 Measurement of Credit Loss on Financial Instruments*

In June 2016, the FASB issued an accounting standards update concerning the measurement of credit losses on financial instruments. The amendments in this update affect the measurement of various financial assets, including loans, debt securities, trade receivables, reinsurance receivables and net investments in leases. For assets measured at amortized cost, the amendments in this update require presentation at the net amount expected to be collected. This results in an allowance for all expected credit losses over an asset’s entire life, with no threshold for recognition. This allowance should be maintained in a valuation account that is deducted from the amortized cost of the asset to result in the net amount for presentation purposes. Credit loss allowances for newly created financial assets and subsequent movements in these allowances will be recognized in the income statement, except for the initial credit losses on assets that are purchased in an already credit-impaired state, which will be added to the purchase price of such assets. For AFS debt securities, credit losses should also be recorded through an allowance. The allowance for credit losses is restricted to the difference between the fair value and amortized cost of the relevant asset. The guidance will be effective for fiscal years, and interim periods within those fiscal years beginning after December 15, 2019. Early adoption is permitted for fiscal years, and interim periods within those fiscal years beginning after December 15, 2018. The updates should be adopted in a modified-retrospective approach, by means of a cumulative-effect adjustment to retained earnings at the beginning of the first reporting period in which the guidance is effective. For securities with an existing other-than-temporary impairment or securities previously acquired with deteriorated quality the relevant provisions should be adopted prospectively. The Company is currently evaluating this guidance and expects that it will have an impact on the Company’s financial position and results of operations, but will not have a material impact on the Company’s cash flows.

*ASU 2016-15 Classification of Certain Cash Receipts and Cash Payments*

In August 2016, the FASB issued an accounting standards update concerning the presentation and classification of certain cash receipts and cash payments in the statement of cash flows. The amendments in this update are intended to address areas where GAAP is unclear and diversity in practice exists. The following areas are covered in this update: (1) debt prepayment or debt extinguishment costs; (2) settlement of zero-coupon debt instruments; (3) contingent consideration payments following a business combination; (4) proceeds from settlement of insurance claims; (5) proceeds from settlement of corporate-owned life insurance policies; (6) distributions received from equity method investees; (7) beneficial interests in securitization transactions; and (8) separation of cash flows. The guidance will be effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The amendments should be applied using a retrospective transition method to the periods presented, unless it is impractical to do so. The Company will adopt this guidance as of January 1, 2018. The guidance will not have a material impact on the Company's cash flows, and will have no impact on the Company's financial position or results of operations.

*ASU 2016-16 Income Taxes: Intra-Entity Transfers of Assets Other Than Inventory*

In October 2016, the FASB issued an accounting standards update concerning the tax effects of intra-entity asset transfers within a group. The new guidance requires an entity to reflect the income tax consequences of an intra-entity transfer of an asset other than inventory when that transfer occurs. This is a departure from current GAAP, which prohibits recognition of tax on such transfers until the asset has been sold to an external party or otherwise realized. The amendments are effective for annual reporting periods beginning after December 15, 2017, and interim periods within those fiscal years. The amendments should be applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The Company will adopt this guidance as of January 1, 2018. This guidance will not have a material impact on the Company's financial condition, results of operations, or cash flows.

*ASU 2016-18 Statement of Cash Flows: Restricted Cash*

In November 2016, the FASB issued an accounting standards update concerning the presentation of restricted cash within the statement of cash flows. Existing GAAP does not provide guidance on the presentation or classification of movements in restricted cash. The update requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included as a component of cash and cash equivalents when reconciling beginning-of-period and end-of-period of such totals within the statement of cash flows. The guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The guidance must be applied retrospectively to all periods presented in the statements of cash flows. The Company will adopt this guidance as of January 1, 2018. As result, the net amount of the change in the restricted cash balances during each reporting period will no longer be presented as a discrete line item "Change in restricted cash" within investing cash flows for each applicable period, as is currently reported in the Company's Consolidated Statements of Cash Flows for the years ended December 31, 2017 and 2016 herein. This guidance will not have an impact on the Company's financial position or results of operations.

*ASU 2017-07 Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*

In March 2017, the FASB issued an accounting standards update concerning the presentation of costs related to defined benefit pension plans and similar plans. The amendments in this ASU principally require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by relevant employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. The amendments in the update are effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those annual periods. The amendments in the ASU relating to presentation in the income statement should be applied retrospectively. Disclosures of the nature of and reason for the change in accounting principle are required in the first interim and annual periods of adoption. The Company will adopt this guidance as of January 1, 2018. This guidance is disclosure-related only, and will not have an impact on the Company's financial position, results of operations or cash flows.

*ASU 2017-12 Targeted Improvements to Accounting for Hedging Activities*

In August 2017, the FASB issued an accounting standards update concerning hedge accounting. This update's targeted amendments to existing hedge accounting requirements better align an entity's risk management activities and financial reporting for hedging relationships via updates to both designation and measurement guidance for qualifying hedges, and the presentation of those results. Regarding designation and measurement, the amendments permit broader use of identified risk components in certain cash flow and fair value hedging relationships involving nonfinancial or interest rate risk. The range of permissible fair value hedges of interest rate risk was also increased. Regarding presentation, the amendments aim to align the recognition of the effects of hedging instruments with hedged items in the financial statements in order to increase the understandability of an entity's intended hedging strategies. As a result, "hedge ineffectiveness" will no longer be separately measured and reported. The entire change in the fair value of a qualifying hedging instrument included in the assessment of hedge effectiveness is either presented in the same income statement line as the hedged item for fair value hedges, or in other comprehensive income for cash flow and net investment hedges. However, in limited situations, certain components of a hedging instrument's change in fair value may be excluded from the assessment of hedge effectiveness.

The update also amends existing external disclosure requirements, while easing internal documentation requirements surrounding hedge effectiveness testing. In particular, the initial quantitative effectiveness test may now be prepared within three months of hedge designation, and subsequent tests may be performed on a qualitative basis in certain cases. For public business entities, the amendments in the update are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early application is permitted in any interim period after issuance of the update. All transition requirements should be applied to hedging relationships existing on the date of adoption. The effect of adoption should be reflected as of the beginning of the fiscal year of adoption. The Company is currently evaluating the impact of this guidance.

*ASU 2018-02 Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*

On February 14, 2018, the FASB issued an accounting standards update concerning the stranded tax effects resulting from the U.S. Tax Cuts and Jobs Act. Under existing GAAP, the effects of changes in tax rates on deferred tax balances are reflected in income, even if the balances related to items of accumulated other comprehensive income. This update permits a reclassification from accumulated other comprehensive income to retained earnings for such stranded tax effects resulting from the U.S Tax Cuts and Jobs Act. Certain disclosures about stranded tax effects will also be required. The amendments in the update are effective for all entities for fiscal years beginning after December 2018, and interim periods within those financial years. For public business entities, early adoption is permitted, including adoption in any interim period for reporting periods for which financial statements have not yet been issued. The amendments should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. Tax Cuts and Jobs Act is recognized. The Company is currently evaluating the impact of this guidance.

## 3. Acquisitions, Disposals and Contribution from Parent

### (a) Partial Sale of New Ocean Capital Management Limited

On October 11, 2016, Fundamental Insurance Investment Ltd ("FII"), an indirect wholly-owned subsidiary of the Company, completed a partial sale, to an unrelated investor, of its common and preference shares in New Ocean Capital Management Limited ("New Ocean"), an entity in which it holds a majority voting interest.

FII received $3.9 million in proceeds for the sale of 7.8% of the common shares held by FII and 6.4% of preference shares held by FII. The Company recorded a pre-tax gain of $3.5 million as a result of this transaction.

### (b) Sale of XL Life Insurance and Annuity Company ("XLLIAC")

On September 30, 2016, X.L. America, Inc. ("XL America") and XL Life and Annuity Holding Company ("XLLAHC"), both indirect wholly-owned subsidiaries of the Company, completed the previously announced sale of the Company's wholly-owned subsidiary XLLIAC to Mutual of Omaha Insurance Company.

XL America and XLLAHC received a closing date payment of $20.9 million in proceeds from the transaction, which was based upon the fair market value of XLLIAC's investment assets and insurance licenses. The Company recorded a pre-tax gain of $3.7 million as a result of this transaction.

### (c) Brooklyn Acquisition

On September 30, 2016, the Company's indirect, wholly-owned subsidiary, Catlin Holdings Limited, completed the acquisition ("Brooklyn Acquisition") of Brooklyn Underwriting Pty Limited and Brooklyn IT Pty Limited (collectively "Brooklyn"). Brooklyn is a specialty underwriting agency in Australia and Lloyd's-approved coverholder, serving brokers across Australia. The Company recorded definite-lived intangible assets of $22.9 million, which is being amortized over their estimated useful lives. See Note 9, "Goodwill and Other Intangible Assets," for further information.

### (d) Allied Acquisition

***Overview***

On February 1, 2016, the Company's indirect, wholly-owned subsidiary, XL Reinsurance America Inc. ("XLRA"), completed the acquisition ("Allied Acquisition") of Allied International Holdings, Inc. ("Allied"). Allied is the holding company of Allied Specialty Insurance, Inc. and T.H.E. Insurance Company, an insurer of the outdoor entertainment industry in the U.S.

***Acquisition Consideration***

The Company made an initial payment of $75.7 million to acquire Allied. Additional contingent consideration was to be paid based on production and underwriting profitability over a three-year period subsequent to the acquisition date. The Company originally estimated the fair market value of these payments to be $15.0 million, resulting in total consideration of $90.7 million recorded for the acquisition. Due to an agreement reached on April 11, 2017, the target payments of contingent consideration were modified to range from $12.5 million to $20.0 million. At December 31, 2017, the Company estimates the fair value of these payments to be approximately $17.0 million, resulting in an additional $2.0 million of expense recorded as "Fee income and other" in the Consolidated Statements of Income for the year ended December 31, 2017.

***Fair Value of Net Assets Acquired and Liabilities Assumed***

The purchase price was allocated to the acquired assets and assumed liabilities of Allied based on estimated fair values on the acquisition date. The estimated fair value of the net assets acquired and liabilities assumed was $76.7 million, which includes indefinite-lived intangible assets of $8.0 million and definite-lived intangible assets of $6.0 million, which will be amortized over their estimated useful lives. Other adjustments to the historical carrying value of acquired assets and liabilities included: the estimated fair value of net loss and loss expense reserves at the present value of expected net loss and loss adjustment expense payments plus a risk premium, the estimated value of the business acquired at the present value of expected underwriting profits with net unearned premiums plus a risk margin less policy servicing costs, and the estimated fair value of real estate assets at appraised market values. In conjunction with the transaction, the Company recognized goodwill of $14.1 million, which is primarily attributable to Allied's underwriting expertise in a niche specialty risk business. The Company allocated all of the $14.1 million of goodwill to its Insurance operations. See Note 9, "Goodwill and Other Intangible Assets," for further information.

**(e) Contribution of Catlin**

***Overview***

On May 1, 2015 (the "Acquisition Date"), the Company's intermediate holding company's (“XL-Ireland”) completed its acquisition of the entire issued share capital of Catlin Group Limited (“Catlin”) as contemplated by the Implementation Agreement, dated January 9, 2015 (the "Implementation Agreement"), by and among XL-Ireland, Green Holdings Limited ("Green Holdings"), a wholly-owned subsidiary of XLB and Catlin.

Pursuant to the terms of the Implementation Agreement, the Catlin Acquisition was implemented by way of a scheme of arrangement (the "Scheme") under Section 99 of the Companies Act 1981 of Bermuda, as amended (the "Companies Act"), and sanctioned by the Supreme Court of Bermuda (the "Court"). Immediately after such Court action, Catlin was merged with and into Green Holdings under Section 104H of the Companies Act, with Green Holdings as the surviving company, pursuant to the terms of that certain Merger Agreement, dated January 9, 2015 (the "Merger Agreement"), among XL-Ireland, Green Holdings and Catlin.

Green Holdings (including all associated goodwill and intangible assets) was contributed to the Company on the same date in exchange for $nil. As a transfer of a business under common control the contribution of Green Holdings to the Company has been treated as a deemed capital contribution to the Company.

## 4. Investments

### (a) Fixed Maturities, Short-Term Investments and Equity Securities

*Classification of Fixed Maturity Securities*

In an effort to improve operational efficiency, the Company has undergone an initiative to transform its investment operations and related reporting. As a result of this initiative, the Company has simplified the classification of its fixed maturity securities by investment type to align its internal and external reporting processes. Corporate securities previously separated into two classifications have been merged into one. Residential mortgage-backed securities have also been merged into a single classification. Collateralized debt obligations are now reported under Other asset-backed securities. Comparative period amounts have been re-presented to conform to the new classification system.

*Amortized Cost and Fair Value Summary*

The cost (amortized cost for fixed maturities and short-term investments), fair value, gross unrealized gains and gross unrealized (losses), including non-credit related OTTI recorded in AOCI of the Company's AFS investments at December 31, 2017 and 2016 were as follows:

| | | Included in AOCI | | | |
|---|---|---|---|---|---|
| **December 31, 2017** *(U.S. dollars in thousands)* | **Cost or Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** | **Non-credit Related OTTI (1)** |
| Fixed maturities - AFS - Excluding Life Funds Withheld Assets | | | | | |
| U.S. Government and Government-Related/Supported ("U.S. Government") | $ 4,264,563 | $ 37,244 | $ (33,320) | $ 4,268,486 | $ — |
| U.S. States, municipalities and political subdivisions | 1,977,920 | 87,718 | (998) | 2,064,640 | — |
| Non-U.S. Sovereign Government, Provincial, Supranational and Government-Related/Supported ("Non-U.S. Government") | 5,133,921 | 114,918 | (48,863) | 5,199,976 | — |
| Corporate | 9,502,522 | 203,210 | (56,824) | 9,648,908 | (18) |
| Residential mortgage-backed securities ("RMBS") | 4,464,443 | 40,623 | (33,785) | 4,471,281 | (4,675) |
| Commercial mortgage-backed securities ("CMBS") | 1,245,747 | 7,336 | (9,951) | 1,243,132 | (280) |
| Other asset-backed securities | 1,468,496 | 30,341 | (6,082) | 1,492,755 | (4,940) |
| **Total fixed maturities - AFS - Excluding Life Funds Withheld Assets** | $ 28,057,612 | $ 521,390 | $ (189,823) | $ 28,389,178 | $ (9,913) |
| **Total short-term investments - Excluding Life Funds Withheld Assets** | 801,210 | 718 | (1,901) | 800,027 | — |
| **Total equity securities - Excluding Life Funds Withheld Assets** | 638,455 | 80,679 | (5,167) | 713,967 | — |
| **Total investments - AFS - Excluding Life Funds Withheld Assets** | $ 29,497,277 | $ 602,787 | $ (196,891) | $ 29,903,172 | $ (9,913) |
| Fixed maturities - AFS - Life Funds Withheld Assets | | | | | |
| U.S. Government | $ 9,050 | $ 2,266 | $ — | $ 11,316 | $ — |
| Non-U.S. Governments | 433,664 | 150,870 | — | 584,534 | — |
| Corporate | 909,589 | 227,624 | — | 1,137,213 | — |
| RMBS | 448 | 67 | — | 515 | — |
| CMBS | 97,356 | 24,916 | — | 122,272 | — |
| Other asset-backed securities | 137,944 | 33,318 | — | 171,262 | — |
| **Total fixed maturities - AFS - Life Funds Withheld Assets** | $ 1,588,051 | $ 439,061 | $ — | $ 2,027,112 | $ — |
| **Total fixed maturities - AFS** | $ 31,085,328 | $ 1,041,848 | $ (196,891) | $ 31,930,284 | $ (9,913) |

(1) Represents the non-credit component of OTTI losses, adjusted for subsequent sales of securities. It does not include the change in fair value subsequent to the impairment measurement date.

| **December 31, 2016** *(U.S. dollars in thousands)* | **Cost or Amortized Cost** | **Included in AOCI** Gross Unrealized Gains | Gross Unrealized Losses | **Fair Value** | **Non-credit Related OTTI (1)** |
|---|---|---|---|---|---|
| Fixed maturities - AFS - Excluding Life Funds Withheld Assets | | | | | |
| U.S. Government | $ 3,710,720 | $ 52,331 | $ (32,530) | $ 3,730,521 | $ — |
| U.S. States, municipalities and political subdivisions | 2,399,678 | 85,862 | (7,428) | 2,478,112 | — |
| Non-U.S. Governments | 5,035,890 | 112,760 | (120,119) | 5,028,531 | — |
| Corporate | 9,862,310 | 191,502 | (118,618) | 9,935,194 | (36) |
| RMBS | 4,206,969 | 65,895 | (51,930) | 4,220,934 | (9,990) |
| CMBS | 670,267 | 4,932 | (10,903) | 664,296 | (338) |
| Other asset-backed securities | 1,252,416 | 13,208 | (12,236) | 1,253,388 | (2,029) |
| **Total fixed maturities - AFS - Excluding Life Funds Withheld Assets** | $ 27,138,250 | $ 526,490 | $ (353,764) | $ 27,310,976 | $ (12,393) |
| **Total short-term investments - Excluding Life Funds Withheld Assets** | 626,142 | 228 | (1,176) | 625,194 | — |
| **Total equity securities - Excluding Life Funds Withheld Assets** | 995,934 | 48,931 | (8,210) | 1,036,655 | — |
| **Total investments - AFS - Excluding Life Funds Withheld Assets** | $ 28,760,326 | $ 575,649 | $ (363,150) | $ 28,972,825 | $ (12,393) |
| Fixed maturities - Life Funds Withheld Assets | | | | | |
| U.S. Government | $ 8,468 | $ 2,108 | $ — | $ 10,577 | $ — |
| Non-U.S. Governments | 454,695 | 169,982 | — | 624,677 | — |
| Corporate | 1,173,670 | 280,938 | — | 1,454,608 | — |
| RMBS | 19,591 | 2,789 | — | 22,380 | — |
| CMBS | 77,762 | 16,478 | — | 94,240 | — |
| Other asset-backed securities | 84,541 | 17,019 | — | 101,560 | — |
| **Total fixed maturities - AFS - Life Funds Withheld Assets** | $ 1,818,727 | $ 489,314 | $ — | $ 2,308,042 | $ — |
| **Total investments - AFS** | $ 30,579,053 | $ 1,064,963 | $ (363,150) | $ 31,280,867 | $ (12,393) |

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(1) Represents the non-credit component of OTTI losses, adjusted for subsequent sales of securities. It does not include the change in fair value subsequent to the impairment measurement date.

The cost (amortized cost for fixed maturities and short-term investments) and fair value of the Company's Trading investments at December 31, 2017 and 2016 were as follows:

| **December 31, 2017** *(U.S. dollars in thousands)* | **Amortized Cost** | **Fair Value** |
|---|---|---|
| Fixed maturities - Trading - Life Funds Withheld Assets | | |
| U.S. Government | $ 11,640 | $ 11,042 |
| U.S. States, municipalities and political subdivisions | 30 | 31 |
| Non-U.S. Governments | 473,849 | 485,171 |
| Corporate | 1,412,846 | 1,460,292 |
| RMBS | 1,020 | 932 |
| CMBS | 7,345 | 7,580 |
| Other asset-backed securities | 39,771 | 41,337 |
| **Total fixed maturities - Trading - Life Funds Withheld Assets** | $ 1,946,501 | $ 2,006,385 |
| **Total short-term investments - Trading - Life Funds Withheld Assets** | $ 14,969 | $ 14,965 |
| **Total investments - Trading - Life Funds Withheld Assets** | $ 1,961,470 | $ 2,021,350 |

| **December 31, 2016** *(U.S. dollars in thousands)* | **Amortized Cost** | **Fair Value** |
|---|---|---|
| Fixed maturities - Trading - Life Funds Withheld Assets | | |
| U.S. Government | $ 14,361 | $ 14,708 |
| U.S. States, municipalities and political subdivisions | $ 219 | $ 224 |
| Non-U.S. Governments | 426,225 | 444,944 |
| Corporate | 1,062,853 | 1,111,205 |
| RMBS | 936 | 961 |
| CMBS | 5,242 | 5,526 |
| Other asset-backed securities | 38,342 | 39,446 |
| **Total fixed maturities - Trading - Life Funds Withheld Assets** | 1,548,178 | 1,617,014 |
| **Total short-term investments - Trading - Life Funds Withheld Assets** | 9,536 | 9,563 |
| **Total investments - Trading - Life Funds Withheld Assets** | 1,557,714 | 1,626,577 |

At December 31, 2017 and 2016, approximately 3.4% and 2.6%, respectively, of the Company's fixed income investment portfolio at fair value, excluding cash and Life Funds Withheld Assets, was invested in securities that were below investment grade or not rated. Approximately 4.0% and 2.8% of the gross unrealized losses in the Company's fixed income investment portfolio, excluding cash and Life Funds Withheld Assets, at December 31, 2017 and 2016, respectively, related to securities that were below investment grade or not rated.

*Contractual Maturities Summary*

The contractual maturities of AFS and Trading fixed income securities at December 31, 2017 and 2016 are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | December 31, 2017 | | December 31, 2016 | |
|---|---|---|---|---|
| *(U.S. dollars in thousands)* | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| **Fixed maturities - AFS - Excluding Life Funds Withheld Assets** | | | | |
| Due less than one year | $ 1,495,135 | $ 1,502,699 | $ 2,009,138 | $ 2,022,534 |
| Due after 1 through 5 years | 12,091,740 | 12,157,474 | 12,208,771 | 12,269,393 |
| Due after 5 through 10 years | 6,241,029 | 6,334,149 | 5,451,637 | 5,473,577 |
| Due after 10 years | 1,051,022 | 1,187,688 | 1,339,052 | 1,406,853 |
| | $ 20,878,926 | $ 21,182,010 | $ 21,008,598 | $ 21,172,357 |
| RMBS | $ 4,464,443 | $ 4,471,281 | $ 4,206,969 | $ 4,220,935 |
| CMBS | 1,245,747 | 1,243,132 | 670,267 | 664,296 |
| Other asset-backed securities | 1,468,496 | 1,492,755 | 1,252,416 | 1,253,388 |
| Total mortgage and asset-backed securities | $ 7,178,686 | $ 7,207,168 | $ 6,129,652 | $ 6,138,619 |
| **Total fixed maturities - AFS - Excluding Life Funds Withheld Assets** | $ 28,057,612 | $ 28,389,178 | $ 27,138,250 | $ 27,310,976 |
| **Fixed maturities - AFS - Life Funds Withheld Assets** | | | | |
| Due less than one year | $ 47,143 | $ 49,233 | $ 71,207 | $ 80,749 |
| Due after 1 through 5 years | 286,524 | 313,227 | 289,710 | 318,605 |
| Due after 5 through 10 years | 168,896 | 205,536 | 274,727 | 324,759 |
| Due after 10 years | 849,740 | 1,165,067 | 1,001,189 | 1,365,749 |
| | $ 1,352,303 | $ 1,733,063 | $ 1,636,833 | $ 2,089,862 |
| RMBS | 448 | 515 | 19,591 | 22,380 |
| CMBS | 97,356 | 122,272 | 77,762 | 94,240 |
| Other asset-backed securities | 137,944 | 171,262 | 84,541 | 101,560 |
| Total mortgage and asset-backed securities | 235,748 | 294,049 | 181,894 | 218,180 |
| **Total fixed maturities - AFS - Life Funds Withheld Assets** | $ 1,588,051 | $ 2,027,112 | $ 1,818,727 | $ 2,308,042 |
| **Total fixed maturities - AFS** | $ 29,645,663 | $ 30,416,290 | $ 28,956,977 | $ 29,619,018 |
| **Fixed maturities - Trading - Life Funds Withheld Assets** | | | | |
| Due less than one year | $ 59,962 | $ 59,605 | $ 59,138 | $ 59,553 |
| Due after 1 through 5 years | 486,847 | 492,998 | 322,574 | 328,997 |
| Due after 5 through 10 years | 645,573 | 657,093 | 507,631 | 521,505 |
| Due after 10 years | 705,983 | 746,840 | 614,315 | 661,026 |
| | $ 1,898,365 | $ 1,956,536 | $ 1,503,658 | $ 1,571,081 |
| RMBS | 1,020 | 932 | 936 | 961 |
| CMBS | 7,345 | 7,580 | 5,242 | 5,526 |
| Other asset-backed securities | 39,771 | 41,337 | 38,342 | 39,446 |
| Total mortgage and asset-backed securities | 48,136 | 49,849 | 44,520 | 45,933 |
| **Total fixed maturities - Trading - Life Funds Withheld Assets** | 1,946,501 | 2,006,385 | 1,548,178 | 1,617,014 |

*Pledged Assets*

Certain of the Company's invested assets are pledged in support of insurance and reinsurance liabilities as well as to collateralize XLB's credit facilities. Such pledges are largely required by the Company's operating subsidiaries that are "non-admitted" under U.S. state insurance regulations, in order for the U.S. cedant to receive statutory credit for reinsurance. Also included in pledged assets are Life Funds Withheld Assets. Additionally, certain deposit liabilities and annuity contracts require the use of pledged assets. As of December 31, 2017 and 2016, the Company had $18.7 billion and $17.0 billion in pledged assets, respectively.

### (b) Gross Unrealized Losses

The following is an analysis of how long the AFS securities at December 31, 2017 and 2016 had been in a continual unrealized loss position:

| December 31, 2017 *(U.S. dollars in thousands)* | Less than 12 months | | Equal to or greater than 12 months | |
|---|---|---|---|---|
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| **Fixed maturities and short-term investments - AFS** | | | | |
| U.S. Government | $ 2,636,596 | $ (21,329) | $ 703,645 | $ (13,860) |
| U.S. States, municipalities and political subdivisions | 90,289 | (632) | 19,583 | (366) |
| Non-U.S. Governments | 1,527,323 | (14,959) | 559,044 | (33,931) |
| Corporate | 2,906,666 | (25,541) | 528,952 | (31,284) |
| RMBS | 2,181,376 | (14,432) | 850,234 | (19,354) |
| CMBS | 584,636 | (4,214) | 137,944 | (5,737) |
| Other asset-backed securities | 250,332 | (1,528) | 138,851 | (4,557) |
| **Total fixed maturities and short-term investments - AFS** | $ 10,177,218 | $ (82,635) | $ 2,938,253 | $ (109,089) |
| **Total equity securities** | $ 58,632 | $ (5,167) | $ — | $ — |

| December 31, 2016 *(U.S. dollars in thousands)* | Less than 12 months | | Equal to or greater than 12 months | |
|---|---|---|---|---|
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| **Fixed maturities and short-term investments - AFS** | | | | |
| U.S. Government | $ 2,395,167 | $ (30,348) | $ 43,873 | $ (2,237) |
| U.S. States, municipalities and political subdivisions | 459,407 | (6,991) | 4,287 | (437) |
| Non-U.S.Governments | 1,795,805 | (75,593) | 288,490 | (45,480) |
| Corporate | 3,351,067 | (81,124) | 264,920 | (37,573) |
| RMBS | 2,459,103 | (42,151) | 201,865 | (9,779) |
| CMBS | 469,653 | (9,599) | 9,665 | (1,304) |
| Other asset-backed securities | 777,435 | (3,888) | 37,439 | (8,434) |
| **Total fixed maturities and short-term investments - AFS** | $ 11,707,637 | $ (249,694) | $ 850,539 | $ (105,244) |
| **Total equity securities** | $ 129,810 | $ (8,210) | $ — | $ — |

The Company had gross unrealized losses totaling $196.9 million on 2,900 securities out of a total of 7,735 held at December 31, 2017 in its AFS Excluding Life Funds Withheld Assets portfolio, which either it considers to be temporarily impaired or reflects non-credit losses on other-than-temporarily impaired assets. Individual security positions comprising this balance have been evaluated by management, in conjunction with the Company's investment managers, to determine the severity of these impairments and whether they should be considered other-than-temporary. Management believes it is more likely than not that the issuer will be able to fund sufficient principal and interest payments to support the current amortized cost.

### (c) Net Investment Income

Net investment income for the years ended December 31, 2017 and 2016 is derived from the following sources:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Fixed maturities, short term investments and cash equivalents - Excluding Life Funds Withheld Assets | 722,462 | 697,160 |
| Fixed maturities, short term investments and cash equivalents - Life Funds Withheld Assets | 127,047 | 154,751 |
| Equity securities and other investments | 37,495 | 34,619 |
| Interest on funds withheld | 15,167 | 10,276 |
| Total gross investment income | 902,171 | 896,806 |
| Investment expenses | (86,840) | (85,876) |
| Total net investment income | 815,331 | 810,930 |

**(d) Net Realized and Unrealized Gains (Losses)**

The following represents an analysis of net realized gains (losses), the change in unrealized gains (losses) on trading securities and net realized and unrealized gains (losses) on investment related derivative instruments for the years ended December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Fixed maturities, short term investments, cash and cash equivalents - Excluding Life Funds Withheld Assets: | | |
| Gross realized gains | $ 153,423 | $ 194,708 |
| Gross realized losses on investments sold | (138,129) | (150,794) |
| OTTI on investments, net of amounts transferred to other comprehensive income | (7,579) | (48,432) |
| Net realized gains (losses) | $ 7,715 | $ (4,518) |
| Equity securities: | | |
| Gross realized gains | $ 96,425 | $ 140,864 |
| Gross realized losses on investments sold | (8,081) | (11,882) |
| OTTI on investments, net of amounts transferred to other comprehensive income | (665) | (30,126) |
| Net realized gains (losses) | $ 87,679 | $ 98,856 |
| Other investments: | | |
| Gross realized gains | $ 37,453 | $ 37,253 |
| Gross realized losses on investments sold | (8,305) | (16,376) |
| OTTI on investments, net of amounts transferred to other comprehensive income | (5,101) | — |
| Net realized gains (losses) | $ 24,047 | $ 20,877 |
| **Net realized gains (losses) on investments - Excluding Life Funds Withheld Assets** | **$ 119,441** | **$ 115,215** |
| Fixed maturities, short term investments, cash and cash equivalents - Life Funds Withheld Assets: | | |
| Gross realized gains | $ 120,922 | $ 185,487 |
| Gross realized losses on investments sold | (5,011) | (32,898) |
| Net unrealized gains (losses) on investments, Trading - Life Funds Withheld Assets | (14,805) | 109,458 |
| OTTI on investments, net of amounts transferred to other comprehensive income | (1,434) | (2,598) |
| **Net realized gains (losses) on investments - Life Funds Withheld Assets** | **$ 99,672** | **$ 259,449** |
| **Net realized gains (losses) on investments** | **$ 219,113** | **$ 374,664** |
| Net realized and unrealized gains (losses) on investment related derivative instruments | $ (4,886) | $ 2,521 |
| **Net realized gains (losses) on investments and net realized and unrealized gains (losses) on investment related derivative instruments** | **$ 214,227** | **$ 377,185** |
| Change in unrealized gains (losses): | | |
| Fixed maturities – AFS - Excluding Life Funds Withheld Assets | 158,606 | $ (84,721) |
| Fixed maturities - AFS - Life Funds Withheld Assets | (50,254) | 14,244 |
| Equity securities | 34,791 | (4,119) |
| Other investments | 12,598 | (63,096) |
| Net change in unrealized gains (losses) on investments | $ 155,741 | $ (137,692) |
| **Total net realized gains (losses) on investments, net realized and unrealized gains (losses) on investment related derivative instruments, and net change in unrealized gains (losses) on investments** | **$ 369,968** | **$ 239,493** |

The components of OTTI charges for the years ended December 31, 2017 and 2016, as defined in Note 2(g), "Significant Accounting Policies - Other-Than-Temporary Impairments of Available for Sale," for investments excluding Life Funds Withheld Assets were:

| | Year ended December 31, | |
|---|---|---|
| *(U.S. dollars in thousands)* | **2017** | **2016** |
| Fixed maturities | | |
| Credit loss impairments | $ 573 | $ 14,814 |
| No longer intend to hold to recovery | — | 3,425 |
| Equities and other investments: | | |
| Impaired more than 11 months or more than 50% | 5,766 | 15,277 |
| No longer intend to hold to recovery | — | 14,849 |
| Currency Losses | 7,006 | 30,193 |
| **OTTI on investments, net of amounts transferred to other comprehensive income** | $ 13,345 | $ 78,558 |

The following table sets forth the amount of credit loss impairments on fixed income securities, for which a portion of the OTTI loss was recognized in Other Comprehensive Income ("OCI"), held by the Company at December 31, 2017 and 2016 and the corresponding changes in such amounts.

| **Credit Loss Impairments**<br>*(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Opening balance at beginning of indicated period | $ 29,056 | $ 32,190 |
| Credit loss impairment recognized in the current period on securities not previously impaired | 124 | 12,867 |
| Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period | (9,713) | (15,269) |
| Additional credit loss impairments recognized in the current period on securities previously impaired | 449 | 1,947 |
| Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected | (1,245) | (2,679) |
| Closing balance at end of indicated period | $ 18,671 | $ 29,056 |

## 5. Investments in Affiliates

Investments in affiliates comprised the following at December 31, 2017 and 2016.

| *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Investment affiliates | $ 1,484,408 | $ 1,674,925 |
| Operating affiliates | 427,588 | 502,720 |
| Total investment affiliates | $ 1,911,996 | $ 2,177,645 |

See Note 2(c), "Significant Accounting Policies - Investments - Investments in Affiliates," for a description of the Company's accounting policy for these assets.

### (a) Investment Affiliates

The Company has invested in certain hedge funds, including funds managed by certain of its investment manager affiliates, and in certain private equity investments and private credit funds (collectively, "private investments") that are accounted for under the equity method due to XLB's ownership percentages in the limited partnerships, LLCs or other similar investment vehicles that form the funds. Collectively, these investments in hedge funds and private investments are classified as "investment affiliates." At December 31, 2017 and 2016, the hedge fund portfolio, accounted for as hedge fund affiliates, employed four strategies: arbitrage, directional, event driven and multi-style.

The Company's equity investment in investment affiliates and equity in net income (loss) from such affiliates as well as certain summarized financial information of the investee on a combined basis (shown as "Combined Funds") are included below:

| | XL Bermuda Investment | | | Combined Funds |
|---|---|---|---|---|
| *(U.S. dollars in thousands, except percentages)* | Carrying Value | Equity in Net Income (Loss) for the Year | Weighted Average XL Percentage Ownership | Total Net Assets (Estimated) (1) |
| **Year Ended December 31, 2017** | | | | |
| *Hedge funds (2)* | $ 1,119,747 | $ 104,169 | 4.0% | $ 27,785,552 |
| *Private investments* | 364,661 | 34,877 | 10.2% | 3,657,119 |
| **Total Investment Affiliates** | $ 1,484,408 | $ 139,046 | 5.1% | $ 31,442,671 |
| **Year Ended December 31, 2016** | | | | |
| *Hedge funds (2)* | $ 1,317,375 | $ 41,670 | 4.8% | $ 27,281,980 |
| *Private investments* | 357,550 | 29,088 | 10.8% | 3,318,073 |
| **Total Investment Affiliates** | $ 1,674,925 | $ 70,758 | 5.5% | $ 30,600,053 |

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(1) Total estimated net assets are generally as at November 30 for hedge fund affiliates and September 30 for private investment fund affiliates.
(2) The Company accounts for its investment in certain funds using the equity method where the Company has significant influence over the related investment management company.

In general, the hedge funds in which the Company is invested require at least 30 days notice of redemption, and may be redeemed on a monthly, quarterly, semi-annual, annual or longer basis, depending upon the specific terms of each fund. Certain hedge funds have a lock-up period and/or may also have the ability to impose a redemption gate. A lock-up period refers to the initial amount of time an investor is contractually required to remain invested before having the ability to redeem. Typically, the imposition of a gate delays a portion of the requested redemption, with only the portion that is not gated settled in cash shortly after the redemption date.

The carrying value of the Company's holdings in hedge fund affiliates that are subject to lockups and/or that have redemption gate provisions in their governing documents at December 31, 2017 and 2016 was $222.7 million and $553.2 million, respectively.

Certain hedge funds may be allowed to invest a portion of their assets in illiquid securities, such as private equity or private debt. In such cases, a common mechanism used is a side-pocket, whereby the illiquid security is assigned to a separate memorandum capital account or other designated account. Typically, the investor loses its redemption rights in the designated account. Only when the illiquid securities in the side-pocket are sold, or otherwise deemed liquid by the fund, may investors redeem that portion of their interest that has been "side-pocketed." At December 31, 2017 and 2016, the carrying value of the Company's hedge fund affiliates held in side-pockets was $20.1 million and $23.5 million, respectively. The underlying assets within these positions are generally expected to be liquidated over a period of approximately two to four years.

### (b) Operating Affiliates

The Company has invested in securities or other forms of direct ownership interests across the capital structure of strategic (re)insurance affiliates, investment management company affiliates, and other strategic and operating affiliates. Collectively, these investments are classified as "operating affiliates."

The Company's equity investment in operating affiliates and equity in net income (loss) from such affiliates as well as certain summarized financial information of the investee as a whole are included below:

| | XL Bermuda Investment | | Combined Investee Summarized Financial Data (Estimated) | | | |
|---|---|---|---|---|---|---|
| **Year ended December 31, 2017** *(U.S. dollars in thousands)* | **Carrying Value** | **Equity in Net Income (Loss) for the Year** | **Total Assets** | **Total Liabilities** | **Total Revenue (Loss)** | **Net Income (Loss)** |
| Insurance affiliates | $ 272,801 | $ 1,780 | $ 2,884,286 | $ 2,099,982 | $ 1,228,091 | $ 14,149 |
| Strategic and other operating affiliates | $ 109,382 | $ 21,144 | $ 3,045,335 | $ 2,628,467 | $ 275,677 | $ 11,195 |
| Investment manager affiliates (1) | 45,405 | 40,721 | 412,071 | 49,028 | 65,569 | 29,835 |
| **Total operating affiliates** | $ 427,588 | $ 63,645 | $ 6,341,692 | $ 4,777,477 | $ 1,569,337 | $ 55,179 |
| **Year ended December 31, 2016** | | | | | | |
| Insurance affiliates | 242,844 | 10,558 | 2,350,967 | 1,549,900 | 914,221 | 52,169 |
| Strategic and other operating affiliates | 203,851 | 2,064 | 3,002,938 | 2,241,400 | 116,638 | (21,745) |
| Investment manager affiliates (1) | 56,025 | 31,775 | 752,336 | 72,114 | 337,782 | 257,004 |
| **Total operating affiliates** | $ 502,720 | $ 44,397 | $ 6,106,241 | $ 3,863,414 | $ 1,368,641 | $ 287,428 |

(1) During the years ended December 31, 2017 and 2016, the Company received distributions from its Investment Manager Affiliates of approximately $32.1 million and $35.9 million, respectively.

In certain investments, the carrying value is different from the share of the investee's underlying net assets. The differences represent goodwill on acquisition, OTTI recorded with respect to the investment, or differences in the retained capital accounts of the various equity holders (including the Company).

See Note 18(c), "Commitments and Contingencies – Investments in Affiliates," for further information regarding commitments related to investments in affiliates.

The Company's most significant operating affiliate at December 31, 2017 is an investment of $124.2 million in Privilege Underwriters, Inc. and its affiliates ("PURE Group"), an insurance provider specializing in products for high net worth individuals. The PURE Group investments consist of: (i) a $77.5 million purchase of 9.9% of the ordinary common units and preferred units of Privilege Group Holdings LP, and 9.9% of the units of Privilege Group Holdings GP, LLC; and (ii) a total of $50.0 million of purchases, at par value, of ten year surplus notes issued by Privilege Underwriters Reciprocal Exchange. Under the terms of an agreement between the parties, effective January 18, 2018, the PURE Group has exercised its option to require the Company to purchase a remaining $25.0 million of ten year surplus notes, at par.

At December 31, 2017, the Company's most significant investment manager affiliate is Highfields Capital, a global equity investment firm.

The Company also has an investment of $40.0 million, representing a 20.0% ownership interest in Mahindra Insurance Brokers Limited.

## 6. Other Investments

Other investments comprised the following at December 31, 2017 and 2016. See Note 2(c), "Significant Accounting Policies - Investments - Other Investments," for a description of the Company's accounting policy for these assets:

| **Year ended December 31,** *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Hedge funds | $ 205,770 | $ 331,972 |
| Private investments | 191,986 | 175,562 |
| Overseas deposits | 570,742 | 493,594 |
| Structured transactions | 172,982 | 142,698 |
| Other | 22,383 | 20,721 |
| **Total other investments** | $ 1,163,863 | $ 1,164,547 |

### (a) Hedge Funds and Private Investments

At December 31, 2017 and 2016, the hedge fund portfolio, accounted for as other investments, employed four strategies as noted above in Note 5, "Investments in Affiliates."

In general, the funds in which the Company is invested require at least 30 days notice of redemption, and may be redeemed on a monthly, quarterly, semi-annual, annual or longer basis, depending upon the specific terms of each fund.

Certain hedge funds have a lock-up period and/or may also have the ability to impose a redemption gate as noted in Note 5, "Investments in Affiliates." The fair value of the Company's holdings in hedge funds that are subject to lockups and/or that have redemption gate provisions in their governing documents at December 31, 2017 and 2016 was $178.0 million and $223.3 million, respectively. The Company did not have any holdings in funds where a redemption gate was imposed at December 31, 2017 or 2016.

Certain hedge funds may be allowed to invest a portion of their assets in illiquid securities, such as private equity or private debt, as noted in Note 5, "Investments in Affiliates." At December 31, 2017 and 2016, the fair value of hedge funds held in side-pockets was $9.2 million and $11.3 million, respectively. The underlying assets within these positions are generally expected to be liquidated over a period of approximately two to four years.

The following represents an analysis of the net unrealized gains for the indicated years ended December 31, 2017 and 2016, and the net realized gains as of December 31, 2017 and 2016 on the Company's hedge funds and private investments:

| Year ended December 31, *(U.S. dollars in thousands)* | Net Unrealized Gains (Losses) 2017 | Net Unrealized Gains (Losses) 2016 | Net Realized Gains (Losses) 2017 | Net Realized Gains (Losses) 2016 |
|---|---|---|---|---|
| Hedge funds | $ 100,103 | $ 134,114 | $ 15,322 | $ 12,212 |
| Private investments | 60,624 | 36,775 | 13,994 | 8,636 |
| **Total** | $ 160,727 | $ 170,889 | $ 29,316 | $ 20,848 |

### (b) Overseas Deposits

Overseas deposits include investments in private funds related to Lloyd's syndicates in which the underlying instruments are primarily government and government-related/supported and corporate fixed income securities. The funds themselves do not trade on an exchange and therefore are not included within AFS securities. Also included in overseas deposits are restricted cash and cash equivalent balances held by Lloyd's syndicates for solvency purposes. Given the restricted nature of these cash balances, they are not included within the cash and cash equivalents category in the Consolidated Balance Sheet.

### (c) Structured Transactions

***National Indemnity Endorsement***

On June 9, 2009, XL Specialty Insurance Company ("XL Specialty"), a wholly-owned subsidiary of the Company, entered into an agreement with National Indemnity Company, an insurance company subsidiary of Berkshire Hathaway Inc. ("National Indemnity"). Under the agreement, and a related reinsurance agreement, National Indemnity agreed to issue endorsements to certain directors and officers liability insurance policies known as "Side A" coverage policies underwritten by XL Specialty (the "Facility") during an eighteen month period that ended on December 31, 2011.

In connection with the Facility, XLB purchased a payment obligation (the "Obligation") in an aggregate principal amount of $150.0 million from National Indemnity. At December 31, 2017, the outstanding Obligation was recorded in other investments at a carrying value of $142.8 million, pays a coupon of 3.5%, and is being accreted to $150.0 million over the 11.5 years term of the payment obligation. The difference between the estimated fair value of the Obligation and the cost of that Obligation at the time of the transaction was approximately $21.9 million and was recorded in Other Assets. This difference, together with fees of $2.5 million, was amortized in relation to the earning of the underlying policies written.

## 7. Derivative Instruments

The Company enters into derivative instruments for both risk management and investment purposes. The Company is exposed to potential loss from various market risks, and manages its market risks based on a comprehensive framework of investment decision authorities ("Authorities Framework") by the XLB Board of Directors. The Authorities Framework is intended to align the risk profile of the Company's investment portfolio to be consistent with the Company's risk tolerance, and other guidelines established by the XLB Board of Directors. The following table summarizes information on the notional amounts and gross amounts of derivative fair values contained in the Consolidated Balance Sheets at December 31, 2017 and 2016:

| | 2017 | | | | 2016 | | | |
|---|---|---|---|---|---|---|---|---|
| *(U.S. dollars in thousands)* | **Asset Derivative Notional Amount** | **Asset Derivative Fair Value** | **Liability Derivative Notional Amount** | **Liability Derivative Fair Value** | **Asset Derivative Notional Amount** | **Asset Derivative Fair Value** | **Liability Derivative Notional Amount** | **Liability Derivative Fair Value** |
| Derivatives designated as hedging instruments: | | | | | | | | |
| Foreign currency exposure | $ 580,194 | $ 5,655 | $ 339,221 | $ 3,968 | $ 1,396,801 | $ 85,175 | $ 583,722 | $ 25,750 |
| Total derivatives designated as hedging instruments | $ 580,194 | $ 5,655 | $ 339,221 | $ 3,968 | $ 1,396,801 | $ 85,175 | $ 583,722 | $ 25,750 |
| Derivatives not designated as hedging instruments: | | | | | | | | |
| *Investment Related Derivatives:* | | | | | | | | |
| Interest rate exposure | $ 181,975 | $ 423 | $ — | $ — | $ — | $ — | $ — | $ — |
| Foreign currency exposure | 263,722 | 6,931 | 141,300 | 2,256 | 10,049 | 190 | 273,767 | 12,137 |
| Credit exposure | 5,000 | 187 | 45,000 | 6,784 | 32,500 | 1,077 | 82,500 | 6,978 |
| Financial market exposure | 30,001 | 1,271 | 6,998 | 42 | 5 | 5 | — | — |
| *Other Non-Investment Derivatives:* | | | | | | | | |
| Foreign currency exposure | — | — | — | — | 181,300 | 1,208 | — | — |
| Credit exposure | — | — | 25,526 | 169 | — | — | 24,490 | 340 |
| Guaranteed minimum income benefit contract | 36,171 | 18,136 | 36,171 | 18,136 | 43,553 | 19,499 | 43,553 | 19,499 |
| Modified coinsurance and funds withheld contracts, including life retrocession embedded derivative (1) | 51,653 | — | 5,014,284 | 31,541 | 59,775 | — | 4,048,446 | — |
| Other | $ 16,000 | $ 191 | $ — | $ — | $ 15,000 | $ 342 | $ — | $ — |
| **Total derivatives not designated as hedging instruments** | $ 584,522 | $ 27,139 | $ 5,269,279 | $ 58,928 | $ 342,182 | $ 22,321 | $ 4,472,756 | $ 38,954 |
| Total derivatives | | $ 32,794 | | $ 62,896 | | $ 107,496 | | $ 64,704 |
| Counterparty netting | | (3,579) | | (3,579) | | (17,947) | | (17,947) |
| Total derivatives net of counterparty netting | | 29,215 | | 59,317 | | 89,549 | | 46,757 |
| Cash collateral held/paid (2) | | (3,920) | | (1,312) | | (36,980) | | (5,810) |
| **Total derivatives as recorded in the Consolidated Balance Sheet** | | $ 25,295 | | $ 58,005 | | $ 52,569 | | $ 40,947 |

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(1) The fair value movements in derivative assets and liabilities relating to modified coinsurance and funds withheld contracts are included within the associated asset or liability at each period end on the face of the Consolidated Balance Sheets. Notional amounts associated with reinsurance agreements under which the Company assumes reinsurance risk are recorded as asset derivative notional amounts. Notional amounts associated with the GreyCastle Life Retro Arrangements and other outward reinsurance contracts under which the Company cedes risk are recorded as liability derivative notional amounts. Included in the liability derivative notional amount as of December 31, 2017 is the cumulative net realized and unrealized loss on the life retrocession embedded derivative of $1.1 billion.

(2) At December 31, 2017, the Company held cash collateral related to foreign currency derivative positions and certain other derivative positions of $3.9 million for derivatives in an asset position and paid cash collateral of $1.3 million for derivatives in a liability position. At December 31, 2016, the Company held cash collateral related to a foreign currency derivative position and certain other derivative positions of $37.0 million for derivatives in an asset position and paid cash collateral of $5.8 million for derivatives in a liability position. The assets and liabilities related to the net collateral paid or held were recorded as Other assets and Other liabilities within the Consolidated Balance Sheets as the collateral and derivative positions are not intended to be settled on a net basis.

Derivative instruments in an asset or liability position are included within "Other assets" or "Other liabilities", respectively, at fair value in the Consolidated Balance Sheets on a net basis where the Company has both a legal right of offset and the intention to settle the contracts on a net basis. Certain embedded derivatives within reinsurance contracts are included in "Reinsurance balances payable." The Company often enters into different types of derivative contracts with a single counterparty, and these contracts are covered under netting agreements. Changes in the fair values of derivatives are shown in the Consolidated Statements of Income as "Net realized and unrealized gains (losses) on derivative instruments," unless the derivatives are designated as hedging instruments. The accounting for derivatives that are designated as hedging instruments is described in Note 1(h), "Significant Accounting Policies - Derivative Instruments."

### (a) Derivative Instruments Designated as Hedges of a Net Investment in a Foreign Operation

The Company utilizes foreign currency contracts to hedge the fair value of certain net investments in foreign operations. During the years ended December 31, 2017 and 2016, the Company entered into foreign currency contracts that were formally designated as hedges of investments in foreign subsidiaries, the majority of which have functional currencies of either the British pound or the Euro. There was no ineffectiveness in these transactions.

The following table provides the weighted average U.S. dollar equivalent of foreign denominated net assets that were hedged and the resulting derivative gain (loss) that was recorded in the foreign currency translation adjustment, net of tax, account within AOCI for the years ended December 31, 2017 and 2016.

| **Derivative Instruments Designated as Hedges of a Net Investment in a Foreign Operation – Summary** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Weighted average of U.S. dollar equivalent of foreign denominated net assets | $ 1,361,477 | $ 2,316,538 |
| Derivative gains (losses) (1) | $ (87,954) | $ 130,365 |

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(1) Derivative gains (losses) from derivative instruments designated as hedges of the net investment in a foreign operation are recorded in the cumulative translation adjustment account within AOCI for each period.

### (b) Derivative Instruments Not Formally Designated As Hedging Instruments

The following table provides the total impact on earnings relating to derivative instruments not formally designated as hedging instruments. The impacts are all recorded through "Net realized and unrealized gains (losses) on derivative instruments" in the Consolidated Statements of Income for the years ended December 31, 2017 and 2016:

| **Net Realized and Unrealized Gains (Losses) on Derivative Instruments** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Investment Related Derivatives: | | |
| Interest rate exposure | $ (213) | $ 781 |
| Foreign currency exposure | (4,384) | (592) |
| Credit exposure | (553) | (1,539) |
| Financial market exposure | 264 | (2,494) |
| Other Non-Investment Derivatives: | | |
| Foreign currency exposure | (1,542) | (1,701) |
| Credit exposure | 770 | 4,424 |
| Modified coinsurance and funds withheld contracts, including life retrocession embedded derivative | (34,133) | 3,300 |
| Other | $ (1,941) | |
| Total derivatives not designated as hedging instruments | $ (41,732) | $ 2,521 |
| Amount of gain (loss) recognized in income from ineffective portion of fair value hedges | — | — |
| **Net realized and unrealized gains (losses) on derivative instruments** | $ (41,732) | $ 2,521 |
| **Net realized and unrealized gains (losses on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets** | $ (206,015) | $ (540,090) |

The Company's objectives in using these derivatives are explained below.

### Investment Related Derivatives

The Company, either directly or through third party investment managers, may use derivative instruments within its investment portfolio, including interest rate swaps and options on interest rate swaps, total return swaps, credit derivatives (including single name and index credit default swaps and options on credit default swaps), equity options, forward contracts and futures (including foreign exchange, bond and stock index, interest rate and commodity futures), primarily as a means of reducing investment risk by economically hedging exposures to interest rate, credit spread, equity price changes and foreign currency risk or, in limited instances, for efficient portfolio management. When using exchange traded or cleared over-the-counter derivatives, the Company is exposed to the credit risk of the applicable clearing house and of the Company's futures commission merchant. When using uncleared over-the-counter derivatives, the Company is exposed to credit risk in the event of non-performance by the counterparties to such derivative contracts. To manage this risk, the Company requires appropriate legal documentation with counterparties that has been reviewed and negotiated by legal counsel on behalf of the Company and complies with the Company's documentation standards, investment guidelines and policies.

*Investment Related Derivatives – Interest Rate Exposure*

The Company utilizes risk management and overlay strategies that incorporate the use of derivative financial instruments, primarily to manage its fixed income portfolio duration and net economic exposure to interest rate risks. The Company may also use interest rate swaps to convert certain liabilities from a fixed rate to a variable rate of interest or use them to convert a variable rate of interest from one basis to another.

*Investment Related Derivatives – Foreign Currency Exposure*

The Company has exposure to foreign currency exchange rate fluctuations through its operations and in its investment portfolio. The Company uses foreign currency contracts to manage its exposure to the effects of fluctuating foreign currencies on the value of certain of its foreign currency fixed maturities and equities. These contracts are not designated as specific hedges for financial reporting purposes and, therefore, realized and unrealized gains and losses on these contracts are recorded in income in the period in which they occur. These contracts generally have maturities of twelve months or less.

In addition, certain of the Company's investment managers may, subject to investment guidelines, enter into forward contracts.

*Investment Related Derivatives – Credit Exposure*

Credit derivatives may be purchased within the Company's investment portfolio in the form of single name and basket credit default swaps and swaptions, which are used to mitigate credit exposure through a reduction in credit spread duration (i.e., macro credit strategies rather than single-name credit hedging) or exposure to securities of selected issuers. Credit derivatives may also be used to efficiently gain exposure to credit markets, subject to guidelines that prohibit the introduction of effective leverage.

*Investment Related Derivatives – Financial Market Exposure*

Stock index futures may be purchased within the Company's investment portfolio to create synthetic equity exposure and to add value to the portfolio with overlay strategies where market inefficiencies are believed to exist. Stock index futures may be sold to facilitate the timely and efficient reduction of equity exposure. Equity option strategies, including both purchases and sales of options, may be used to add value or reduce exposure with overlay or other strategies. From time to time, the Company may enter into other financial market exposure derivative contracts on various indices and other underlying financial instruments including, but not limited to, equity options, total return swaps, and commodity contracts.

**Other Non-Investment Derivatives**

*Foreign Currency Contracts*

In the fourth quarter of 2017, the Company entered into an average rate option to mitigate the risk of foreign currency exposure to certain cash flows denominated in the British pound. The option will mature in the fourth quarter of 2018. In the prior year, the Company entered into a similar average rate option.

*Credit Exposure*

During the year ended December 31, 2017, the Company entered into a non-investment-related credit derivative relating to a number of reference pool mortgage tranches associated with actual mortgage loans that were securitized into agency mortgage-backed securities and sold as Structured Agency Credit Risk Notes. At December 31, 2017, there was no reported event of default on this obligation. The credit derivative is recorded at fair value based upon models developed by the Company. Significant unobservable inputs considered in the valuation include the impact of changes in interest rates, future defaults, delinquency and prepayment rates, credit spreads, changes in credit quality, and other market factors.

*Guaranteed Minimum Income Benefit Contract*

The Company has derivatives embedded in certain reinsurance contracts. For a certain life reinsurance contract, the Company pays the ceding company a fixed amount equal to the estimated present value of the excess of the guaranteed benefit over the account balance upon the policyholder's election to take the income benefit. The fair value of this derivative is determined based on the present value of expected cash flows.

*Modified Coinsurance and Funds Withheld Contracts, including Life Retrocession Embedded Derivative*

The Company has modified coinsurance and funds withheld reinsurance agreements that provide for a return to be paid based on a portfolio of fixed income securities. As such, the agreements contain an embedded derivative. The embedded derivative is bifurcated from the funds withheld balance and recorded at fair value, with changes in fair value recognized in earnings through "Net realized and unrealized gains (losses) on derivative instruments."

In addition, the Company entered into the GreyCastle Life Retro Arrangements as described in Note 2(c), "Significant Accounting Policies - Investments - Investments Related to Life Retrocession Arrangements written on a Funds Withheld Basis," and "Note 2(e), "Significant Accounting Policies - Reinsurance." The embedded derivative related to the GreyCastle Life Retro Arrangements is recorded at fair value with changes in fair value recognized in earnings through "Net realized and unrealized gains (losses) on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets."

The impact of the GreyCastle Life Retro Arrangements on the Company's results for the years ended December 31, 2017 and 2016 was as follows:

| **Impact of GreyCastle Life Retro Arrangements** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Underwriting profit (loss) (1) | $ — | $ — |
| Net investment income - Life Funds Withheld Assets | 127,047 | 154,751 |
| Net realized gains (losses) on investments sold - Life Funds Withheld Assets | 115,911 | 152,589 |
| Net unrealized gains (losses) on investments, Trading - Life Funds Withheld Assets | (14,805) | 109,458 |
| OTTI on investments - Life Funds Withheld Assets | (1,434) | (2,598) |
| Foreign exchange (gains) losses | 30,711 | (8,988) |
| Other income and expenses | (108) | (154) |
| Net realized and unrealized gains (losses) on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets | (206,015) | (540,090) |
| **Net income (loss)** | $ 51,307 | $ (135,032) |
| Change in net unrealized gains (losses) on investments - Life Funds Withheld Assets | (51,983) | (4,502) |
| Change in adjustments related to future policy benefit reserves | 27,184 | 62,295 |
| Change in cumulative translation adjustment - Life Funds Withheld Assets | (26,508) | 77,239 |
| **Total changes to other comprehensive income as a result of GreyCastle Life Retro Arrangements** | $ (51,307) | $ 135,032 |
| **Comprehensive income (loss)** | $ — | $ — |

(1) The impact to comprehensive income relating to the GreyCastle Life Retro Arrangements was nil for the years ended December 31, 2017 and 2016.

As shown in the table above, although the Company's net income (loss) is subject to variability related to the GreyCastle Life Retro Arrangements, there is minimal net impact on the Company's comprehensive income in any period. The life retrocession embedded derivative value includes the interest income, unrealized gains and losses, and realized gains and losses from sales of the Life Funds Withheld Assets.

<u>Other</u>

The Company has entered into short term weather derivative swap agreements as the fixed rate payer which provide for a return to be paid to the Company based on the occurrence of certain industry weather events. The derivatives are recorded at fair value with changes in fair value recognized in earnings through "Net realized and unrealized gains (losses) on derivative instruments."

### (c) Derivative Instruments Designated as Fair Value Hedges

The Company may designate certain of its derivative instruments as fair value hedges or cash flow hedges, in which case it formally and contemporaneously documents all relationships between the hedging instruments and hedged items and links the hedging derivative to specific assets and liabilities. The Company assesses the effectiveness of the hedge both at inception and on an on-going basis, and determines whether the hedge is highly effective in offsetting changes in fair value or cash flows of the linked hedged item.

***Settlement of Fair Value Hedges***

During the fourth quarter of 2010 and the third quarter of 2012, the Company settled five interest rate contracts designated as fair value hedges of certain of the Company's structured indemnity contracts. The gain on settlement of these contracts, which represented the effective portion of the hedging relationship, was recorded as an increase in the carrying value of the deposit liabilities and is being amortized through interest expense over the remaining term of the structured indemnity contracts.

A summary of the fair value hedges that have been settled and their impact on results up to the indicated periods, as well as the remaining balance of the fair value hedges and average years remaining to maturity at December 31, 2017 and 2016 are shown below:

| **Settlement of Fair Value Hedges - Summary**<br>*(U.S. dollars in thousands, except years)* | **Fair Value Hedges - Structured Indemnity Contracts December 31, 2017** | **2016** |
|---|---|---|
| Cumulative reduction to interest expense | $ 122,118 | $ 113,292 |
| Remaining balance | $ 111,077 | $ 119,903 |
| Weighted average years remaining to maturity | 18.7 | 20.1 |

### (d) Contingent Credit Features

Certain derivative agreements entered into by the Company or its subsidiaries contain credit rating downgrade provisions that permit early termination of the agreements by the counterparty if collateral is not posted following failure to maintain certain credit ratings from one or more of the principal credit rating agencies. If the Company were required to terminate such agreements early due to a credit rating downgrade, it could potentially be in a net liability position at the time of settlement of such agreements. The aggregate fair value of all derivative agreements containing such rating downgrade provisions that were in a liability position and any collateral posted under these agreements as of December 31, 2017 and 2016 were as follows:

| **Contingent Credit Features - Summary:**<br>*(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Aggregate fair value of derivative agreements with downgrade provisions in a net liability position | $ 7,464 | $ 14,130 |
| Collateral posted to counterparty | $ 40 | $ 4,360 |

## 8. Fair Value Measurements

### (a) Fair Value Summary

The following tables set forth the Company's assets and liabilities that were accounted for at fair value at December 31, 2017 and 2016 by level within the fair value hierarchy. For further information, see Note 2 (b), "Significant Accounting Policies – Fair Value Measurements":

| **December 31, 2017** *(U.S. dollars in thousands)* | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** | **Counterparty Netting** | **Balance at December 31, 2017** |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Fixed maturities - AFS - Excluding Life Funds Withheld Assets | | | | | |
| U.S. Government | $ — | $ 4,250,196 | $ 18,290 | $ — | $ 4,268,486 |
| U.S. States, municipalities and political subdivisions | — | 2,064,640 | — | — | 2,064,640 |
| Non-U.S. Governments | — | 5,199,976 | — | — | 5,199,976 |
| Corporate | — | 9,647,616 | 1,292 | — | 9,648,908 |
| RMBS | — | 4,471,281 | — | — | 4,471,281 |
| CMBS | — | 1,243,132 | — | — | 1,243,132 |
| Other asset-backed securities | — | 1,487,523 | 5,232 | — | 1,492,755 |
| **Total fixed maturities - AFS - Excluding Funds Withheld Assets, at fair value** | $ — | $ 28,364,364 | $ 24,814 | $ — | $ 28,389,178 |
| Short-term investments, at fair value (1) | | 800,027 | — | — | 800,027 |
| Equity securities, at fair value | 557,510 | 156,457 | — | — | 713,967 |
| **Total investments AFS - Excluding Life Funds Withheld Assets** | $ 557,510 | $ 29,320,848 | $ 24,814 | $ — | $ 29,903,172 |
| Fixed maturities - AFS - Life Funds Withheld Assets | | | | | |
| U.S. Government | — | 11,316 | — | — | 11,316 |
| Non-U.S. Governments | — | 584,534 | — | — | 584,534 |
| Corporate | — | 1,137,213 | — | — | 1,137,213 |
| RMBS | — | 515 | — | — | 515 |
| CMBS | — | 122,272 | — | — | 122,272 |
| Other asset-backed securities | — | 171,262 | — | — | 171,262 |
| **Total fixed maturities - AFS - Life Funds Withheld Assets, at fair value** | — | 2,027,112 | — | — | 2,027,112 |
| **Total investments - AFS, at fair value** | 557,510 | 31,347,960 | 24,814 | — | 31,930,284 |
| Fixed Maturities - Trading | | | | | |
| U.S. Government | — | 11,042 | — | — | 11,042 |
| U.S. States, municipalities and political subdivisions | — | 31 | — | — | 31 |
| Non-U.S. Governments | — | 485,171 | — | — | 485,171 |
| Corporate | — | 1,460,292 | — | — | 1,460,292 |
| RMBS | — | 932 | — | — | 932 |
| CMBS | — | 7,580 | — | — | 7,580 |
| Other asset-backed securities | — | 41,337 | — | — | 41,337 |
| **Total fixed maturities - Trading - Life Funds Withheld Assets, at fair value** | — | 2,006,385 | — | — | 2,006,385 |
| Short-term investments, at fair value (1) | — | 14,965 | — | — | 14,965 |
| **Total investments, Trading** | — | 2,021,350 | — | — | 2,021,350 |
| Cash equivalents (2) | 279,224 | 1,218,462 | — | — | 1,497,686 |
| Cash equivalents - Life Funds Withheld Assets (2) | — | 67,982 | — | — | 67,982 |
| Other investments (3) | | 570,931 | 221,708 | | 792,639 |
| Other assets (4) | | 14,467 | 18,327 | (3,579) | 29,215 |
| Total assets accounted for at fair value | $ 836,734 | $ 35,241,152 | $ 264,849 | $ (3,579) | $ 36,339,156 |
| **Liabilities** | | | | | |
| Funds withheld on GreyCastle Life Retro Arrangements (net of future policy benefit reserves recoverable) (5) | $ — | $ 1,112,969 | $ — | $ — | $ 1,112,969 |
| Other liabilities (4) | — | 44,591 | 18,305 | (3,579) | 59,317 |
| **Total liabilities accounted for at fair value** | $ — | $ 1,157,560 | $ 18,305 | $ (3,579) | $ 1,172,286 |

| **December 31, 2016** *(U.S. dollars in thousands)* | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** | **Counterparty Netting** | **Balance at December 31, 2016** |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Fixed maturities - AFS - Excluding Life Funds Withheld Assets | | | | | |
| U.S. Government | $ — | $ 3,705,770 | $ 24,751 | $ — | $ 3,730,521 |
| U.S. States, municipalities and political subdivisions | — | 2,478,112 | — | — | 2,478,112 |
| Non-U.S. Governments | — | 5,028,531 | — | — | 5,028,531 |
| Corporate | — | 9,915,109 | 20,085 | — | 9,935,194 |
| RMBS | — | 4,220,934 | — | — | 4,220,934 |
| CMBS | — | 664,197 | 99 | — | 664,296 |
| Other asset-backed securities | — | 1,252,257 | 1,131 | — | 1,253,388 |
| **Total fixed maturities, - AFS - Excluding Withheld Assets, at fair value** | $ — | $ 27,264,910 | $ 46,066 | $ — | $ 27,310,976 |
| Short-term investments, at fair value (1) | — | 625,194 | — | — | 625,194 |
| Equity securities, at fair value | 897,988 | 138,667 | — | — | 1,036,655 |
| **Total investments AFS - Excluding Funds Withheld Assets** | $ 897,988 | $ 28,028,771 | $ 46,066 | $ — | $ 28,972,825 |
| Fixed maturities - Life Funds Withheld Assets | | | | | |
| U.S. Government | — | $ 10,577 | $ — | $ — | $ 10,577 |
| Non-U.S. Governments | — | 624,677 | — | — | 624,677 |
| Corporate | — | 1,454,608 | — | — | 1,454,608 |
| RMBS | — | 22,380 | — | — | 22,380 |
| CMBS | — | 94,240 | — | — | 94,240 |
| Other asset-backed securities | — | 101,560 | — | — | 101,560 |
| **Total fixed maturities - AFS - Life Funds Withheld Assets, at fair value** | $ — | $ 2,308,042 | $ — | $ — | $ 2,308,042 |
| **Total investments - AFS, at fair value** | $ 897,988 | $ 30,336,813 | $ 46,066 | $ — | $ 31,280,867 |
| Fixed maturities - Trading - Life Funds Withheld Assets, at fair value | | | | | |
| U.S. Government | $ — | $ 14,708 | $ — | $ — | $ 14,708 |
| U.S. States, municipalities and political subdivisions | — | 224 | — | — | 224 |
| Non-U.S. Governments | — | 444,944 | — | — | 444,944 |
| Corporate | — | 1,111,205 | — | — | 1,111,205 |
| RMBS | — | 961 | — | — | 961 |
| CMBS | — | 5,526 | — | — | 5,526 |
| Other asset-backed securities | — | 39,446 | — | — | 39,446 |
| **Total fixed maturities - Trading - Life Funds Withheld Assets, at fair value** | $ — | $ 1,617,014 | $ — | $ — | $ 1,617,014 |
| Short-term investments, at fair value | — | 9,563 | — | — | 9,563 |
| **Total investments, Trading** | $ — | $ 1,626,577 | $ — | $ — | $ 1,626,577 |
| Cash equivalents (2) | 573,398 | 1,080,109 | — | — | 1,653,507 |
| Cash equivalents - Life Funds Withheld Assets (2) | — | 72,798 | — | — | 72,798 |
| Other Investments (3) | — | 493,874 | 205,512 | — | 699,386 |
| Other assets (4) | — | 87,655 | 19,841 | (17,947) | 89,549 |
| Total assets accounted for at fair value | $ 1,471,386 | $ 33,697,826 | $ 271,419 | $ (17,947) | $ 35,422,684 |
| **Liabilities** | | | | | |
| Funds withheld on life retrocession arrangements (net of future policy benefit reserves recoverable) (5) | $ — | $ 937,721 | $ — | $ — | $ 937,721 |
| **Other liabilities (4)** | — | 44,865 | 19,839 | (17,947) | 46,757 |
| Total liabilities accounted for at fair value | $ — | $ 982,586 | $ 19,839 | $ (17,947) | $ 984,478 |

(1) Short-term investments consist primarily of Corporate securities and U.S. and Non-U.S. Government and Government-Related/ Supported securities.
(2) Cash equivalents balances subject to fair value measurement include certificates of deposit and money market funds. Operating cash balances are not subject to recurring fair value measurement guidance.
(3) Excluded from Other Investments are certain investments that are measured using net asset value as a practical expedient in the amount of $198.2 million and $322.9 million as of December 31, 2017 and December 31, 2016, respectively. Under GAAP, these investments are excluded from the fair value hierarchy table. In addition, the Other investments balance excludes loans held at amortized cost, which totaled $173.0 million at December 31, 2017 and $142.3 million at December 31, 2016. For further information, see Note 6, “Other Investments.”
(4) Other assets and other liabilities include derivative instruments. The derivative balances included in each category are reported gross of cash collateral by level with a counterparty netting adjustment presented separately in the Counterparty Netting column. The fair values of the individual derivative contracts are reported gross in their respective levels based on the fair value hierarchy. For further details regarding derivative fair values and associated collateral received or paid, see Note 7, "Derivative Instruments."
(5) Funds withheld on life retrocession arrangements (net of future policy benefit reserves recoverable) include balances related to the life retrocession embedded derivative, under which all investment results associated with the Life Funds Withheld Assets related the GreyCastle Life Retro Arrangements described in Note 1, accrue to the benefit of GCLR.

### (b) Level 2 Asset Valuations

*U.S. Government, Corporate and Non-U.S Governments*

Transaction activity inputs utilized in the valuation of fair value hierarchy Level 2 securities within these sub-categories include actual trades, dealer posts, results of bids-wanted, institutional secondary offerings, primary market offerings and Trade Reporting and Compliance Engine ("TRACE") trade feeds. As part of the evaluation process, transaction activity is compared to prior evaluations and necessary adjustments are made accordingly. Market-color inputs include actively quoted benchmark issues, buy-side/evaluator dialogue, sell-side/evaluator dialogue and credit derivative indices.

*U.S. States, municipalities and political subdivisions*

Transaction activity inputs utilized in the valuation of fair value hierarchy Level 2 securities within this sub-category include actual trades, dealer posts, results of bids-wanted, institutional secondary offerings, primary market offerings, and Municipal Securities Rulemaking trade feeds. As part of the evaluation process, transaction activity is compared to prior evaluations and necessary adjustments are made accordingly. Market-color inputs include bids, offerings, two-sided markets, buy-side/evaluator dialogue and sell-side/evaluator dialogue. Credit information inputs include issuer financial statements, default and material event notices, developer reports and liquidation and restructuring analyses.

*RMBS, CMBS and Other asset-backed securities*

As part of the fair valuation process, Level 2 securities in these sub-categories are analyzed by collateral type, deal structure, deal performance and vintage. Market inputs into the valuation process for each sub-category include reported or observed trades, results of bids-wanted, buy-side/sell-side evaluator dialogue, dealer offering and market research reports. Cash flow inputs into the evaluation process include conditional prepayment rates, conditional decay rates, delinquency and loss severity rates. This assumptive data is reviewed and updated using third party reported information to reflect current market convention

*Equity securities and other investments*

Equity securities and other investment securities generally include investments in thinly traded equity funds and fixed income funds (including Overseas Deposits). Fair value is determined based upon prices received from pricing services as well as from net asset values ("NAV") received from the fund administrators.

*Other assets and other liabilities*

Other assets and other liabilities primarily include over-the-counter ("OTC") derivatives, which are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative independent pricing sources where an understanding of the inputs utilized in arriving at the valuations is obtained. Where models are used, the selection of a particular model to value an OTC derivative depends upon the contractual terms and specific risks inherent in the instrument as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, interest rate swaps and options, model inputs can generally be verified against observable inputs and model selection does not involve significant management judgment.

*Funds withheld on GreyCastle Life Retro Arrangements (net of future policy benefit reserves recoverable)*

The calculation of the change in fair value of the embedded derivative associated with the GreyCastle Life Retro Arrangements includes the interest income, realized and unrealized gains and losses on Life Funds Withheld Assets and certain expenses related to the Life Funds Withheld Assets. The fair value of the embedded derivative is included in "Funds withheld on GreyCastle life retrocession arrangements, net of future policy benefit reserves recoverable" on the Consolidated Balance Sheets. The fair value of the embedded derivative is considered a Level 2 valuation.

There were no significant transfers between Level 1 and Level 2 during each of the years ended December 31, 2017 and 2016.

**(c) Level 3 Assets and Liabilities**

The tables below present additional information about assets and liabilities measured at fair value on a recurring basis and for which Level 3 inputs were utilized to determine fair value. The tables present a reconciliation of the beginning and ending balances for the years ended December 31, 2017 and 2016 for all financial assets and liabilities measured at fair value using significant unobservable inputs (Level 3) at December 31, 2017 and 2016, respectively. The tables do not include gains or losses that were reported in Level 3 in prior periods for assets that were transferred out of Level 3 prior to December 31, 2017 and 2016, respectively. Gains and losses for assets and liabilities classified within Level 3 in the table below may include changes in fair value that are attributable to both observable inputs (Levels 1 and 2) and unobservable inputs (Level 3). Further, it should be noted that the following tables do not take into consideration the effect of offsetting Level 1 and 2 financial instruments entered into by the Company that are either economically hedged by certain exposures to the Level 3 positions or that hedge the exposures in Level 3 positions.

In general, Level 3 assets include securities for which values were obtained from brokers where either significant inputs were utilized in determining the values that were difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification. Transfers into or out of Level 3 primarily arise as a result of the valuations utilized by the Company changing between either those provided by independent pricing services that do not contain significant unobservable inputs and other valuations sourced from brokers that are considered Level 3.

*Fixed maturities and short-term investments*

The Company's Level 3 assets consist primarily of U.S. Government securities, Corporates and Other asset-backed securities, for which non-binding broker quotes are the primary source of the valuations. Sufficient information regarding the specific inputs utilized by the brokers was not available to support a Level 2 classification. The Company obtains the majority of broker quotes for these securities from third party investment managers who perform independent verifications of these valuations using pricing matrices based upon information gathered by market traders. In addition, for the majority of these securities, the Company compares the broker quotes to independent valuations obtained from pricing services, which may also consist of broker quotes, to assess if the prices received represent a reasonable estimate of the fair value. Although the Company does not have access to the specific unobservable inputs that may have been used in the fair value measurements of these securities provided by brokers, we would expect that the significant inputs considered are prepayment rates, probability of default, loss severity in the event of default, recovery rates, liquidity premiums and reinvestment rates. Significant increases (decreases) in any of those inputs in isolation could result in a significantly different fair value measurement. Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

The remainder of the Level 3 assets relate primarily to private investments (including funds) and certain derivative positions as described below.

*Other investments*

Included within the other investments component of the Company's Level 3 valuations are private investments (including funds) and hedge funds where the Company is not deemed to have significant influence over the investee. The fair value of these investments is based upon net asset values received from the investment manager or general partner of the respective entity. The underlying investments held by the investee that form the basis of the net asset value include assets such as private business ventures and are such that significant Level 3 inputs are utilized in the determination of the individual underlying holding values. Accordingly, the fair value of the Company's investment in each entity is classified within Level 3. Management reviews the values and incorporates factors such as the most recent financial information received, annual audited financial statements and the values at which capital transactions with the investee take place when applying judgment regarding whether any adjustments should be made to the net asset value received in recording the fair value of each position. Investments in hedge funds included in other investments utilize strategies including arbitrage, directional, event driven and multi-style. The funds potentially have lockup and gate provisions which may limit redemption liquidity. For further details regarding the nature of other investments and related features, see Note 6, "Other Investments."

*Derivative instruments*

Derivative instruments recorded within other liabilities and classified within Level 3: include credit derivatives sold providing protection on senior tranches of structured finance transactions where the value is obtained directly from the investment bank counterparty and sufficient information regarding the inputs utilized in such valuation was not obtained to support a Level 2 classification and guaranteed minimum income benefits embedded within one reinsurance contract. The majority of inputs utilized in the valuations of these types of derivative contracts are considered Level 1 or Level 2; however, each valuation includes at least one Level 3 input that was significant to the valuation and, accordingly, the values are disclosed within Level 3.

**Level 3 Assets and Liabilities - Year End December 31, 2017**

| *(U.S. dollars in thousands)* | Balance, beginning of period | Realized gains (losses) | Movement in unrealized gains (losses) | Purchases and Issuances | Sales | Settlements | Net transfers into out of) Level 3 (2) | Balance, end of period | Movement in total gains (losses) relating to investments still held |
|---|---|---|---|---|---|---|---|---|---|
| U.S. Government | $ 24,751 | $ (80) | $ (372) | $ — | $ — | $ (1,251) | $ (4,758) | $ 18,290 | $ 37 |
| Corporate | 20,085 | (50) | 57 | — | (20,014) | (31) | 1,245 | 1,292 | (2) |
| RMBS | — | 17 | (526) | — | — | (173) | 682 | — | — |
| CMBS | 99 | 61 | (55) | 698 | — | (105) | (698) | — | — |
| Other asset-backed securities | 1,131 | 101 | 1,114 | 22,472 | (5,216) | (957) | (13,413) | 5,232 | — |
| Short-term investments | — | — | — | 11,693 | (11,662) | (31) | — | — | — |
| Other investments | 205,513 | 14,538 | 23,709 | 32,830 | (2,207) | (42,811) | (9,864) | 221,708 | (189) |
| Derivative Contracts - Net | 2 | — | 20 | — | — | — | — | 22 | 22 |
| Total | $ 251,581 | $ 14,587 | $ 23,947 | $ 67,693 | $ (39,099) | $ (45,359) | $ (26,806) | $ 246,544 | $ (132) |

**Level 3 Assets and Liabilities - Year End December 31, 2016**

| *(U.S. dollars in thousands)* | Balance, beginning of period | Realized gains (losses) | Movement in unrealized gains (losses) | Purchases and Issuances | Sales | Settlements | Net transfers into out of) Level 3 (2) | Balance, end of period | Movement in total gains (losses) relating to investments still held |
|---|---|---|---|---|---|---|---|---|---|
| U.S. Government | $ 45,063 | $ 264 | $ 687 | $ — | $ (19,101) | $ (2,162) | $ — | $ 24,751 | $ 886 |
| Corporate | 53,873 | (2,991) | 23 | 2,032 | (30,420) | (6) | (2,426) | 20,085 | 45 |
| RMBS | 3,077 | (3) | 7 | — | — | (229) | (2,852) | — | — |
| CMBS | — | — | (3) | — | — | — | 102 | 99 | (3) |
| Other asset-backed securities | 50,265 | 668 | 4,757 | 1,072 | — | (37,220) | (18,411) | 1,131 | 4,479 |
| Short-term investments | — | — | — | — | — | — | — | — | — |
| Other investments | 282,666 | 17,814 | (10,496) | 47,998 | (27,676) | (43,259) | (61,535) | 205,512 | 2,454 |
| Derivative Contracts - Net | (9,791) | — | 9,793 | — | — | — | — | 2 | 10 |
| **Total** | $ 425,153 | $ 15,752 | $ 4,768 | $ 51,102 | $ (77,197) | $ (82,876) | $ (85,122) | $ 251,580 | $ 7,871 |

(1) Net transfers include both movement in and movement out of Level 3. Corporate for 2017 includes incoming transfers of $1.4 million partially offset by $0.1 million of outgoing transfers. RMBS for 2017 includes incoming transfers $4.1 million partially offset by $3.4 million of outgoing transfers. Other asset-backed securities for 2017 includes outgoing transfers of $25.4 million partially offset by $12.0 million of incoming transfers. Corporate - Non-Financials securities for 2016 includes $9.7 million of incoming transfers partially offset by $1.9 million outgoing transfers. Other asset-backed securities for 2016 includes $5.0 million of outgoing transfers partially offset by $3.0 million of incoming transfers.

### (d) Financial Instruments Not Carried at Fair Value

Authoritative guidance over disclosures about the fair value of financial instruments requires additional disclosure of fair value information for financial instruments not carried at fair value in both interim and annual reporting periods. Certain financial instruments, particularly insurance contracts, are excluded from these fair value disclosure requirements. The carrying values of cash and cash equivalents, accrued investment income, net receivable from investments sold, other assets, net payable for investments purchased, other liabilities and other financial instruments not included below approximated their fair values. The following table includes financial instruments for which the carrying value differs from the estimated fair values at December 31, 2017 and 2016. All of these fair value estimates are considered Level 2 fair value measurements.

| | 2017 | | 2016 | |
|---|---|---|---|---|
| *(U.S. dollars in thousands)* | **Carrying Value** | **Fair Value** | **Carrying Value** | **Fair Value** |
| Financial Assets - Other investments, structured transactions | 172,982 | 182,222 | 142,271 | 153,173 |
| Deposit liabilities | $ 1,042,677 | $ 1,266,682 | $ 1,116,233 | $ 1,337,406 |
| **Financial Liabilities** | $ 1,042,677 | $ 1,266,682 | $ 1,116,233 | $ 1,337,406 |

The Company historically participated in structured transactions. XLB's remaining structured transaction is largely comprised of an investment in a payment obligation with an insurance company. This transaction is carried at amortized cost. The fair value of this investment held by the Company is determined through use of an internal model utilizing benchmark yields, issuer spreads and reference data.

Deposit liabilities include obligations under structured insurance and reinsurance transactions. For purposes of fair value disclosures, the Company determined the estimated fair value of the deposit liabilities by assuming a discount rate equal to the appropriate U.S. Treasury rate plus 45.5 basis points and 50.0 basis points at December 31, 2017 and 2016, respectively. The discount rate incorporates the Company's own credit risk into the determination of estimated fair value.

The fair values of the Company's notes payable and debt outstanding were determined based on quoted market prices.

There are no significant concentrations of credit risk within the Company's financial instruments not carried at fair value as defined in the authoritative guidance over necessary disclosures, which excludes certain financial instruments, particularly insurance contracts.

## 9. Goodwill and Other Intangible Assets

The following table presents an analysis of goodwill, intangible assets with an indefinite life and intangible assets with a definite life for the years ended December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | **Goodwill** | **Intangible assets with an indefinite life** | **Intangible assets with a definite life** | **Total** |
|---|---|---|---|---|
| Balance at December 31, 2014 | $ 279,623 | $ 15,366 | $ 16,650 | $ 311,639 |
| Additions | 807,381 | 673,000 | 315,000 | 1,795,381 |
| Amortization | — | — | (15,517) | (15,517) |
| Foreign currency translation | (9,686) | (5,507) | (2,356) | (17,549) |
| Balance at December 31, 2015 | $ 1,077,318 | $ 682,859 | $ 313,777 | $ 2,073,954 |
| Additions | 14,084 | 8,000 | 28,948 | 51,032 |
| Amortization | — | — | (22,422) | (22,422) |
| Foreign currency translation | (14,190) | (8,080) | (12,953) | (35,223) |
| Balance at December 31, 2016 | $ 1,077,212 | $ 682,779 | $ 307,350 | $ 2,067,341 |
| Amortization | — | — | (21,834) | (21,834) |
| Foreign currency translation | 20,625 | 16,235 | 7,071 | 43,931 |
| Balance at December 31, 2017 | $ 1,097,837 | $ 699,014 | $ 292,587 | $ 2,089,438 |

*Goodwill*

At December 31, 2017 and 2016, the Company had goodwill of $1,097.8 million and $1,077.2 million, respectively.

In February 2016, as a result of the transaction described in Note 3(d), "Acquisitions, Disposals and Contribution from Parent - Allied Acquisition," the Company recognized goodwill of approximately $14.1 million. The transaction was accounted for using the acquisition method under which the Company recorded the identifiable assets acquired, including indefinite-lived and definite-lived intangible assets, and liabilities assumed, at their acquisition date fair values, and recorded the excess of consideration transferred over the net assets acquired as goodwill.

The estimated fair values of the reporting units' goodwill exceeded their estimated net book values at December 31, 2017, and therefore no impairments were recorded during 2017. At December 31, 2017 and 2016, the ending goodwill balance is comprised of gross goodwill of $1.6 billion, offset by accumulated impairment charges of $0.4 billion at December 31, 2017 and 2016. For further details regarding the Company's impairment process, see Note 2(k), "Significant Accounting Policies - Goodwill, Intangibles and Other Long-Lived Assets."

*Other Intangible Assets*

At December 31, 2017 and 2016, the ending definite-lived intangible assets balance is comprised of $354.2 million and $347.2 million, respectively, of gross intangible assets, offset by accumulated amortization of $61.6 million and $39.8 million, respectively. Future amortization expenses of current intangible assets are as follows and will amortize over a weighted average period of 16.7 years:

| Year Ended December 31,<br>(U.S. dollars in thousands) | | |
|---|---|---|
| 2018 | $ | 20,291 |
| 2019 | | 20,041 |
| 2020 | | 19,957 |
| 2021 | | 19,957 |
| 2022 | | 19,957 |
| 2023-2036 | | 192,384 |
| **Total expected amortization expenses** | $ | 292,587 |

In connection with the transaction described in Note 3(c), "Acquisitions, Disposals and Contribution from Parent - Brooklyn Acquisition," the Company acquired definite-lived intangible assets of $22.9 million, which will be amortized over their estimated useful lives.

In connection with the transaction described in Note 3(d), "Acquisitions, Disposals and Contribution from Parent - Allied Acquisition," the Company acquired indefinite-lived intangible assets of $8.0 million and definite-lived intangible assets of $6.0 million, which will be amortized over their estimated useful lives.

## 10. Losses and Loss Expenses

The following table represents a reconciliation of the beginning and ending balances of unpaid losses and loss expenses, including an analysis of the Company's paid and unpaid losses and loss expenses incurred for the years indicated:

| *(U.S. dollars in thousands)* | | 2017 | | 2016 |
|---|---|---|---|---|
| Unpaid losses and loss expenses at the beginning of the year | $ | 25,939,571 | $ | 25,439,744 |
| Unpaid losses and loss expenses recoverable at the beginning of the year (1) | | 5,480,300 | | 5,248,905 |
| Net unpaid losses and loss expenses at the beginning of the year | $ | 20,459,271 | $ | 20,190,839 |
| Acquired reserves | | — | | 101,315 |
| Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in: | | | | |
| Current year | | 8,149,690 | | 6,374,377 |
| Prior year | | (147,770) | | (301,542) |
| Total net incurred losses and loss expenses | $ | 8,001,920 | $ | 6,072,835 |
| Exchange rate effects | | 460,187 | | (571,198) |
| Less net losses and loss expenses paid in respect of losses occurring in: | | | | |
| Current year | | 2,175,250 | | 1,444,251 |
| Prior year | | 4,288,795 | | 3,890,269 |
| Total net paid losses | $ | 6,464,045 | $ | 5,334,520 |
| Net unpaid losses and loss expenses at the end of the year | | 22,457,333 | | 20,459,271 |
| Unpaid losses and loss expenses recoverable (1) | | 7,239,446 | | 5,480,300 |
| **Unpaid losses and loss expenses at the end of the year** | $ | 29,696,779 | $ | 25,939,571 |

(1) P&C business only, net of provision for uncollectible reinsurance. See note 12, "Reinsurance", for further information.

### (a) Liability for Unpaid Losses and Loss Expenses

As the Company earns premiums for the underwriting risks it assumes, an estimate of the expected ultimate losses related to the premium is established. Loss reserves for unpaid loss and loss expenses are established due to the significant periods of time that may elapse between the occurrence, reporting and settlement of a loss. The process of establishing reserves for unpaid P&C claims can be complex and is subject to considerable variability, as it requires the use of judgment to make informed estimates. These estimates are based on numerous factors, and may be revised as additional experience and other data become available and are reviewed, as new or improved methodologies are developed or as current laws change. Loss reserves include:

- Case reserves - reserves for reported losses and loss expenses that have not yet been settled; and
- IBNR reserves - reserves for incurred but not reported losses or for reported losses over and above the amount of case reserves.

### Case Reserves

Case reserves for the Company's P&C operations are established by management based on amounts reported from insureds or ceding companies and consultation with legal counsel, and represent the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company. The method of establishing case reserves for reported claims differs among the Company's operations.

With respect to the Insurance operations, the Company is notified of insured losses and records a case reserve for the estimated amount of the settlement, if any. The estimate reflects the judgment of claims personnel based on general reserving practices, the experience and knowledge of such personnel regarding the nature of the specific claim and, where appropriate, advice of legal counsel. Reserves are also established to provide for the estimated expense of settling claims, including legal and other fees and the general expenses of administering the claims adjustment process.

With respect to Reinsurance operations, case reserves for reported claims are generally established based on reports received from ceding companies. Additional case reserves may be established by the Company to reflect the estimated ultimate cost of a loss. For reinsurers, uncertainty in the reserving process stems, in part, from timing lags inherent in reporting by the claimant to the primary insurer, and subsequently by the primary insurer to the reinsurer. As a predominantly broker market reinsurer for both excess-of-loss and proportional contracts, the Company is potentially subject to an additional timing lag in the receipt of information, as the primary insurer reports to the broker who in turn reports to the Company.

Since the Company relies on information regarding paid losses, case reserves and IBNR provided by ceding companies to estimate its liability for unpaid losses and loss adjustment expenses ("LAE"), certain procedures are maintained in order to help determine the completeness and accuracy of such information. Periodically, management assesses the reporting activities of its ceding companies on the basis of qualitative and quantitative criteria. In addition to conferring with ceding companies or brokers on claims matters, XLB's claims personnel conduct periodic audits of specific claims and the overall claims procedures of ceding companies at their offices. The Company relies on its ability to effectively monitor the claims handling and claims reserving practices of ceding companies in order to help establish the proper reinsurance premium for reinsurance agreements and to establish proper loss reserves. Disputes with ceding companies have been rare and generally have been resolved through negotiation.

In addition to information received from ceding companies on reported claims, the Company also utilizes information on the pattern of ceding company loss reporting and loss settlements from previous catastrophic events in order to estimate the ultimate liability related to catastrophic events such as hurricanes. Commercial catastrophe model analyses and zonal aggregate exposures are utilized to assess potential client loss before and after an event. Initial cedant loss reports are generally obtained shortly after a catastrophic event, with subsequent updates received as new information becomes available. The Company actively requests loss updates from cedants periodically while there is still considerable uncertainty for an event, often for the first year following an event. The Company's claim settlement processes also incorporate an update to the total loss reserve at the time a claim payment is made to a ceding company.

While the reliance on loss reports from ceding companies may increase the level of uncertainty associated with the estimation of total loss reserves for property catastrophe reinsurance relative to direct property insurance, there are several factors which serve to reduce the uncertainty in loss reserve estimates for property catastrophe reinsurance. First, for large natural catastrophe events, aggregate limits in property catastrophe reinsurance contracts are in some cases fully exhausted by the loss reserve estimates. Second, as a reinsurer, the Company has access to information from a broad cross section of the insurance industry. The Company utilizes such information in order to perform consistency checks on the data provided by ceding companies and is able to identify trends in loss reporting and settlement activity and incorporate such information in the estimate of IBNR reserves. Finally, the Company also supplements the loss information received from cedants with loss estimates developed by market share techniques and/or from third party catastrophe models applied to exposure data supplied by cedants.

**IBNR Reserves**

IBNR reserves represent management's best estimate, at a given point in time, of the amount in excess of case reserves that is needed for the future settlement and loss adjustment costs associated with claims incurred. It is possible that the ultimate liability may differ materially from these estimates. Because the ultimate amount of unpaid losses and LAE is uncertain, management believes that quantitative techniques to estimate these amounts are enhanced by professional and managerial judgment. Management reviews the IBNR estimates produced by its actuarial department and determines its best estimate of the liabilities to record in the financial statements. The Company considers this single point estimate to be the mean expected outcome.

IBNR reserves are estimated by the Company's actuaries using several standard actuarial methodologies including the loss ratio method, the loss development or chain ladder method, the Bornhuetter-Ferguson ("BF") method and frequency and severity approaches. IBNR related to a specific event may be based on the estimated exposure to an industry loss and may include the use of catastrophe modeling software. On a quarterly basis, IBNR reserves are reviewed by the Company's actuaries, and are adjusted as new information becomes available. Any such adjustments are accounted for as changes in estimates and are reflected in the results of operations in the period in which they are made.

The Company's actuaries use one set of assumptions in calculating the single point estimate, which includes actual loss data, loss development factors, loss ratios, reported claim frequency and severity. The actuarial reviews and documentation are completed in accordance with professional actuarial standards with reserves established on a basis consistent with GAAP. The selected assumptions reflect the actuary's judgment based on historical data and experience combined with information concerning current underwriting, economic, judicial, regulatory and other influences on ultimate claim settlements.

When estimating IBNR reserves, each insurance and reinsurance business unit segregates business into exposure classes. Within each class, the business is further segregated by either the year in which the contract incepted ("underwriting year"), the year in which the claim occurred ("accident year"), or the year in which the claim is reported ("report year"). Within the Insurance Operations, reviews are on an accident year, underwriting year, or report year basis depending on the nature of the business. The Reinsurance operations is reviewed on an underwriting year basis. In each case, management believes the selected method represents an appropriate basis for evaluating the reserve associated with each.

Generally, initial actuarial estimates of IBNR reserves not related to a specific event are based on the loss ratio method applied to each class of business. Actual paid losses and case reserves ("reported losses") are subtracted from expected ultimate losses to determine IBNR reserves. Estimates of the initial expected ultimate losses involve management judgment and are based on historical information for that class of business, which includes loss ratios, market conditions, changes in pricing and conditions, underwriting changes, changes in claims emergence, and other factors that may influence expected ultimate losses.

Over time, as greater numbers of claims are reported, actuarial estimates of IBNR are based on the BF method and loss development techniques. The BF method utilizes actual loss data and the expected patterns of loss emergence, combined with an initial expectation of ultimate losses to determine an estimate of ultimate losses. This method may be appropriate when there is limited actual loss data and a relatively less stable pattern of loss emergence. The chain ladder method utilizes actual loss data and expected patterns of loss emergence to determine an estimate of ultimate losses that is independent of the initial expectation of ultimate losses. This method may be appropriate when there is a relatively stable pattern of loss emergence and a relatively larger number of reported claims. Multiple estimates of ultimate losses using a variety of actuarial methods are calculated for each class of business for each year of loss experience. The Company's actuaries look at each class and determine the most appropriate point estimate based on the characteristics of the particular class and other relevant factors, such as historical ultimate loss ratios, the presence of individual large losses, and known occurrences that have not yet resulted in reported losses. Once the actuaries make their determination of the most appropriate point estimate for each class, this information is aggregated and presented to management for review and approval.

The pattern of loss emergence is determined using actuarial analysis and judgment and is based on the historical patterns of the recording of paid and reported losses, as well as industry information. Information that may cause historical patterns to differ from future patterns is considered and reflected in expected patterns as appropriate. For property, marine and aviation insurance, losses are generally reported within 2 to 3 years from the beginning of the accident year. For casualty insurance, loss emergence patterns can vary from 3 years to over 20 years depending on the type of business. For other insurance, loss emergence patterns generally fall within these ranges. For reinsurance business, loss reporting lags the corresponding insurance classes often by at least one quarter due to the need for loss information to flow from the ceding companies generally via reinsurance intermediaries. Such lags in loss reporting are reflected in the actuary's selections of loss reporting patterns used in establishing our reserves.

Such estimates are not precise because, among other things, they are based on predictions of future developments and estimates of future trends in claim severity, claim frequency and other issues. In the process of estimating IBNR reserves, provisions for economic inflation and changes in the social and legal environment are considered, but involve considerable judgment. When estimating IBNR reserves, more judgment is typically required for lines of business with longer loss emergence patterns.

Due to the low frequency and high severity nature of some of the business the Company underwrites, our reserve estimates are highly dependent on actuarial and management judgment and are therefore uncertain. In property classes, there can be additional uncertainty in loss estimation related to large catastrophe events. With wind events, such as hurricanes, the damage assessment process may take more than a year. The cost of claims is subject to volatility due to supply shortages for construction materials and labor. In the case of earthquakes, the damage assessment process may take several years as buildings are discovered to have structural weaknesses not initially detected. The uncertainty inherent in IBNR reserve estimates is particularly pronounced for casualty coverages, such as excess liability, professional liability and workers' compensation, where information emerges relatively slowly over time.

The three types of property and casualty reserve exposures with the longest tails included in the Company's portfolio are:

- high layer excess casualty insurance;
- casualty reinsurance; and
- discontinued asbestos and run-off environmental insurance and reinsurance liabilities.

Certain aspects of casualty operations complicate the actuarial process for establishing reserves. Certain casualty business written by insurance operations is high layer excess casualty business, meaning that liability attaches after large deductibles, including self-insurance or insurance from other sources. The Company began writing this type of business in 1986 and issued policies in forms that were different from traditional policies used by the industry at that time. Initially, there was a lack of industry data available for this type of business. Consequently, the basis for establishing loss reserves for this type of business was largely based upon judgment and the Company's reported loss experience, which was used as a basis for determining ultimate losses and, therefore, IBNR reserves. Over time, the amount of available historical loss experience data has increased. As a result, there is a larger statistical base to assist in establishing reserves for these excess casualty insurance claims.

High layer excess casualty insurance claims typically involve claims relating to (i) a "shock loss" such as an explosion or transportation accident causing severe damage to persons and/or property over a short period of time, (ii) a "non-shock" loss where a large number of claimants are exposed to injurious conditions over a longer period of time, such as exposure to chemicals or pharmaceuticals or (iii) a professional liability loss such as a medical malpractice claim. In each case, these claims are ultimately settled following extensive negotiations and legal proceedings. This process typically takes 5 to 15 years following the date of loss.

Reinsurance operations by their nature add further complications to the reserving process, particularly for the casualty business written, in that there is an inherent lag in the timing and reporting of a loss event from an insured or ceding company to the reinsurer. This reporting lag creates an even longer period of time between the policy inception and when a claim is finally settled. As a result, more judgment is required to establish reserves for ultimate claims in reinsurance operations.

Casualty reinsurance business involves reserving methods that generally include historical aggregated claim information as reported by ceding companies, combined with the results of claims and underwriting reviews of a sample of the ceding company's claims and underwriting files. Therefore, we do not always receive detailed claim information for this line of business.

Discontinued asbestos and run-off environmental liabilities are attached to certain policies previously written by NAC Re Corp. (now known as XL Reinsurance America Inc.), prior to being acquired by the Company; from business of Winterthur purchased by the Company from AXA Insurance in 2001; from a loss portfolio transfer in 2006; and acquired as a result of the Contribution of Catlin. At December 31, 2017, total gross unpaid losses and loss expenses with respect to these businesses represented less than 1% of unpaid losses and loss expenses of the Company.

Unpaid losses and loss expenses prior to reinsurance recoveries for the years ended December 31, 2017 and 2016 comprise the following:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Reserve for reported losses and loss expenses | $ 12,869,644 | $ 10,343,481 |
| Reserve for losses incurred but not reported | 16,827,135 | 15,596,090 |
| **Unpaid losses and loss expenses** | $ 29,696,779 | $ 25,939,571 |

**Claims Development**

Management has determined that the appropriate level of disaggregation for the incurred and paid claims development information best falls into six categories within its two operations. This level of disaggregation is consistent with the Company's historical disclosure levels and provides groupings of the Company's insurance and reinsurance businesses of a credible size and with similar claim development characteristics, particularly payment patterns. It should be noted that when estimating IBNR reserves, the Company's Insurance and Reinsurance operations segregate business into exposure classes and a large number of classes are reviewed in total based on coverage, region and policy and loss emergence characteristics. Furthermore, large losses and catastrophe events are evaluated separately.

As noted previously, reserve reviews are carried out on an accident year, underwriting year or report year basis depending on the nature of the business. Typically, reserve reviews are carried out gross of reinsurance with ceded reinsurance recoveries evaluated separately to arrive at net reserves. However, in accordance with accounting guidance, the disclosures presented herein are accident year triangles, presented net of reinsurance recoverables. Underwriting year triangles are converted to an accident year basis using assumptions consistent with the underlying premium earning profiles and considering large losses in their respective accident year. Similarly, ceded reinsurance recoverables are allocated to accident year and class of business in order to present net accident year triangles. While we have compiled the triangles on a best efforts basis, the allocation bases required to develop historical net accident year triangles should be viewed as approximations only.

Within the Insurance operations, there are four business groups: Property; Specialty; Professional; and Casualty and other. Within the Reinsurance operations, all major products fall within two categories: Property and Other Short-Tail Lines, and Casualty and Other Long-Tail Lines. The Company has also provided aggregate triangles for the total Company and the Insurance and Reinsurance operations to reflect the levels at which the Company manages its business.

The nature of the Company's high excess of loss liability and catastrophe business can result in loss events that are both irregular and significant. Similarly, adjustments to reserves for individual years can be irregular and significant. Such adjustments are part of the normal course of business of the Company. There is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. Furthermore, changes in business mix over time, including discontinuation of certain classes of business and growth in others, can impact development patterns. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on the Company's historical results.

As discussed in further detail in part (c), except for certain workers’ compensation (including long term disability) liabilities and certain bodily injury liability claims, emanating from U.K. exposures, predominantly from the U.K. motor liability portfolio, the Company does not discount its unpaid losses and loss expenses. The development in the tables included herein is presented on a gross of discount basis, reflecting the undiscounted case reserves established using a tabular reserving methodology and the undiscounted IBNR. The amount of discount is then determined for both Case and IBNR reserves and booked accordingly. The amount of discount is included in the reconciliation of the reserves to the Consolidated Balance Sheet.

As a result of the Contribution of Catlin in 2015 as noted in Note 3(e), "Acquisitions, Disposals and Contribution from Parent", the Company acquired approximately $5.4 billion of unpaid claims liability, net of reinsurance, as well as $101.3 million of unpaid claims liability, net of reinsurance due to the Allied Acquisition in 2016. For purposes of this disclosure, the Company has applied the retrospective method for these acquired reserves, including the combined companies' incurred and paid claim development histories throughout the tables. It should be noted that historical reserves for the acquired businesses were established by the respective companies using methods, assumptions and procedures then in effect which may differ from the Company's current reserving bases.

The Company has also revalued all historical data using exchange rates at December 31, 2017 in order to mitigate the effect of foreign exchange on the development throughout the triangles. Due to currency mix changes from one year end to the next, revaluation of incurred losses will result in different year-on-year movements within the triangles with each annual presentation. This approach for handling foreign exchange movements within the triangles differs somewhat from the underlying calculation of prior year development in the Company's financial statements due to the inclusion of historical loss payments as well as reserves and the level of granularity used in the calculation. The differences have been deemed not to be material.

The number of reported claims is provided for the Insurance operations on a per claim basis and excludes those claims which closed with no payment. It should be noted that certain claims may eventually close with no payment in the future at which time the claims will be excluded on a prospective basis. The number of reported claims can vary over time due to changes in mix of business and policy terms and conditions. In the Notes to the 2016 Consolidated Financial Statements, Insurance operations claim counts included nil claims for a portion of the portfolio, and excluded the remainder. In the current year Notes to the Consolidated Financial Statements, the Company has fully aligned the portfolio in this regard; nil claims have been entirely excluded from the claim counts. Had this alignment occurred in the prior year, the reported number of claims in the 2016 Consolidated Financial Statements would have been lower by a range of between 3% and 13% across accident years.For the Reinsurance operations, the number of reported claims is not provided due to the common industry practice of cedants reporting loss information for proportional treaties on a bulk basis without comprehensive claim details. Therefore, it is impractical to provide meaningful claim count detail for the Company's Reinsurance business.

The Average Annual Percentage Payout of Incurred Losses for each age has been derived using a weighted average of all cumulative paid amounts as a percentage of 2017 incurred losses and allocated loss expenses. The average annual percentage payout of incurred losses presented are unaudited and are presented as supplementary information. The average annual percentage payout can change over time due to changes in business mix, policy terms and conditions as well as ceded reinsurance arrangements. As an example, due to a large multi-line quota share contract and multi-year non-standard auto deals written in the more recent years and included within our Reinsurance Casualty and Other Long-Tail portfolio, there is an upward trend in average annual percentage payout observed from last year.

As previously noted, the process of establishing reserves for unpaid P&C claims can be complex and is subject to considerable variability, as it requires the use of judgment to make informed estimates. These estimates are based on numerous factors, and may be revised as additional experience and data become available, as new or improved methodologies are developed or as current laws change. In addition, there is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. This variability may result in either favorable or adverse development in the Incurred Loss and Allocated Loss Expense triangles provided by the Company. The variability experienced to date has been in line with management’s expectations given the underlying business written by the Company. We have provided additional commentary for the individual categories below:

For the Insurance operations in total, while individual accident years have both favorable and adverse incremental development across the triangle, accident years 2008 to 2013 have all developed favorably since the first evaluation. The 2014 to 2016 accident years reflect adverse development due primarily to large loss activity in several lines including professional and casualty.

For the Insurance Property category, individual accident years have generally developed favorably as updated loss estimates were received and volatility in the loss estimates decreased. The 2014 accident year experienced adverse development from the 2014 evaluation to the 2015 evaluation due to development on a large fire loss which occurred in late December 2014. The 2014 accident year then developed favorably from the 2015 evaluation to the 2016 evaluation. The 2015 accident year experienced adverse development from the first evaluation in 2015 to the second evaluation in 2016 due to movements on several claims in the international property and construction businesses.

For the Insurance Specialty category, individual accident years have generally developed favorably, though with decreasing magnitude over time. The adverse experience emerging on the 2016 accident year has been driven by unfavorable attritional and large claims experience in several portfolios. This category includes a range of businesses with both short-tail and medium-tail exposures. Typically, development in the second year relates to short-tail lines with development on medium-tail business being reflected at subsequent evaluations.

For the Insurance Professional category, individual accident years have both favorable and adverse development across the triangle. These developments relate to the complexity associated with claims in this class of business. In 2008, the Company strengthened its reserves for the 2007 report/accident year due to the developing subprime-credit crisis. Due to the claims-made nature of the underlying Professional policies, the subprime-credit crisis impacted the 2008 to 2012 report years and reserves were re-allocated from the 2007 report year to these later years as claims developed. The cumulative impact of the credit crisis and developing loss trends were more severe than originally expected for these years. The 2014-2016 report years have experienced adverse development due to large loss activity in the international financial lines management liability book and the discontinued design subcontractors default portfolio.

For the Insurance Casualty and Other category, individual accident years have both favorable and adverse development across the triangle. These developments relate to the complexity associated with claims in this class of business and the high level of attachment of the Company’s excess policies. The 2010 accident year experienced more adverse development than other accident years due to development on the Deepwater Horizon event. The 2013 to 2015 accident years reflect adverse development due to large loss activity relating to the excess casualty portfolio and strengthening of the excess and surplus portfolio and the newly acquired Allied business. The 2016 accident year shows minimal adverse development during 2017.

For the Reinsurance operations in total, while individual accident years have both favorable and adverse incremental development across the triangle, all accident years except for the 2016 accident year developed favorably since the first evaluation. The modest unfavorable development on the 2016 accident year emanates from the Property and Other Short Tail category as noted below.

For the Reinsurance Property and Other Short Tail category, individual accident years have generally developed favorably as updated loss estimates were received and volatility in the loss estimates decreased. The two outliers were the 2010 and 2012 accident years where there was modest adverse development related to large loss events from the business acquired in the Contribution of Catlin. Specifically, the 2010 adverse development relates to the Buncefield Explosion and the New Zealand Darfield Earthquake offset by more recent favorable developments on other large losses and attritional experience. The 2012 development relates to Costa Concordia and Superstorm Sandy. The favorable development on the 2011 accident year relates in part to reductions on the Japan Earthquake and Tsunami event also within the business acquired in the Contribution of Catlin. As noted earlier, the historical reserves for the acquired businesses were established by the respective companies using methods, assumptions and procedures then in effect which may differ from the Company's current reserving bases. The recent favorable development on 2013 mainly relates to releases on Typhoon Fitow, Central European Floods and favorable attritional experience across all short tailed lines. The unfavorable development on the 2016 accident year relates to deteriorations on the New Zealand Kaikoura Earthquake and Texas Hailstorm events

For the Reinsurance Casualty and Other Long Tail category, the earlier years had modest favorable development and the later years had modest adverse development. The adverse development for the later accident years relates to changes in reserving methodology for certain long tail lines of business that occurred in calendar years 2012 and 2015. In 2012, the Company changed its methodology to hold an explicit discount on loss reserves for U.K. bodily injury claims expected to settle via Periodical Payment Orders ("PPOs"). As these claims became more prevalent and costly, reserves were strengthened on an undiscounted basis. However, with the implementation of discounting, there was a minimal change in the loss reserves, net of the discount. Similarly, a significant portion of the increase in the Incurred Losses and Allocated Loss Expense, Net of Reinsurance for the 2015 calendar year is due to a change in the methodology used to determine the undiscounted ultimate losses for the reinsurance workers' compensation liabilities acquired in the Contribution of Catlin resulting in a large increase in the undiscounted losses but an insignificant change in the discounted losses. The increase in incurred losses and unallocated loss expenses for the 2017 calendar year is driven by the change in the Ogden discount rate (from 2.5% to -0.75%) used by the courts to determine lump sum compensation for claimants in the UK impacting UK motor, Employer's and General Liability classes. This is partially offset by favorable attritional experience on the North America Casualty book.

*Total Property and Casualty*

*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | IBNR (1) | Number of Claims |
| 2008 | $ 5,644,208 | $ 5,735,428 | $ 5,651,657 | $ 5,674,761 | $ 5,631,593 | $ 5,603,554 | $ 5,572,963 | $ 5,510,523 | $ 5,471,441 | $ 5,410,125 | $ 213,925 | N/A |
| 2009 | | 4,763,117 | 4,755,362 | 4,668,243 | 4,689,064 | 4,680,173 | 4,685,356 | 4,555,586 | 4,525,234 | 4,542,173 | 293,117 | N/A |
| 2010 | | | 5,141,028 | 5,272,265 | 5,158,742 | 5,178,036 | 5,127,836 | 5,109,862 | 5,138,545 | 5,053,432 | 300,001 | N/A |
| 2011 | | | | 6,430,567 | 6,392,279 | 6,306,319 | 6,175,271 | 6,311,990 | 6,276,173 | 6,226,953 | 433,196 | N/A |
| 2012 | | | | | 5,869,907 | 5,836,701 | 5,808,941 | 5,930,172 | 5,837,626 | 5,827,240 | 566,059 | N/A |
| 2013 | | | | | | 5,767,068 | 5,777,217 | 5,739,200 | 5,632,776 | 5,526,922 | 652,927 | N/A |
| 2014 | | | | | | | 5,368,693 | 5,549,389 | 5,580,769 | 5,574,378 | 987,715 | N/A |
| 2015 | | | | | | | | 5,540,823 | 5,678,720 | 5,864,953 | 1,405,335 | N/A |
| 2016 | | | | | | | | | 6,182,999 | 6,427,610 | 2,013,460 | N/A |
| 2017 | | | | | | | | | | 8,108,442 | 4,386,436 | N/A |
| | | | | | | | | | | $58,562,228 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| 2008 | $ 810,334 | $ 2,051,520 | $ 2,934,270 | $ 3,539,510 | $ 4,049,900 | $ 4,352,467 | $ 4,568,478 | $ 4,704,623 | $ 4,827,462 | $ 4,897,567 |
| 2009 | | 657,811 | 1,573,893 | 2,254,270 | 2,731,005 | 3,204,371 | 3,460,344 | 3,650,893 | 3,767,363 | 3,844,074 |
| 2010 | | | 873,754 | 1,926,916 | 2,740,308 | 3,252,357 | 3,634,321 | 3,971,942 | 4,212,573 | 4,358,655 |
| 2011 | | | | 1,285,733 | 2,963,941 | 3,778,977 | 4,373,375 | 4,883,707 | 5,175,876 | 5,375,172 |
| 2012 | | | | | 979,204 | 2,317,760 | 3,232,741 | 3,903,535 | 4,312,155 | 4,665,888 |
| 2013 | | | | | | 1,009,683 | 2,285,432 | 3,171,205 | 3,755,115 | 4,207,557 |
| 2014 | | | | | | | 985,112 | 2,322,853 | 3,188,259 | 3,765,670 |
| 2015 | | | | | | | | 997,289 | 2,217,824 | 3,277,189 |
| 2016 | | | | | | | | | 1,233,032 | 2,769,701 |
| 2017 | | | | | | | | | | 1,684,974 |
| | | | | | | | | | | $38,846,447 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 2,451,126 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $22,166,907 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 18% | 23% | 15% | 11% | 8% | 5% | 4% | 2% | 2% | 3% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

*Insurance Operations*

*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 3,980,331 | $ 4,082,887 | $ 4,042,042 | $ 4,083,129 | $ 4,027,990 | $ 4,000,716 | $ 3,970,698 | $ 3,934,337 | $ 3,898,706 | $ 3,859,215 | $ 125,683 | 48.668 |
| **2009** | | 3,566,518 | 3,589,904 | 3,551,370 | 3,579,030 | 3,580,582 | 3,601,916 | 3,469,966 | 3,447,870 | 3,467,258 | 179,179 | 48.912 |
| **2010** | | | 3,806,180 | 3,920,528 | 3,805,979 | 3,842,324 | 3,794,776 | 3,769,113 | 3,807,684 | 3,737,724 | 190,030 | 55.114 |
| **2011** | | | | 4,140,334 | 4,120,075 | 4,139,325 | 4,049,553 | 4,154,898 | 4,127,808 | 4,083,928 | 292,990 | 59.373 |
| **2012** | | | | | 3,991,564 | 3,931,116 | 3,923,936 | 4,055,833 | 3,984,388 | 3,973,579 | 364,324 | 64.064 |
| **2013** | | | | | | 4,072,919 | 4,148,375 | 4,125,518 | 4,064,032 | 3,982,810 | 449,668 | 70.379 |
| **2014** | | | | | | | 3,873,356 | 4,049,578 | 4,111,762 | 4,126,635 | 759,437 | 80.946 |
| **2015** | | | | | | | | 3,975,009 | 4,168,619 | 4,348,859 | 1,058,392 | 94.968 |
| **2016** | | | | | | | | | 4,294,206 | 4,526,453 | 1,459,995 | 102.466 |
| **2017** | | | | | | | | | | 5,068,500 | 2,435,748 | 73.518 |
| | | | | | | | | | | $41,174,961 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 476,792 | $ 1,383,392 | $ 2,032,058 | $ 2,498,765 | $ 2,922,681 | $ 3,156,209 | $ 3,325,230 | $ 3,431,608 | $ 3,512,792 | $ 3,561,228 |
| **2009** | | 477,677 | 1,172,186 | 1,712,626 | 2,101,695 | 2,498,379 | 2,706,905 | 2,864,085 | 2,946,407 | 3,002,238 |
| **2010** | | | 627,377 | 1,423,331 | 2,041,175 | 2,444,498 | 2,764,877 | 3,001,709 | 3,163,363 | 3,273,536 |
| **2011** | | | | 674,219 | 1,675,220 | 2,289,261 | 2,739,159 | 3,159,121 | 3,394,821 | 3,535,878 |
| **2012** | | | | | 658,877 | 1,520,685 | 2,145,780 | 2,660,153 | 2,976,781 | 3,228,221 |
| **2013** | | | | | | 683,757 | 1,567,382 | 2,220,578 | 2,691,262 | 3,039,989 |
| **2014** | | | | | | | 692,365 | 1,650,664 | 2,338,259 | 2,771,499 |
| **2015** | | | | | | | | 715,111 | 1,613,855 | 2,396,659 |
| **2016** | | | | | | | | | 889,975 | 1,923,192 |
| **2017** | | | | | | | | | | 1,076,889 |
| | | | | | | | | | | $27,809,329 |
| | All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | 988,847 |
| | Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | 14,354,479 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 17% | 22% | 16% | 11% | 9% | 6% | 4% | 2% | 2% | 3% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Property**
*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 850,761 | $ 849,039 | $ 815,929 | $ 797,027 | $ 793,740 | $ 786,429 | $ 785,673 | $ 783,904 | $ 782,156 | $ 784,699 | $ 12,884 | 7.86 |
| **2009** | | 409,525 | 384,987 | 368,148 | 360,747 | 354,587 | 354,888 | 352,427 | 350,438 | 356,760 | 5,625 | 6.736 |
| **2010** | | | 614,975 | 629,454 | 600,272 | 582,803 | 576,699 | 584,289 | 581,195 | 581,492 | 8,919 | 7.604 |
| **2011** | | | | 1,015,292 | 950,884 | 927,416 | 892,650 | 882,602 | 875,589 | 871,842 | 71 | 9.239 |
| **2012** | | | | | 706,411 | 680,608 | 655,395 | 656,688 | 648,211 | 645,148 | 6,639 | 10.197 |
| **2013** | | | | | | 766,897 | 748,537 | 725,484 | 718,804 | 716,067 | 10,823 | 11.381 |
| **2014** | | | | | | | 729,439 | 766,516 | 757,109 | 756,646 | 12,039 | 13.954 |
| **2015** | | | | | | | | 822,971 | 846,954 | 839,474 | 38,686 | 16.747 |
| **2016** | | | | | | | | | 989,575 | 1,113,153 | 51,908 | 20.372 |
| **2017** | | | | | | | | | | 1,655,009 | 275,986 | 17.088 |
| | | | | | | | | | | $ 8,320,290 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 156,169 | $ 480,476 | $ 619,072 | $ 673,976 | $ 751,128 | $ 769,740 | $ 772,250 | $ 764,451 | $ 767,073 | $ 768,092 |
| **2009** | | 88,549 | 198,738 | 262,119 | 295,786 | 316,849 | 319,161 | 338,609 | 341,939 | 346,694 |
| **2010** | | | 172,596 | 396,953 | 495,909 | 544,973 | 556,204 | 535,734 | 541,777 | 546,255 |
| **2011** | | | | 222,071 | 637,440 | 777,503 | 819,464 | 849,147 | 850,727 | 858,866 |
| **2012** | | | | | 168,359 | 404,469 | 550,774 | 594,798 | 614,891 | 625,089 |
| **2013** | | | | | | 172,866 | 474,473 | 613,722 | 666,485 | 683,854 |
| **2014** | | | | | | | 186,475 | 523,596 | 674,517 | 708,562 |
| **2015** | | | | | | | | 231,415 | 503,459 | 666,765 |
| **2016** | | | | | | | | | 334,272 | 699,497 |
| **2017** | | | | | | | | | | 500,273 |
| | | | | | | | | | | $ 6,403,947 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 13,430 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 1,929,773 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 27% | 38% | 19% | 7% | 4% | —% | 1% | (1)% | 2% | —% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Specialty**
*(in thousands,except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | IBNR (1) | Number of Claims |
| 2008 | $ 891,890 | $ 968,492 | $ 910,335 | $ 890,963 | $ 876,491 | $ 864,078 | $ 837,617 | $ 856,842 | $ 851,009 | $ 839,244 | $ (2,387) | 19,242 |
| 2009 | | 1,014,909 | 1,008,485 | 936,862 | 909,680 | 897,121 | 887,959 | 831,410 | 822,085 | 821,551 | 1,578 | 18,360 |
| 2010 | | | 1,030,506 | 987,403 | 918,623 | 901,020 | 875,049 | 863,079 | 863,284 | 860,409 | 11,198 | 21,791 |
| 2011 | | | | 999,603 | 1,000,374 | 962,256 | 925,539 | 940,624 | 934,612 | 922,492 | 24,446 | 22,704 |
| 2012 | | | | | 1,039,752 | 986,668 | 946,199 | 936,682 | 920,827 | 907,145 | 7,976 | 25,341 |
| 2013 | | | | | | 969,561 | 1,011,519 | 973,591 | 973,662 | 963,962 | 23,499 | 28,501 |
| 2014 | | | | | | | 972,197 | 988,726 | 971,827 | 962,638 | 28,881 | 35,063 |
| 2015 | | | | | | | | 995,703 | 1,054,941 | 1,054,762 | 76,262 | 43,706 |
| 2016 | | | | | | | | | 1,107,572 | 1,174,955 | 120,726 | 48,416 |
| 2017 | | | | | | | | | | 1,112,192 | 403,497 | 33,402 |
| | | | | | | | | | | $ 9,619,350 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| 2008 | $ 253,344 | $ 529,159 | $ 659,645 | $ 722,183 | $ 765,430 | $ 791,525 | $ 809,870 | $ 817,093 | $ 821,401 | $ 821,249 |
| 2009 | | 321,635 | 568,559 | 680,060 | 733,742 | 758,202 | 776,899 | 787,163 | 790,078 | 796,935 |
| 2010 | | | 327,917 | 566,060 | 680,947 | 736,611 | 780,483 | 798,099 | 807,477 | 816,193 |
| 2011 | | | | 303,685 | 622,701 | 759,238 | 818,112 | 842,024 | 865,691 | 873,203 |
| 2012 | | | | | 323,488 | 610,222 | 722,133 | 793,659 | 830,272 | 848,480 |
| 2013 | | | | | | 343,578 | 617,540 | 741,972 | 818,201 | 859,290 |
| 2014 | | | | | | | 348,944 | 635,917 | 768,421 | 831,653 |
| 2015 | | | | | | | | 346,794 | 675,618 | 828,146 |
| 2016 | | | | | | | | | 424,069 | 800,160 |
| 2.017 | | | | | | | | | | 433,901 |
| | | | | | | | | | | $ 7,909,210 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 132,594 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 1,842,734 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 36% | 31% | 14% | 7% | 4% | 3% | 1% | 1% | 1% | —% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Professional**
*(in thousands, except for number of claims)*

| Incurred Losses and Allocated Loss Expenses, Net of Reinsurance | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2016 | |
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | IBNR (1) | Number of Claims |
| 2007 | $ 1,047,124 | $ 1,101,965 | $ 1,147,534 | $ 1,239,730 | $ 1,218,280 | $ 1,198,484 | $ 1,194,919 | $1,162,130 | $ 1,140,790 | $ 1,131,120 | $ 26,453 | 4,165 |
| 2008 | | 981,970 | 1,050,410 | 1,112,512 | 1,180,339 | 1,219,714 | 1,229,584 | 1,196,459 | 1,192,299 | 1,199,359 | 68,143 | 4,851 |
| 2009 | | | 1,006,646 | 1,003,305 | 975,366 | 1,053,660 | 1,013,567 | 1,035,210 | 1,081,736 | 1,053,011 | 56,712 | 4,517 |
| 2010 | | | | 987,023 | 978,863 | 1,035,722 | 1,050,516 | 1,123,136 | 1,133,524 | 1,130,481 | 141,147 | 4,203 |
| 2011 | | | | | 995,783 | 997,484 | 1,033,040 | 1,148,277 | 1,142,555 | 1,155,566 | 174,871 | 4,295 |
| 2012 | | | | | | 984,798 | 982,485 | 960,557 | 938,328 | 863,145 | 159,645 | 4,503 |
| 2013 | | | | | | | 762,491 | 815,411 | 857,762 | 883,975 | 272,364 | 4,602 |
| 2014 | | | | | | | | 772,779 | 816,200 | 935,466 | 372,222 | 5,120 |
| 2015 | | | | | | | | | 750,041 | 772,377 | 477,454 | 4,490 |
| 2016 | | | | | | | | | | 854,050 | 727,596 | 2,530 |
| | | | | | | | | | | $ 9,978,550 | Total | |

| Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | For the Years Ended December 31, | | | | | | | | | |
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| Accident Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| 2008 | $ 18,371 | $ 186,817 | $ 350,967 | $ 522,556 | $ 706,956 | $ 793,754 | $ 865,795 | $ 924,630 | $ 986,705 | $ 996,837 |
| 2009 | | 22,596 | 162,488 | 341,997 | 516,995 | 758,394 | 852,865 | 937,925 | 965,159 | 982,106 |
| 2010 | | | 22,132 | 157,847 | 330,563 | 487,964 | 632,809 | 746,509 | 816,307 | 851,235 |
| 2011 | | | | 29,116 | 146,330 | 319,404 | 486,621 | 691,769 | 827,268 | 890,169 |
| 2012 | | | | | 44,763 | 197,103 | 382,218 | 599,630 | 723,313 | 839,544 |
| 2013 | | | | | | 36,847 | 154,971 | 309,475 | 465,463 | 587,897 |
| 2014 | | | | | | | 17,185 | 140,718 | 315,969 | 453,178 |
| 2015 | | | | | | | | 22,667 | 140,307 | 319,050 |
| 2016 | | | | | | | | | 23,688 | 141,813 |
| 2017 | | | | | | | | | | 21,074 |
| | | | | | | | | | | $ 6,082,903 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 160,193 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 4,055,840 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 3% | 13% | 16% | 16% | 15% | 9% | 6% | 3% | 3% | 4% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Casualty and other**
*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 1,190,556 | $ 1,163,391 | $ 1,168,244 | $ 1,155,409 | $ 1,139,479 | $ 1,151,725 | $ 1,152,489 | $ 1,131,461 | $ 1,124,751 | $ 1,104,152 | $ 88,733 | 17,401 |
| **2009** | | 1,160,114 | 1,146,022 | 1,133,848 | 1,128,264 | 1,109,160 | 1,129,485 | 1,089,670 | 1,083,048 | 1,089,588 | 103,833 | 18,965 |
| **2010** | | | 1,154,053 | 1,300,366 | 1,311,718 | 1,304,841 | 1,329,461 | 1,286,535 | 1,281,469 | 1,242,812 | 113,201 | 21,202 |
| **2011** | | | | 1,138,416 | 1,189,954 | 1,213,931 | 1,180,848 | 1,208,536 | 1,184,083 | 1,159,113 | 127,326 | 23,227 |
| **2012** | | | | | 1,249,618 | 1,266,356 | 1,289,302 | 1,314,186 | 1,272,795 | 1,265,720 | 174,838 | 24,231 |
| **2013** | | | | | | 1,351,663 | 1,405,834 | 1,465,886 | 1,433,238 | 1,439,636 | 255,701 | 25,994 |
| **2014** | | | | | | | 1,409,229 | 1,478,925 | 1,525,064 | 1,523,376 | 446,153 | 27,327 |
| **2015** | | | | | | | | 1,383,556 | 1,450,524 | 1,519,157 | 571,222 | 29,395 |
| **2016** | | | | | | | | | 1,447,018 | 1,465,968 | 809,907 | 29,188 |
| **2017** | | | | | | | | | | 1,447,249 | 1,028,669 | 20,498 |
| | | | | | | | | | | $13,256,771 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 48,908 | $ 186,940 | $ 402,374 | $ 580,050 | $ 699,167 | $ 801,190 | $ 877,315 | $ 925,434 | $ 937,613 | $ 975,050 |
| **2009** | | 44,897 | 242,401 | 428,450 | 555,172 | 664,934 | 757,980 | 800,388 | 849,231 | 876,503 |
| **2010** | | | 104,732 | 302,471 | 533,756 | 674,950 | 795,381 | 921,367 | 997,802 | 1,059,853 |
| **2011** | | | | 119,347 | 268,749 | 433,116 | 614,962 | 776,181 | 851,135 | 913,640 |
| **2012** | | | | | 122,267 | 308,891 | 490,655 | 672,066 | 808,305 | 915,108 |
| **2013** | | | | | | 130,466 | 320,398 | 555,409 | 741,113 | 908,948 |
| **2014** | | | | | | | 139,761 | 350,433 | 579,352 | 778,106 |
| **2015** | | | | | | | | 114,235 | 294,471 | 582,698 |
| **2016** | | | | | | | | | 107,946 | 281,722 |
| **2.017** | | | | | | | | | | 121,641 |
| | | | | | | | | | | $ 7,413,269 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 682,630 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 6,526,132 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 8% | 14% | 17% | 14% | 11% | 9% | 6% | 4% | —% | 6% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

*Reinsurance Operations*

*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 1,663,877 | $ 1,652,541 | $ 1,609,615 | $ 1,591,632 | $ 1,603,603 | $ 1,602,838 | $ 1,602,265 | $ 1,576,186 | $ 1,572,735 | $ 1,550,910 | $ 88,242 | N/A |
| **2009** | | 1,196,599 | 1,165,458 | 1,116,873 | 1,110,034 | 1,099,591 | 1,083,440 | 1,085,620 | 1,077,364 | 1,074,915 | 113,938 | N/A |
| **2010** | | | 1,334,848 | 1,351,737 | 1,352,763 | 1,335,712 | 1,333,060 | 1,340,749 | 1,330,861 | 1,315,708 | 109,971 | N/A |
| **2011** | | | | 2,290,233 | 2,272,204 | 2,166,994 | 2,125,718 | 2,157,092 | 2,148,365 | 2,143,025 | 140,206 | N/A |
| **2012** | | | | | 1,878,343 | 1,905,585 | 1,885,005 | 1,874,339 | 1,853,238 | 1,853,661 | 201,735 | N/A |
| **2013** | | | | | | 1,694,149 | 1,628,842 | 1,613,682 | 1,568,744 | 1,544,112 | 203,259 | N/A |
| **2014** | | | | | | | 1,495,337 | 1,499,811 | 1,469,007 | 1,447,743 | 228,278 | N/A |
| **2015** | | | | | | | | 1,565,814 | 1,510,101 | 1,516,094 | 346,943 | N/A |
| **2016** | | | | | | | | | 1,888,793 | 1,901,157 | 553,465 | N/A |
| **2017** | | | | | | | | | | 3,039,942 | 1,950,688 | N/A |
| | | | | | | | | | | $17,387,267 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 333,542 | $ 668,128 | $ 902,212 | $ 1,040,745 | $ 1,127,219 | $ 1,196,258 | $ 1,243,248 | $ 1,273,015 | $ 1,314,670 | $ 1,336,339 |
| **2009** | | 180,134 | 401,707 | 541,644 | 629,310 | 705,992 | 753,439 | 786,808 | 820,956 | 841,836 |
| **2010** | | | 246,377 | 503,585 | 699,133 | 807,859 | 869,444 | 970,233 | 1,049,210 | 1,085,119 |
| **2011** | | | | 611,514 | 1,288,721 | 1,489,716 | 1,634,216 | 1,724,586 | 1,781,055 | 1,839,294 |
| **2012** | | | | | 320,327 | 797,075 | 1,086,961 | 1,243,382 | 1,335,374 | 1,437,667 |
| **2013** | | | | | | 325,926 | 718,050 | 950,627 | 1,063,853 | 1,167,568 |
| **2014** | | | | | | | 292,747 | 672,189 | 850,000 | 994,171 |
| **2015** | | | | | | | | 282,178 | 603,969 | 880,530 |
| **2016** | | | | | | | | | 343,057 | 846,509 |
| **2.017** | | | | | | | | | | 608,085 |
| | | | | | | | | | | $11,037,118 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 1,462,279 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 7,812,428 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 20% | 25% | 14% | 8% | 5% | 4% | 4% | —% | 1% | 4% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Property and Other Short-tail Lines**
*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | **For the Years Ended December 31,** | | | | | | | | | | **As of Dec 31, 2017** | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 944,428 | $ 927,527 | $ 906,400 | $ 883,361 | $ 867,449 | $ 863,157 | $ 867,653 | $ 860,502 | $ 867,774 | $ 843,257 | $ 383 | N/A |
| **2009** | | 595,960 | 555,200 | 518,460 | 499,580 | 489,873 | 485,983 | 479,643 | 484,055 | 476,171 | 172 | N/A |
| **2010** | | | 856,962 | 875,225 | 881,152 | 883,526 | 890,473 | 871,329 | 873,474 | 853,011 | (13) | N/A |
| **2011** | | | | 1,778,947 | 1,749,879 | 1,665,442 | 1,639,503 | 1,644,225 | 1,636,012 | 1,628,065 | 36,404 | N/A |
| **2012** | | | | | 1,293,247 | 1,315,130 | 1,305,260 | 1,274,482 | 1,263,237 | 1,264,859 | 65,579 | N/A |
| **2013** | | | | | | 1,119,339 | 1,065,389 | 1,022,634 | 985,614 | 952,356 | 10,501 | N/A |
| **2014** | | | | | | | 899,370 | 877,472 | 836,156 | 809,032 | 18,848 | N/A |
| **2015** | | | | | | | | 912,777 | 855,184 | 864,595 | 111,925 | N/A |
| **2016** | | | | | | | | | 1,168,219 | 1,183,480 | 184,699 | N/A |
| **2017** | | | | | | | | | | 1,970,911 | 1,142,221 | N/A |
| | | | | | | | | | | $10,845,737 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | **Unaudited** | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 296,808 | $ 549,370 | $ 702,796 | $ 767,424 | $ 794,530 | $ 811,850 | $ 816,846 | $ 814,278 | $ 827,401 | $ 830,128 |
| **2009** | | 147,904 | 315,599 | 400,250 | 432,286 | 452,112 | 456,855 | 456,520 | 464,315 | 466,604 |
| **2010** | | | 229,065 | 453,814 | 605,997 | 669,277 | 694,525 | 762,176 | 814,534 | 831,559 |
| **2011** | | | | 595,601 | 1,228,014 | 1,382,680 | 1,473,573 | 1,515,800 | 1,537,012 | 1,560,091 |
| **2012** | | | | | 294,986 | 723,095 | 946,583 | 1,043,324 | 1,084,530 | 1,130,777 |
| **2013** | | | | | | 297,848 | 633,594 | 805,866 | 859,679 | 909,414 |
| **2014** | | | | | | | 254,289 | 571,832 | 676,511 | 740,624 |
| **2015** | | | | | | | | 238,030 | 483,754 | 656,520 |
| **2016** | | | | | | | | | 275,958 | 679,948 |
| **2.017** | | | | | | | | | | 468,988 |
| | | | | | | | | | | $ 8,274,653 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 209,170 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 2,780,254 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| **Year 1** | **Year 2** | **Year 3** | **Year 4** | **Year 5** | **Year 6** | **Year 7** | **Year 8** | **Year 9** | **Year 10** |
|---|---|---|---|---|---|---|---|---|---|
| 29% | 35% | 17% | 7% | 3% | 2% | 3% | 1% | 1% | —% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

**Casualty and Other Long-Tail Lines**
*(in thousands, except for number of claims)*

**Incurred Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | | As of Dec 31, 2017 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | | | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **IBNR (1)** | **Number of Claims** |
| **2008** | $ 719,449 | $ 725,014 | $ 703,215 | $ 708,271 | $ 736,154 | $ 739,681 | $ 734,612 | $ 715,684 | $ 704,961 | $ 707,653 | $ 87,859 | N/A |
| **2009** | | 600,639 | 610,258 | 598,413 | 610,454 | 609,718 | 597,457 | 605,977 | 593,309 | 598,744 | 113,766 | N/A |
| **2010** | | | 477,886 | 476,512 | 471,611 | 452,186 | 442,587 | 469,420 | 457,387 | 462,697 | 109,984 | N/A |
| **2011** | | | | 511,286 | 522,325 | 501,552 | 486,215 | 512,867 | 512,353 | 514,960 | 103,802 | N/A |
| **2012** | | | | | 585,096 | 590,455 | 579,745 | 599,857 | 590,001 | 588,802 | 136,156 | N/A |
| **2013** | | | | | | 574,810 | 563,453 | 591,048 | 583,130 | 591,756 | 192,758 | N/A |
| **2014** | | | | | | | 595,967 | 622,339 | 632,851 | 638,711 | 209,430 | N/A |
| **2015** | | | | | | | | 653,037 | 654,917 | 651,499 | 235,018 | N/A |
| **2016** | | | | | | | | | 720,574 | 717,677 | 368,766 | N/A |
| **2017** | | | | | | | | | | 1,069,031 | 808,467 | N/A |
| | | | | | | | | | | $ 6,541,530 | Total | |

**Cumulative Paid Losses and Allocated Loss Expenses, Net of Reinsurance**

| | For the Years Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | Unaudited | |
| **Accident Year** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** |
| **2008** | $ 36,734 | $ 118,758 | $ 199,416 | $ 273,321 | $ 332,689 | $ 384,408 | $ 426,402 | $ 458,737 | $ 487,269 | $ 506,211 |
| **2009** | | 32,230 | 86,108 | 141,394 | 197,024 | 253,880 | 296,584 | 330,288 | 356,641 | 375,232 |
| **2010** | | | 17,312 | 49,771 | 93,136 | 138,582 | 174,919 | 208,057 | 234,676 | 253,560 |
| **2011** | | | | 15,913 | 60,707 | 107,036 | 160,643 | 208,786 | 244,043 | 279,203 |
| **2012** | | | | | 25,341 | 73,980 | 140,378 | 200,058 | 250,844 | 306,890 |
| **2013** | | | | | | 28,078 | 84,456 | 144,761 | 204,174 | 258,154 |
| **2014** | | | | | | | 38,458 | 100,357 | 173,489 | 253,547 |
| **2015** | | | | | | | | 44,148 | 120,215 | 224,010 |
| **2016** | | | | | | | | | 67,099 | 166,561 |
| **2017** | | | | | | | | | | 139,097 |
| | | | | | | | | | | $ 2,762,465 |
| All outstanding liabilities prior to 2008, net of reinsurance | | | | | | | | | | 1,253,109 |
| Liabilities for unpaid losses and loss expenses, net of reinsurance | | | | | | | | | | $ 5,032,174 |

**Average Annual Percentage Payout of Incurred Losses by Age, Net of Reinsurance**

| Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|
| 7% | 9% | 10% | 9% | 8% | 7% | 6% | 5% | 6% | 6% |

(1) Total IBNR Liabilities Plus Expected Development on Reported Claims

*Reconciliation*

| *(U.S. dollars in thousands)* | | December 31, 2017 |
|---|---|---|
| Net outstanding liabilities | | |
| Insurance Operations | | |
| Property | $ | 1,929,773 |
| Specialty | | 1,842,734 |
| Professional | | 4,055,840 |
| Casualty and other | | 6,526,132 |
| Reinsurance Operations | | |
| Property and Other Short-Tail lines | | 2,780,254 |
| Casualty and Other Long-Tail lines | | 5,032,174 |
| **Subtotal, disaggregated triangles** | $ | 22,166,907 |
| | | |
| Unallocated loss expenses | | 578,995 |
| Discount (1) | | (415,479) |
| Provision for uncollectible reinsurance | | 41,103 |
| Other | | 85,807 |
| **Total net liability for unpaid losses and loss expenses** | | 22,457,333 |
| | | |
| Reinsurance recoverable on unpaid losses | | |
| Insurance Operations | | |
| Property | $ | 959,498 |
| Specialty | | 672,794 |
| Professional | | 1,386,847 |
| Casualty and other | | 3,367,498 |
| Reinsurance Operations | | |
| Property and Other Short-Tail lines | | 647,194 |
| Casualty and Other Long-Tail lines | | 125,003 |
| Other | | 80,612 |
| **Total recoverable on unpaid losses and loss expenses** | $ | 7,239,446 |
| | | |
| **Unpaid losses and loss expenses** | $ | 29,696,779 |

(1) As noted in Note 10(c), "Losses and Loss Expenses - Loss Reserve Discounting," the Company discounts only certain workers' compensation (including long term disability) liabilities and certain bodily injury liability claims, emanating from U.K. exposures, predominantly from the U.K. motor liability portfolio.

**(b) Net losses and loss expenses incurred**

Net losses and loss expenses incurred for the years indicated are comprised of:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Loss and loss expenses payments | $ 8,037,317 | $ 6,828,012 |
| Change in unpaid losses and loss expenses | 3,184,307 | 976,401 |
| Change in unpaid losses and loss expenses recoverable | (1,646,432) | (238,086) |
| Paid loss recoveries | (1,573,272) | (1,493,492) |
| Net losses and loss expenses incurred | $ 8,001,920 | $ 6,072,835 |

The following table presents the net (favorable) adverse prior year loss development of the Company's loss and loss expense reserves for its property and casualty operations for each of the years indicated:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Insurance operations | $ (41,759) | $ (91,459) |
| Reinsurance operations | (106,011) | (210,083) |
| **Total** | $ (147,770) | $ (301,542) |

The significant developments in prior year loss reserve estimates for each of the years indicated within the Company's Insurance and Reinsurance operations are discussed below.

*Insurance Operations*

The following table summarizes the net (favorable) adverse prior year development by business group relating to the Insurance operations  for the years ended December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Property | $ 96,383 | $ (38,078) |
| Specialty | (4,474) | (5,658) |
| Professional | (9,569) | 10,897 |
| Casualty and other | (124,099) | (58,620) |
| **Total** | $ (41,759) | $ (91,459) |

Net favorable prior year reserve development of $41.8 million for the year ended December 31, 2017 for the Insurance operations. This amount differs from the implied change in ultimate losses that can be calculated from the above triangles because the triangles exclude accident years prior to 2007 as well as minor business and, as noted earlier, utilize a different approach for handling foreign exchange. The total net prior year development of $41.8 million was driven by the following:

- For property lines, net prior year development was $96.4 million unfavorable. This was driven by adverse attritional loss experience on the 2015 and 2016 underwriting years within the London wholesale property book, which led to strengthening of $62.2 million. In addition, significant large loss experience primarily on 2016 losses on the energy property book resulted in strengthening of $39.9 million.
- For specialty lines, net prior year development was $4.5 million favorable. This was driven by better than expected attritional loss experience in aerospace. This was partially offset by worse than expected large loss experience in more recent years in the crisis management and political risk & trade credit portfolios.
- For professional lines, net prior year development was $9.6 million favorable. This was driven by releases of favorable experience in the core standard commercial portfolio in North America on the 2014 and prior exposure years. This was partially offset by strengthening in the professional select miscellaneous error and omissions portfolio and by strengthening in the international financial lines management liability book due to significant large loss experience primarily in 2014 and 2015 exposure years.
- For casualty and other lines, net prior year development was $124.1 million favorable. This was driven by consistent benign experience on a mature North America casualty portfolio resulting in releases of $64.7 million, as well as reductions to reflect better than expected loss experience reported on North America construction and global risk management. This was partially offset by strengthening to reflect worse than expected loss experience reported on the excess and surplus business.

Net favorable prior year reserve development totaled $91.5 million for the Insurance operations for the year ended December 31, 2016. Casualty benefited from release in international casualty primarily to reflect better than expected loss experience reported on the general and professional liability portfolios, predominantly on the 2011 and prior years. Better than expected loss experience reported for both catastrophe and non-catastrophe exposures led to release in property. Significant large loss activity on the international financial lines management liability book led to strengthening in professional.

There is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on the Company's historical results.

*Reinsurance Operations*

The following table summarizes the net (favorable) adverse prior year development by line of business relating to the Reinsurance operations for the years ended December 31, 2016 and 2017:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Property and Other Short-Tail Lines | $ (140,771) | $ (134,440) |
| Casualty and Other Long-Tail Lines | 34,760 | (75,643) |
| **Total** | $ (106,011) | $ (210,083) |

Net favorable prior year reserve development for the year ended December 31, 2017 totaled $106.0 million for the Reinsurance operations. This amount differs from the implied change in ultimate losses that can be calculated from the above triangles because the triangles exclude accident years prior to 2007 as well as minor business and, as noted earlier, utilize a different approach for handling foreign exchange. The total net prior year development of $106.0 million was attributable to the following:

- Net favorable prior year development for the short-tail lines totaled $140.8 million. Details of the significant components are as follows:
  - For property catastrophe lines, net prior year development was $63.0 million favorable .This was mainly to releases from our reserves for older catastrophes losses and better than expected experience on attritional losses.
  - For property other lines, net prior year development was $63.1 million favorable. This was mainly driven by favorable experience on older catastrophes and large losses and better than expected experience on attritional losses.
  - For specialty lines, net prior year development was $14.6 million. This was mainly due to favorable catastrophe and large loss experience and better than expected development on attritional losses. This was partially offset by strengthening on one large loss in the aviation book.
- Net favorable prior year development for the long-tail lines totaled $34.8 million. Details of the significant components are as follows:
  - For casualty lines, net prior year development was $46.3 million unfavorable primarily due to the change in the Ogden discount rate from 2.5% to negative 0.75% and unfavorable development on large losses.
  - For other lines, net prior year development was $11.6 million favorable largely due to better than expected experience on attritional losses, mainly on the credit and surety book and on the whole account book.

Net favorable prior year reserve development totaled $210.1 million for the year ended December 31, 2016. The short-tail lines benefited from $25.6 million in favorable development from property other lines, $76.6 million favorable development in property catastrophe lines and $32.2 million in favorable development within specialty lines. The release in long tail lines was due to favorable development of $65.5 million and $10.0 million in casualty and other, respectively.

There is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on the Company's historical results.

**(c) Loss Reserve Discounting**

Except for certain workers' compensation (including long term disability) liabilities and certain bodily injury liability claims, emanating from U.K. exposures, predominantly from the U.K. motor liability portfolio, the Company does not discount its unpaid losses and loss expenses.

The Company utilizes tabular reserving for workers' compensation (including long-term disability) unpaid losses that are considered fixed and determinable, and discounts such losses using an interest rate of 3.75% in 2017 and 2016. The interest rate approximates the implied return on the market-based assets supporting the expected cash flows of the Company's liabilities. The tabular reserving methodology results in applying uniform and consistent criteria for establishing expected future indemnity and medical payments (including an explicit factor for inflation) and the use of mortality tables to determine expected payment periods. Tabular unpaid losses and loss expenses, net of reinsurance, at December 31, 2017 and 2016 on an undiscounted basis were $762.8 million and $727.4 million, respectively. The aggregate discount for the time value of money deducted to derive the liability for unpaid losses and loss expenses were $295.8 million and $287.7 million at December 31, 2017 and 2016, respectively.

The related discounted unpaid losses and loss expenses were $467.0 million and $439.7 million at December 31, 2017 and 2016, respectively. The interest accretion related to the unwind of the discounted reserves was $19.2 million and $18.6 million during the years ended December 31, 2017 and 2016, respectively. This interest accretion was recorded in the incurred loss line as adverse prior year development.

The Company records a specific reserve allowance for Periodical Payment Orders ("PPOs") related to bodily injury liability claims. This allowance includes the unpaid losses for claims already settled and notified as PPOs at December 31, 2017, as well as the unpaid losses for claims to be settled in the future. The future care element of the unpaid losses was discounted using an interest rate of 2% at both December 31, 2017 and 2016. Unpaid losses and loss expenses, net of reinsurance, at December 31, 2017 and 2016 on an undiscounted basis were $269.9 million and $281.6 million, respectively. The aggregate discount for the time value of money deducted to derive the liability for the unpaid losses and loss expenses were $119.7 million and $125.9 million at December 31, 2017 and 2016. After discounting the future care element, the unpaid losses and loss expenses were $150.2 million and $155.7 million at December 31, 2017 and 2016, respectively. The decrease in the net undiscounted unpaid losses and loss expenses between December 31, 2017 and 2016 is mainly due to foreign exchange rate movements. The interest accretion related to the unwind of the discounted reserves was $2.8 million during the calendar years ended December 31, 2017 and 2016. This interest accretion was recorded in the incurred loss line as adverse prior year development.

**(d) Discontinued Asbestos and Run-Off Environmental Related Claims**

The Company's reserving process includes a continuing evaluation of the potential impact on unpaid liabilities from exposure to discontinued asbestos and run-off environmental related claims, including related loss adjustment expenses. Liabilities are established to cover both known and incurred but not reported claims. The Company's reserving and exposures to environmental liability business currently written within the Casualty underwriting division are not included in this note, which only relates to specific discontinued and/or run-off coverages that were not originally written specifically to cover environmental hazards.

The Company's exposure to discontinued asbestos and run-off environmental related claims arises from the following four sources:

(1) Reinsurance contracts written, both on a proportional and excess basis, after 1972. The Company discontinued writing contracts with these exposures in 1985. Business written was across many different policies, each with a relatively small contract limit. The Company's reported asbestos claims relate to both traditional products and premises and operations coverage.

(2) Winterthur - business of Winterthur purchased by the Company from AXA Insurance (formerly Winterthur Swiss Insurance Company) in 2001. Pursuant to the Sale and Purchase Agreement and related agreements, AXA Insurance reimburses the Company for all asbestos losses.

(3) During 2006, the Company acquired $40.2 million in losses through a loss portfolio transfer contract of which $18.3 million in losses related to asbestos and environmental claims. Given the terms of the policy, the combined aggregate limit on the total acquired reserves is $60.0 million, not including coverage for claims handling costs over a defined period.

(4) Contribution of Catlin - aviation insurance contracts written by Catlin in the Lloyd's market where the specific asbestos exclusion language was not implemented until 2003. Exposures only extend back to 1993 as Equitas was established to take on the Lloyd's market exposure for 1992 and prior. Exposure is due to asbestos-containing products in use by the aviation industry leading to claims against aviation manufacturers for asbestosis, mesothelioma and lung cancer.

A reconciliation of the opening and closing unpaid losses and loss expenses related to discontinued asbestos and run-off environmental exposure claims for the years indicated is as follows:

| **Year ended December 31,** *(U.S. dollars in thousands)* | | **2017** | | **2016** |
|---|---|---|---|---|
| Net unpaid losses and loss expenses at beginning of year | $ | 92,834 | $ | 93,704 |
| Net incurred losses and loss expenses | | (175) | | 9,042 |
| Less net paid losses and loss expenses | | 5,178 | | 9,912 |
| Net increase (decrease) in unpaid losses and loss expenses | $ | (5,353) | $ | (870) |
| Net unpaid losses and loss expenses at end of year | | 87,481 | | 92,834 |
| Unpaid losses and loss expenses recoverable at end of year | | 83,305 | | 83,430 |
| **Gross unpaid losses and loss expenses at end of year** | $ | 170,786 | $ | 176,264 |

Reserves for incurred but not reported losses, net of reinsurance, included in the above table were $51.3 million and $60.3 million at December 31, 2017 and 2016, respectively. Unpaid losses recoverable are net of potential uncollectible amounts.

At December 31, 2017, the Company had 2,176 open claim files for potential discontinued asbestos claims exposures and 435 open claim files for potential run-off environmental claims exposures. Approximately 37% and 34% of the open claim files are due to precautionary claim notices in 2017 and 2016, respectively. Precautionary claim notices are submitted by the ceding companies in order to preserve their right to receive coverage under the reinsurance contract. Such notices do not contain an incurred loss amount to the Company.

The development of the number of open claim files for potential discontinued asbestos and run-off environmental claims, including precautionary claims, is as follows:

| | **Asbestos Claims** | **Environmental Claims** |
|---|---|---|
| Total number of claims outstanding at December 31, 2015 | 2,591 | 430 |
| New claims reported in 2016 | 579 | 69 |
| Claims resolved in 2016 | (753) | (41) |
| Total number of claims outstanding at December 31, 2016 | 2,417 | 458 |
| New claims reported in 2017 | 435 | 24 |
| Claims resolved in 2017 | (676) | (47) |
| **Total number of claims outstanding at December 31, 2017** | 2,176 | 435 |

The Company's reserving process includes an ongoing evaluation of the potential impact on unpaid liabilities from exposure to discontinued asbestos and run-off environmental claims, including related loss adjustment expenses. Liabilities are established to cover both known and IBNR claims.

The estimation of loss and loss expense liabilities for discontinued asbestos and run-off environmental exposures is subject to much greater uncertainty than is normally associated with the establishment of liabilities for certain other exposures due to several factors, including: (i) uncertain legal interpretations and application of insurance and reinsurance coverage and liability; (ii) the lack of reliable available historical claims data as an indicator of future claims development; (iii) an uncertain political climate which may impact, among other areas, the nature and amount of costs for remediating waste sites; and (iv) the potential of insurers and reinsurers to reach agreements in order to avoid further significant legal costs. Due to the potential significance of these uncertainties, the Company believes that no meaningful range of loss and loss expense liabilities beyond recorded reserves can be established. As the Company's net unpaid loss and loss expense reserves related to discontinued asbestos and run-off environmental exposures are less than 1% of the total net reserves at December 31, 2017 and 2016, further adverse development is not expected to be material to the Company's overall net loss reserves. The Company believes it has made reasonable provisions for its discontinued asbestos and run-off environmental exposures and is unaware of any specific issues that would significantly affect its estimate of loss and loss expenses.

## 11. Future Policy Benefit Reserves

Net future policy benefit reserves are comprised of the following:

| **As of December 31** *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Traditional Life | $ 756,470 | $ 737,252 |
| Annuities | 2,854,456 | 2,768,795 |
| Gross future policy benefit reserves | $ 3,610,926 | $ 3,506,047 |
| Reinsurance recoverable - GreyCastle Life Retro Arrangements | $ (3,191,584) | $ (3,072,615) |
| Reinsurance recoverable - U.S. Term Life Retro Arrangements | $ (242,762) | $ (270,238) |
| Reinsurance recoverable - Other life retrocessions | $ (8,321) | $ (10,997) |
| Net future policy benefit reserves | $ 168,259 | $ 152,197 |

The Company entered into long duration contracts that subject the Company to mortality and morbidity risks and that were accounted for as life premiums earned. Future policy benefit reserves were established using appropriate assumptions for investment yields, mortality, and expenses, including a provision for adverse deviation. The average interest rate used for the determination of the future policy benefits for these contracts was 4.0% at December 31, 2017 and 2016.

Under the terms of the sale of the life reinsurance subsidiary to GreyCastle in 2014, the Company has reinsured $3.2 billion and $3.1 billion at December 31, 2017 and 2016 respectively, of its future policy benefit reserves under the GreyCastle Life Retro Arrangements. The Company continues to own, on a funds withheld basis, assets supporting the GreyCastle Life Retro Arrangements consisting of cash, fixed maturity securities and accrued interest. Based upon the contractual right of offset, the funds withheld liability owing to GCLR is recorded net of future policy benefit reserves recoverable, and is included within "Funds withheld on GreyCastle life retrocession arrangements (net of future policy benefit reserves recoverable)" on the Consolidated Balance Sheets, and is comprised of the following at December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Assets held on a funds withheld basis relating to the GreyCastle Life Retro Arrangements | $ 4,190,803 | $ 4,071,583 |
| Reinsurance recoverable from GCLR | (3,191,584) | (3,072,615) |
| **Funds withheld on GreyCastle life retrocession arrangements (net of future policy benefit reserves recoverable)** | $ 999,219 | $ 998,968 |

The Company has also reinsured an additional $242.8 million and $270.2 million at December 31, 2017 and 2016, respectively, of its U.S. Term Life future policy benefit reserves ("U.S. Term Life Retro Arrangements"). The Company continues to own, on a funds withheld basis, assets supporting the U.S. Term Life Retro Arrangements. Based upon the contractual right of offset, the funds withheld liability is recorded net of future policy benefit reserves recoverable, and is included within "Reinsurance balances payable" on the Consolidated Balance Sheets.

## 12. Reinsurance

The Company utilizes reinsurance and retrocession agreements principally to increase aggregate capacity and to reduce the risk of loss on business assumed. The Company's reinsurance and retrocession agreements provide for recovery of a portion of losses and loss expenses from reinsurers, and reinsurance recoverables are recorded as assets. The purchase of reinsurance does not relieve the Company of its obligation to policyholders. Under its reinsurance security policy, the Company seeks to cede business to reinsurers generally with a financial strength rating of "A" or better. The Company considers reinsurers that are not rated or do not fall within the above rating categories and may grant exceptions to the Company's general policy on a case-by-case basis.

The effect of reinsurance and retrocessional activity on premiums written and earned from property and casualty operations is shown below:

| | Premiums Written Year Ended December 31, | | Premiums Earned Year Ended December 31, | |
|---|---|---|---|---|
| *(U.S. dollars in thousands)* | **2017** | **2016** | **2017** | **2016** |
| Direct | $ 8,965,259 | $ 9,166,627 | $ 9,078,575 | $ 9,142,690 |
| Assumed | 5,787,313 | 4,458,981 | 4,903,909 | 4,074,817 |
| Ceded | (4,084,148) | (3,394,972) | (3,658,206) | (3,451,620) |
| **Net** | $ 10,668,424 | $ 10,230,636 | $ 10,324,278 | $ 9,765,887 |

The Company recorded reinsurance recoveries on losses and loss expenses incurred of $3.2 billion and $1.7 billion for the years ended December 31, 2017 and 2016, respectively.

The following table presents a summary of total reinsurance assets for the years ended December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Unpaid losses and loss expenses recoverable - P&C Operations | $ 7,239,446 | $ 5,480,300 |
| Unpaid losses and loss expenses recoverable - Corporate and Other | 8,277 | 10,997 |
| Total unpaid losses and loss expenses recoverable | 7,247,723 | 5,491,297 |
| Reinsurance balances receivable | 930,114 | 577,479 |
| Ceded unearned premiums | 2,198,217 | 1,687,864 |
| **Total reinsurance assets** | $ 10,376,054 | $ 7,756,640 |

The table above excludes a combined $3.2 billion and $0.2 billion of the Company's future policy benefit reserve recoverables under the GreyCastle Life Retro Arrangements and U.S. Term Life Retro Arrangements, as defined in Note 11, "Future Policy Benefit Reserves," respectively, and are also excluded from the remainder of this disclosure.

Reinsurance assets include amounts recoverable from reinsurers on both paid and unpaid losses and loss expenses which are contractual rights subject to credit risk. Amounts recoverable on unpaid losses and loss expenses will not be due for collection until sometime in the future. Economic conditions and operational performance of a particular reinsurer may impact its ability to fully meet these obligations. As such, the collectibility of such amounts requires significant estimation by the Company.

The provision for uncollectible reinsurance on unpaid losses and loss expenses recoverable is established principally based on an analysis of reinsurer credit quality, using default factors derived from reinsurer financial strength ratings. This analysis contemplates collateral in place, which is generally limited to assets held in trust, letters of credit and funds held by the Company with the same legal entity for which the Company believes there is a right of offset. The Company is the beneficiary of letters of credit, trust accounts and funds withheld in the aggregate amount of $6.7 billion and $4.1 billion at December 31, 2017 and 2016, respectively, collateralizing reinsurance recoverables with respect to certain reinsurers.

The Company uses an aging analysis to estimate uncollectible reinsurance balances receivable relating to paid losses in addition to recording allowances relating to any specific balances with known collectibility issues, irrespective of aging. The balances are aged from the date the expected recovery was billed to the reinsurer. Provisions are applied at specified percentages of the outstanding balances based upon the aging profile. Allowances otherwise required as a result of the aging process may not be recorded to the extent that specific facts and circumstances exist that lead management to believe that amounts will ultimately be collectible.

The following table presents a summary of the Company's allowance for uncollectible reinsurance at December 31, 2017 and 2016:

| *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Allowance relating to unpaid losses and loss expenses recoverable | $ 41,103 | $ 42,119 |
| Allowance relating to reinsurance balances receivable | 22,733 | 20,710 |
| **Total allowance for uncollectible reinsurance** | $ 63,836 | $ 62,829 |

At December 31, 2017 and 2016, approximately 95.6% and 95.4%, respectively, of the total reinsurance assets, net of collateral held, was due from reinsurers with a financial strength rating of "A" or better. The following table sets forth the ratings profile of the Company's reinsurers at December 31, 2017:

| Reinsurer Financial Strength Rating | % of Total |
|---|---|
| AAA | —% |
| AA | 37.0% |
| A | 58.6% |
| BBB | 0.5% |
| BB and below | 0.7% |
| Captives | 3.1% |
| Not Rated | 0.1% |
| Total | 100.0% |

The following is an analysis of the total reinsurance assets, net of collateral held, at December 31, 2017, by reinsurers owing 3% or more of such total:

| Name of Reinsurer | Reinsurer Financial Strength Rating | % of Total |
|---|---|---|
| Munich Reinsurance Co. | AA-/Stable | 10.5% |
| Lloyd's Syndicates | A+/Negative | 7.4% |
| Arch Reinsurance Company | A+/Negative | 7.3% |
| Transatlantic Reinsurance Company | A+/Stable | 5.1% |
| AXIS Reinsurance Co. | A+/Negative | 5.0% |
| Endurance Assurance Corporation | A/Positive | 4.3% |
| Hannover Rueck SE | AA-/Stable | 3.5% |
| National Indemnity Company | AA+/Negative | 3.1% |
| Swiss Reinsurance Co. | AA-/Stable | 3.1% |
| Everest Reinsurance (Bermuda) Ltd. | A+/Stable | 3.0% |

## 13. Deposit Liabilities

The Company has entered into certain insurance and reinsurance policies that transfer insufficient risk under GAAP to be accounted for as insurance or reinsurance transactions and are recognized as deposits. These structured P&C agreements have been recorded as deposit liabilities and are initially matched by an equivalent amount of investments. The Company has investment risk related to its ability to generate sufficient investment income to enable the total invested assets to cover the payment of the ultimate liability. See Note 4, "Investments," for further information relating to the Company's net investment income as well as realized and unrealized investment (losses) gains. Each deposit liability accrues at a rate equal to the internal rate of return of the payment receipts and obligations due during the life of the agreement. Where the timing and/or amount of future payments are uncertain, cash flows reflecting the Company's actuarially determined best estimates are utilized. Deposit liabilities are initially recorded at an amount equal to the assets received.

At December 31, 2017 and 2016, total deposit liabilities were $1.0 billion and $1.1 billion, respectively. For the years ended December 31, 2017 and 2016 interest expense of $25.3 million and $39.7 million, respectively, was recorded related to the accretion of deposit liabilities.

## 14. Financing Arrangements

### (a) Letter of Credit ("LOC") Facilities and Other Sources of Collateral

The Company has several credit facilities provided on both syndicated and bilateral bases from commercial banks. As described in more detail below, the Company may utilize the full capacity of these credit facilities to issue LOC in support of non-admitted insurance and reinsurance operations in the U.S. and to meet capital requirements at Lloyd's. Alternatively, under certain of the credit facilities, the Company instead may elect to utilize a stated portion of such facilities' capacity for revolving loans to support other operating or financing needs, which would reduce the amount available for LOC. The Company and several of its wholly-owned subsidiaries provide guarantees, on a joint and several basis, for obligations of the Company under certain of these facilities.

The following table presents the Company's ten and nine unsecured LOC facilities and revolving credit facilities at December 31, 2017 and 2016, respectively:

| *(U.S. dollars in thousands)* | December 31, 2017 | | December 31, 2016 | |
|---|---|---|---|---|
| **Facility Name:** | **Commitment** | **In Use/ Outstanding** | **Commitment** | **In Use/ Outstanding** |
| 2015 Citi Facility | $ — | $ — | $ 250,000 | $ 245,000 |
| Goldman Facility | — | — | 200,000 | 200,000 |
| 2016 Credit Agricole Facility I | 125,000 | 125,000 | 125,000 | 125,000 |
| 2016 Credit Agricole Facility II | 125,000 | 125,000 | 125,000 | 125,000 |
| 2017 Commonwealth Bank Facility | 215,000 | 215,000 | | |
| 2017 Credit Suisse Facility | 100,000 | 100,000 | | |
| FAL Facility I | 125,000 | 125,000 | 125,000 | 125,000 |
| FAL Facility II | 125,000 | 125,000 | 125,000 | 125,000 |
| FAL Facility III | 125,000 | 125,000 | 125,000 | 125,000 |
| FAL Facility IV | 125,000 | 125,000 | 125,000 | 125,000 |
| Syndicated Unsecured Facility | 750,000 | 2,000 | 750,000 | |
| 2017 Commerzbank Facility | 100,000 | 100,000 | | |
| | $ 1,915,000 | $ 1,167,000 | $ 1,950,000 | $ 1,195,000 |
| Facilities collateralized by certain investment assets | 1,477,986 | 1,382,226 | 2,041,687 | 1,150,293 |
| Total LOC facilities | $ 3,392,986 | $ 2,549,226 | $ 3,991,687 | $ 2,345,293 |
| Percentage of facilities collateralized by certain investment assets | | 54.2% | | 48.6% |

Certain credit facilities permit the Company to utilize up to $750.0 million and $1.0 billion as of December 31, 2017 and December 31, 2016, respectively, for revolving loans to support general operating and financing needs. At December 31, 2017 and December 31, 2016, $2.0 million and $245.0 million, respectively, were utilized under these facilities to issue letters of credit, leaving $748.0 million and $755.0 million, respectively, available to support other operating and financing needs.

*Funds at Lloyd's*

In November 2015, we entered into four bilateral unsecured credit agreements, each providing for $125 million of letters of credit for Funds at Lloyd's purposes (FAL Facility I, FAL Facility II, FAL Facility III, and FAL Facility IV, collectively the "FAL Facilities") for an aggregate amount of $500 million. Each of the FAL Facilities expires in 2019. The FAL Facilities replaced four unsecured bilateral facilities available for utilization by Catlin Insurance Company Ltd. ("Catlin-Bermuda") for Funds at Lloyd's purposes that we terminated in November 2015.

*Syndicated Facilities*

On August 5, 2016, the Company entered into agreements with a banking syndicate to provide: (a) a new secured credit facility that provides for the issuance of letters of credit up to $750 million (the "Secured Syndicated Facility"), and (b) a new unsecured credit facility that provides for the issuance of letters of credit and revolving credit loans up to $750 million (the "Unsecured Syndicated Facility", and together with the Secured Syndicated Facility, the "Syndicated Facilities"). The Company has the option to increase the maximum amount of letters of credit available under the facilities by $500 million in aggregate across the facilities.

In connection with the Syndicated Facilities, the Company's previous syndicated credit agreements originally entered into in November 2013, as well as certain related security arrangements, were terminated. The commitments under the Syndicated Facilities are available until, the earlier of (i) August 5, 2021 (unless extended by the parties), and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon the occurrence of certain events of default.

The availability of letters of credit under the Secured Syndicated Facility is subject to a borrowing base requirement, determined on the basis of specified percentages of the face value of eligible categories of assets varying by type of collateral. In the event that such credit support is insufficient, the Company could be required to provide alternative security to cedants. This could take the form of insurance trusts supported by the investment portfolio or funds withheld (amounts retained by ceding companies to collateralize loss or premium reserves) using the Company's cash resources or combinations thereof. The face amount of letters of credit required is driven by, among other things, loss development of existing reserves, the payment pattern of such reserves, the expansion of business written by the Company and the loss experience of such business.

*Credit Agricole Facilities*

In November and December of 2016, we entered into two credit agreements with Credit Agricole Corporate and Investment Bank ("Credit Agricole Facility I" and "Credit Agricole Facility II," respectively, and collectively, the "Credit Agricole Facilities"). Each credit agreement provides for the issuance of letters of credit in an amount up to $125 million. The commitments under the Credit Agricole Facilities expire on, and such facilities are available until, the earlier of (i) December 15, 2019, provided that, if neither the Company nor the lender provides notice to the other not more than 90 days, but at least 30 days, prior to such date, the commitment termination date will be extended to December 15, 2020, and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon the occurrence of certain events of default.

*Commonwealth Bank Facility*

On June 19, 2017, the Company entered into a new credit agreement with Commonwealth Bank of Australia, as administrative agent and issuing lender ("2017 Commonwealth Bank Facility"). The capacity available under this standby letter of credit is $215 million. The commitments under the 2017 Commonwealth Bank Facility expire on, and such credit facility is available until, the earlier of (i) September 15, 2020 and (ii) the date of termination in whole of the commitment upon an optional termination or reduction of the commitment by the account party or upon the occurrence of certain events of default.

*Credit Suisse Bank Facility*

On September 15, 2017, the Company entered into a new credit agreement with Credit Suisse Bank, as administrative agent and issuing lender ("2017 Credit Suisse Facility"). The capacity available under this standby letter of credit is $100 million. The commitments under the 2017 Credit Suisse Facility expire on, and such credit facility is available until, the earlier of (i) June 19, 2020 and (ii) the date of termination in whole of the commitment upon an optional termination or reduction of the commitment by the account party or upon the occurrence of certain events of default.

*Commerzbank Bank Facility*

On September 15, 2017, the Company entered into a new credit agreement with Commerzbank AG, as administrative agent and issuing lender ("2017 Commerzbank Facility"). The capacity available under this standby letter of credit is $100 million. The commitments under the 2017 Commerzbank Facility expire on, and such credit facility is available until, the earlier of (i) September 15, 2022 and (ii) the date of termination in whole of the commitment upon an optional termination or reduction of the commitment by the account party or upon the occurrence of certain events of default.

*Insurance Trusts and other matters*

In addition to letters of credit, the Company has established insurance trusts in the U.S. that provide cedants with statutory relief required under state insurance regulation in the U.S. It is anticipated that the commercial facilities may be renewed on expiry but such renewals are subject to the availability of credit from banks utilized by the Company and may be renewed with materially different terms and conditions. In the event that such credit support is insufficient, the Company could be required to provide alternative security to cedants. This could take the form of additional insurance trusts supported by the Company's investment portfolio or funds withheld using the Company's cash resources. The value of letters of credit required is driven by, among other things, loss development of existing reserves, the payment pattern of such reserves, the expansion of business written by the Company and the loss experience of such business.

The majority, of the Company's bank facilities, indentures and other documents relating to the Company's outstanding indebtedness (collectively, the "Company's Debt Documents"), which are described above, contain cross acceleration or cross default provisions to each other and the Company's Debt Documents contain affirmative and negative covenants as well as certain customary events of default. These covenants provide for, among other things, a maximum ratio of total consolidated debt plus consolidated net worth. Generally, each of the Company's Debt Documents provide for an event of default in the event of bankruptcy, insolvency or reorganization of the Company, and the majority of the Company's bank facilities provide an event of default if there is a change of control in the Company.

Given that many of the Company's Debt Documents contain cross acceleration or cross default provisions, a default by one of these subsidiaries may result in all holders declaring their debt due and payable and accelerating all debt due under those documents. If this were to occur, the Company may not have funds sufficient at that time to repay any or all of such indebtedness.

## 15. Related Party Transactions

### (a) Investment Manager Affiliates

At December 31, 2017 and 2016, the Company owned minority stakes in three and four independent investment management companies ("Investment Manager Affiliates"), respectively, that are actively managing client capital and seeking growth opportunities. The Company also invests in certain of the funds and limited partnerships and other legal entities managed by these affiliates, and through these funds and partnerships pays management fees and in some instances performance fees to the Company's Investment Manager Affiliates. In addition, at December 31, 2017 and 2016, the Company owned a minority stake in an independent firm, that provides technology and other services to alternative asset managers and allocators. The Company's interest in this enterprise is reported as an Investment Manager Affiliate, and the Company pays fees to this Investment Manager Affiliate, in exchange for it providing its services to the Company. Investment Manager Affiliate results are reported in the Consolidated Statements of Income as "Income (loss) from operating affiliates." See Note 5, "Investments in Affiliates," included herein, for further information.

### (b) Assumed Reinsurance Contracts

In the normal course of business, the Company enters into assumed reinsurance contracts with certain of its insurance affiliates, or their subsidiaries. During the years ended December 31, 2017 and 2016, these contracts resulted in reported net premiums, reported net losses and reported net acquisition costs as summarized below.

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Reported net premiums | $ 128,148 | $ 94,358 |
| Reported net losses | $ 97,759 | $ 44,728 |
| Reported net acquisition costs | $ 51,917 | $ 39,131 |

### (c) New Ocean

Commencing in 2014, several of the Company's wholly-owned subsidiaries retroceded assumed reinsurance business to special purpose reinsurers that receive capital from funds managed by the Company's subsidiary, New Ocean Capital Management ("New Ocean"), as, discussed in Note 16, "Variable Interest Entities." Underwriting administration services are provided to the special purpose reinsurers by other subsidiaries of the Company under service fee agreements, while investment advisory services are provided by New Ocean. During the year ended December 31, 2017, ceded premiums earned, ceded losses and loss expenses incurred, ceding commission income, and other fee income related to these retrocessional contracts were not material to the Company.

**(d) XL Innovate**

In April 2015, the Company announced the creation and sponsorship of the XL Innovate Fund, LP ("XL Innovate"), a venture capital initiative with a strategic focus on developing new capabilities in the insurance sector. The majority of XL Innovate's initial capital was financed by the Company. XL Innovate primarily seeks investments in equity positions of entities that provide new market opportunities for the Company throughout the world, striving to create partnerships outside of the traditional underwriting space to find ways to underwrite currently uninsured risks. The family trust of an employee of the Company owns a 5.21% non-controlling equity interest in XL Innovate. The employee serves as a member of the board of directors of both New Energy and XL Innovate, and maintains responsibility over the business generated by it. The underlying investments held by XL Innovate are reflected in the Company's Consolidated Financial Statements in accordance with the Accounting Policies provided in Note 1, "Significant Accounting Policies," based on the Company's level of investment in, and control over, such entities. Aside from investments made where the employee's family trust maintains non-controlling interest, there were no other material transactions between the Company and this employee for the year ended December 31, 2017.

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## 16. Variable Interest Entities

At times, the Company has utilized VIEs both indirectly and directly in the ordinary course of the Company's business. Within its investment portfolio, the Company has holdings in hedge funds, private equity entities and other investment vehicles. A number of these vehicles are considered VIEs based on their legal form and the generally passive role of their investors. As the Company lacks the ability to control the activities that most significantly impact the economic performance of these VIEs, the Company is not considered the primary beneficiary and does not consolidate these entities. The activities of the entities are generally limited to holding investments. The exposure to loss from these investments is limited to the carrying value of the investments at the balance sheet date.

In 2013, the Company, along with other investors, formed New Ocean to act as an investment manager that focuses on providing third-party investors access to insurance-linked securities and other insurance and reinsurance capital markets products. The Company holds a majority voting interest in New Ocean through its ownership of common shares and, accordingly, the financial statements of New Ocean have been included in the Consolidated Financial Statements of the Company. None of the assets, liabilities, revenues or net income of New Ocean were material to the Company during the current year. The equity interest attributable to third party investors in New Ocean recorded in the Company's Consolidated Balance Sheets as "Non-controlling interest in equity of consolidated subsidiaries" was $0.5 million and $1.0 million at December 31, 2017 and December 31, 2016, respectively.

After the establishment of New Ocean in 2013, the Company, along with other investors, formed a new Bermuda-based company, New Ocean Focus Cat Fund Ltd. ("New Ocean FCFL"), which is considered a VIE under GAAP. During the second quarter of 2014, the company formed another Bermuda-based investment company, New Ocean Market Value Cat Funds, Ltd. ("New Ocean MVCFL"), which is also considered a VIE under GAAP. New Ocean MVCFL primarily invests in insurance-linked securities, with a current focus on catastrophe bonds.

In 2014, New Ocean FCFL invested in a special purpose Bermuda reinsurer, Vector Reinsurance Ltd ("Vector Re"), which was formed for the purpose of underwriting collateralized excess-of-loss reinsurance with a focus on global property catastrophe risks. In the first quarter of 2015, New Ocean MVCFL also invested in Vector Re. Most of Vector Re's current underwriting activity relates to reinsurance business assumed from the Company's subsidiaries. Underwriting administration and claims services are provided to Vector Re by the Company under service fee contracts, while investment advisory services are provided by New Ocean.

The Company currently holds a controlling financial interests in New Ocean FCFL and New Ocean MVCFL, and by extension, Vector Re. Accordingly, the total net assets of New Ocean FCFL, New Ocean MVCFL and Vector Re are included in the Consolidated Financial Statements of the Company as noted below. The Company's shares of revenue and net income in these VIEs were not material to the Company for the year ended December 31, 2017. All inter-company transactions between the Company's entities have been eliminated in consolidation.

| *(U.S. dollars in thousands)* | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Total net assets | $ 242,605 | $ 223,373 |
| Non-controlling interest | 134,139 | 112,081 |
| **Total net assets attributable to XLB** | $ 108,466 | $ 111,292 |

## 17. Retirement Plans

The Company provides pension benefits to eligible employees through various defined contribution and defined benefit retirement plans sponsored by the Company, which vary for each subsidiary. Plan assets are invested principally in equity securities and fixed maturities.

### (a) Defined contribution plans

The Company has qualified defined contribution plans that are managed externally and to which employees and the Company contribute a certain percentage of the employee's pensionable salary each month. The Company's contribution generally vests after an employee has been with the Company for five years. The Company's expenses for its qualified contributory defined contribution retirement plans were $72.2 million and $86.3 million at December 31, 2017 and 2016, respectively.

### (b) Defined benefit plans

The Company maintains defined benefit plans that cover certain employees as follows:

***U.S. Plan***

A qualified non-contributory defined benefit pension plan exists to cover a number of U.S. employees. The plan was curtailed in 2002 and was closed to new entrants at that time. Under the terms of the curtailment, existing plan participants were no longer entitled to earn additional defined benefits for future services performed after the curtailment date; however, accrued benefits are eligible for annual cost-of-living increases. This plan also includes a non-qualified supplemental defined benefit plan designed to compensate individuals to the extent that their benefits under the Company's qualified plan are curtailed due to IRS Code limitations. Benefits are based on years of service and compensation, as defined in the plan, during the highest consecutive three years of the employee's last ten years of employment.

In addition, pursuant to agreements entered into by the Company, certain former employees have received benefit type guarantees, not formally a part of any established plan. The liability recorded with respect to these agreements at each of December 31, 2017 and 2016 was $2.4 million and $2.3 million, respectively, representing the entire unfunded projected benefit obligations.

***U.K. Plans***

A contributory defined benefit pension plan exists in the U.K., but has been closed to new entrants since 1996. Benefits are based on length of service and compensation as defined in the trust deed and rules. The pension liability recorded was $2.3 million and $4.1 million at December 31, 2017 and 2016, respectively, representing the entire unfunded projected obligation.

In connection with the Contribution of Catlin, the Company assumed additional assets and liabilities associated with a further U.K. defined benefit plan within Catlin. This plan has been closed to new members since 1993. The current membership consists only of pensioners and deferred members. Benefits are based on length of service and compensation.

***Other European Plans***

Certain contributory defined benefit pension plans exist in Germany which are closed to new entrants. Benefits are generally based on length of service and compensation defined in the related agreements.

***Other Plans***

The Company also acquired certain defined benefit pension liabilities with the acquisition of XL GAPS in 2007. The related balances are not included in the tables below as the liabilities are insured under an annuity type contract.

### *Funded Status - All Plans*

The funded status by geographical region of all the Company's retirement plans at December 31, 2017 and 2016 is as follows:

| ***Funded Status*** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| U.S. | $ (13,700) | $ (14,093) |
| U.K. | 1,606 | (2,316) |
| Other European | (26,484) | (26,377) |
| **Funded status – end of year** | $ (38,578) | $ (42,786) |

The status of all the Company's retirement plans at December 31, 2017 and 2016 is as follows:

| ***Change in projected benefit obligation*** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Projected benefit obligation – beginning of year | $ 120,038 | $ 122,165 |
| Service cost (1) | 1,296 | 1,701 |
| Interest cost | 3,620 | 5,126 |
| Actuarial (gain) / loss | (958) | 7,948 |
| Benefits and expenses paid | (5,831) | (5,977) |
| Foreign currency (gains) / losses | 7,531 | (10,248) |
| Settlements | (1,270) | (677) |
| Projected benefit obligation – end of year | $ 124,426 | $ 120,038 |

(1) Service costs include cost of living adjustments on curtailed plans.

| ***Change in plan assets*** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Fair value of plan assets – beginning of year | $ 77,252 | $ 79,402 |
| Actual return on plan assets | 7,900 | 8,499 |
| Employer contributions | 1,588 | 2,077 |
| Benefits and expenses paid | (4,769) | (4,577) |
| Foreign currency gains / (losses) | 3,877 | (8,149) |
| Fair value of plan assets – end of year | $ 85,848 | $ 77,252 |
| Funded status – end of year | $ (38,578) | $ (42,786) |
| Accrued pension liability | $ 38,578 | $ 42,786 |

The components of the net benefit cost for the years ended December 31, 2017 and 2016 are as follows:

| ***Components of net benefit cost*** *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Service cost | $ 1,296 | $ 1,701 |
| Interest cost | 3,620 | 5,126 |
| Expected return on plan assets | (3,522) | (4,357) |
| Amortization of net actuarial loss | 2,158 | 1,705 |
| Net benefit cost | $ 3,552 | $ 4,175 |

***Assumptions - All Plans***

Several assumptions and statistical variables are used in the models to calculate the expenses and liability related to the plans. The Company, in consultation with its actuaries, determines assumptions about the discount rate, the expected rate of return on plan assets and the rate of compensation increase. The table below includes disclosure of these rates on a weighted - average basis, for the years ended December 31, 2017 and 2016 as indicated:

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| | U.S. Plans | U.K. Plans | Other European Plans | U.S. Plans | U.K. Plans | Other European Plans |
| **Net Benefit Cost – Weighted-average assumptions** | | | | | | |
| Discount rate | 4.04% | 2.56% | 2.00% | 4.25% | 2.74% | 1.33% |
| Expected long-term rate of return on plan assets | 6.00% | 2.57% | N/A | 6.00% | 2.77% | N/A |
| Rate of compensation increase | N/A | 3.51% | 2.50% | N/A | 3.62% | 2.50% |
| **Benefit Obligation – Weighted-average assumptions** | | | | | | |
| Discount rate | 3.49% | 2.56% | 2.00% | 4.04% | 2.76% | 1.33% |
| Rate of compensation increase | N/A | 3.51% | 2.50% | N/A | 3.62% | 2.50% |

The expected long-term rate of return assumption is determined by adding expected inflation to the expected long-term real rates of various asset classes taking into account expected volatility and correlation between the various asset classes.

***Plan Assets - All Plans***

The U.S. Plan assets at December 31, 2017 and 2016 consist of three mutual funds. The first fund seeks long-term capital appreciation by investing in both other equity mutual funds and direct equity securities, with a focus on companies in the U.S., other developed countries and emerging markets. While the fund primarily invests in large companies, it may have exposure to companies in all market capitalization ranges.

The second fund invests primarily in U.S. government, U.S. government agency, and investment grade corporate bonds. The fund employs a high total investment return through a combination of current income and capital appreciation.

The third fund seeks to outperform longer-duration benchmarks without excess volatility through investing primarily in long-duration, investment-grade corporate and sovereign bonds.

The fair value of the U.S. Plan assets at December 31, 2017 and 2016 was $42.7 million and $38.7 million, respectively. As the investments of the retirement plan are mutual funds, they fall within Level 1 in the fair value hierarchy. The inputs and methodologies used in determining the fair value of these assets are consistent with those used to measure the Company's assets as set out in Note 8, "Fair Value Measurements."

The U.K. pension plan assets, including those acquired as part of the Contribution of Catlin, are held in a separate trustee administered fund to meet long term liabilities to past and present employees. The table below shows the composition of the plans' assets and the fair value of each major category of plan assets at December 31, 2017 and 2016, as well as the potential returns of the different asset classes. The totals of the asset values held in various externally managed portfolios are provided by third party pricing vendors. There is no significant concentration of risk within plan assets. The assets in the plans and the expected rates of return were as follows:

| *(U.S. dollars in thousands, except percentages)* | Expected Return on Assets for 2017 | Fair Value at December 31, 2017 | Expected Return on Assets for 2016 | Fair Value at December 31, 2016 |
|---|---|---|---|---|
| Equities and growth funds | 5.6% | $ 11,035 | 5.7% | $ 9,122 |
| Gilts | 1.9% | 15,785 | 2.4% | 15,459 |
| Corporate bonds | 2.6% | 16,021 | 3.3% | 13,850 |
| Other (cash) | 0.5% | 320 | 0.5% | 89 |
| Total market fair value of assets | | $ 43,161 | | $ 38,520 |

As the remaining other European plans are unfunded, they held no plan assets at December 31, 2017 and 2016.

***Funding / Expected Cash Flows - U.S. Plan***

Under the U.S. defined benefit plans, the Company's policy is to make annual contributions to the plan that are deductible for federal income tax purposes and that meet the minimum funding standards required by law. The contribution level is determined by utilizing the projected unit credit cost method and different actuarial assumptions than those used for pension expense purposes. The Company's funding policy provides that contributions to the plan shall be at least equal to the minimum funding requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended by the Pension Protection Act of 2006. During the fiscal year beginning January 1, 2018, the U.S. defined benefit plans expect to make contributions of $1.4 million.

The estimated future benefit payments with respect to the U.S. defined benefit pension plans are as follows:

| *(U.S. dollars in thousands)* | Retirement Plan | Benefits Equalization Plan | Total |
|---|---|---|---|
| 2018 | $ 1,106 | $ 354 | $ 1,460 |
| 2019 | $ 1,248 | $ 452 | $ 1,700 |
| 2020 | $ 1,397 | $ 469 | $ 1,866 |
| 2021 | $ 1,690 | $ 504 | $ 2,194 |
| 2022 | $ 1,800 | $ 536 | $ 2,336 |
| 2023-2027 | $ 11,560 | $ 2,939 | $ 14,499 |

***Funding - U.K. Plans***

The Company's U.K. plan administered for employees who joined prior to the Contribution of Catlin, is subject to triennial funding valuations, the most recent of which was conducted as of June 30, 2015 and was reported in 2016. The $1.0 million deficit (calculated on a realistic basis) is being funded over a 4-year period.

With respect to the U.K. plan assumed as part of the Contribution of Catlin, the most recent funding valuation was prepared as at October 1, 2016. No contributions were required following that valuation. During 2018, it is expected that no contributions will be paid to the plan.

## 18. Commitments and Contingencies

### (a) Concentrations of Credit Risk

The creditworthiness of any counterparty is evaluated by the Company, taking into account credit ratings assigned by rating agencies. The credit approval process involves an assessment of factors including, among others, the counterparty and country and industry credit exposure limits. Collateral may be required, at the discretion of the Company, on certain transactions based on the creditworthiness of the counterparty.

The areas where significant concentrations of credit risk may exist include total reinsurance assets as noted in Note 12, "Reinsurance," and in the investment fixed income portfolio.

***Reinsurance Assets***

The Company's reinsurance assets result from reinsurance arrangements in the course of its operations. A credit exposure exists with respect to reinsurance assets as they may be uncollectible. The Company manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and if necessary, the Company may hold collateral in the form of funds, trust accounts and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis.

***Fixed Income Portfolio***

The Company did not have an aggregate direct investment in any single corporate issuer in excess of 5% of the Company's shareholders' equity at December 31, 2017 and 2016. Corporate issuers represent only direct exposure to fixed maturities and short-term investments of the parent issuer and its subsidiaries. These exposures exclude asset and mortgage backed securities that were issued, sponsored or serviced by the parent and government-guaranteed issues, but do include covered bonds.

***Broker credit risk***

In addition, the Company underwrites a significant amount of its insurance and reinsurance property and casualty business through brokers and a credit risk exists should any of these brokers be unable to fulfill their contractual obligations with respect to the payments of insurance and reinsurance balances to the Company. During the two years ended December 31, 2017 and 2016, P&C gross written premiums generated from or placed by the below companies individually accounted for more than 10% of the Company's consolidated gross written premiums from P&C operations, as follows:

| (Percentage of consolidated gross written premiums from P&C operations) | 2017 | 2016 |
|---|---|---|
| AON Corporation and subsidiaries | 17% | 18% |
| Marsh & McLennan Companies | 18% | 18% |
| Willis Group and subsidiaries | 10% | 11% |

These brokers are large, well established companies and there are no indications that any of them are financially troubled. No other broker and no one insured or reinsured accounted for more than 10% of gross premiums written from P&C operations in any of the two years ended December 31, 2017 and 2016.

**(b) Other Investments**

The Company has committed to invest in certain private equity and private credit limited partnerships, limited liability companies or similar structures. At December 31, 2017, the Company had unfunded commitments with these entities totaling $82.6 million over a weighted average period of 6.5 years.

**(c) Investments in Affiliates**

The Company has committed to invest in certain private equity and private credit limited partnerships, limited liability companies or similar structures where it accounts for its holdings in these structures under the equity method. At December 31, 2017, the Company had unfunded commitments, with these entities totaling to $308.0 million over a weighted average period of 5.1 years.

**(d) Properties**

The Company rents space for certain of its offices under leases that expire through 2031. Total rent expense under operating leases for the years ended December 31, 2017 and 2016 was approximately $76.3 million and $68.0 million, respectively. Future minimum rental commitments under existing operating leases are expected to be as follows:

| **Year Ended December 31,** *(U.S. dollars in thousands)* | | |
|---|---|---|
| 2018 | $ | 74,765 |
| 2019 | | 65,903 |
| 2020 | | 59,328 |
| 2021 | | 54,624 |
| 2022 | | 45,630 |
| 2023 - 2031 | | 68,202 |
| **Total minimum future rentals** | $ | 368,452 |

In 2003, the Company entered into a purchase, sale and leaseback transaction to acquire new office space in London. The Company has recognized a capital lease asset net of accumulated depreciation of $55.7 million and $55.5 million, a capital lease liability of $94.2 million and $89.9 million, and a deferred gain liability of $16.9 million, for both periods, related to the sale and leaseback, at December 31, 2017 and 2016, respectively. The gain is being amortized to income in line with the amortization of the asset. The future minimum lease payments annually for the next five years are noted in the following table. as well as the aggregate for beyond five years. The total future minimum lease payments in the aggregate are expected to be $133.4 million.

| **Year Ended December 31,** *(U.S. dollars in thousands)* | | |
|---|---|---|
| 2018 | $ | 11,269 |
| 2019 | | 11,551 |
| 2020 | | 11,840 |
| 2021 | | 12,136 |
| 2022 | | 12,439 |
| 2023-2028 | | 74,142 |
| **Total minimum future lease payments** | $ | 133,377 |

### (e) Tax Matters

Neither the Company nor its non-U.S. subsidiaries have paid U.S. corporate income taxes on the basis that they are not engaged in a trade or business or otherwise subject to taxation in the United States. However, because definitive identification of activities that constitute being engaged in a trade or business in the United States is not provided by the Internal Revenue Code ("IRS Code"), regulations or court decisions, there can be no assurance that the Internal Revenue Service will not contend that the Company or its non-U.S. subsidiaries are engaged in a trade or business or otherwise subject to taxation in the United States. If the Company or its non-U.S. subsidiaries were considered to be engaged in a trade or business in the United States (and, if the Company or such subsidiaries were to qualify for the benefits under the income tax treaty between the United States and Bermuda and other countries in which the Company operates, such businesses would be considered to be attributable to a "permanent establishment" in the United States), the Company or such subsidiaries could be subject to U.S. tax at regular tax rates on their respective taxable income that is effectively connected with their U.S. trade or business plus an additional "branch profits" tax (at a rate as high as 30%) on such income remaining after the regular tax, in which case there could be a significant adverse effect on the Company's results of operations and financial position.

### (f) Letters of Credit

At December 31, 2017 and 2016, $2.5 billion and $2.3 billion of letters of credit were outstanding, of which 54.2% and 48.6%, respectively, were collateralized by the Company's investment portfolios, primarily supporting U.S. non-admitted business and the Company's Lloyd's syndicates' capital requirements.

### (g) Litigation

The Company and its subsidiaries are subject to litigation and arbitration in the normal course of business. These lawsuits and arbitrations principally involve claims on policies of insurance and contracts of reinsurance and are typical for the Company and for the property and casualty insurance and reinsurance industry in general. Such claims proceedings are considered in connection with the Company's loss and loss expense reserves. Reserves in varying amounts may or may not be established in respect of particular claims proceedings based on many factors, including the legal merits thereof. In addition to litigation relating to insurance and reinsurance claims, the Company and its subsidiaries are subject to lawsuits and regulatory actions in the normal course of business that do not arise from or directly relate to claims on insurance or reinsurance policies. This category of business litigation typically involves, among other things, allegations of underwriting errors or misconduct, employment claims, regulatory activity, shareholder disputes or disputes arising from business ventures. The status of these legal actions is actively monitored by management.

Legal actions are subject to inherent uncertainties, and future events could change management's assessment of the probability or estimated amount of potential losses from pending or threatened legal actions. Based on available information, it is the opinion of management that the ultimate resolution of pending or threatened legal actions other than claims proceedings, both individually and in the aggregate, will not result in losses having a material adverse effect on the Company's financial position or liquidity at December 31, 2017.

If management believes that, based on available information, it is at least reasonably possible that a material loss (or additional material loss in excess of any accrual) will be incurred in connection with any legal actions other than claims proceedings, the Company discloses an estimate of the possible loss or range of loss, either individually or in the aggregate, as appropriate, if such an estimate can be made, or discloses that an estimate cannot be made. Based on the Company's assessment at December 31, 2017, no such disclosures were considered necessary.

### (h) Financial Guarantee Exposures

In February 2017, the Company negotiated the termination of its final outstanding financial guarantee contracts. These contracts provided credit support for a variety of collateral types, including some issued by European financial institutions. The Company will not recognize any financial costs or any security valuation losses as a result of these terminations.

## 19. Share Capital

### *a) Authorized and Issued*

The authorized share capital of XLB is 15,000,000, par value $0.10 each. On April 27, 2016 as part of a strategic business decision, the Company issued a further 2,500,000 shares, par value $0.10 each and hence the total issued and outstanding shares as at December 31, 2017 and 2016 was 12,500,000, respectively.

The following table is a summary of ordinary shares issued and outstanding:

| *(in thousands)* | **2017** | **2016** |
|---|---|---|
| Balance – beginning of year | 1,250 | 1,000 |
| Issue of shares | — | 250 |
| **Balance – end of year** | 1,250 | 1,250 |

### *b) Acquisition of Non-controlling Preferred Shares*

In connection with the contribution of Catlin from the Parent, the Company received 0.6 million non-cumulative perpetual preferred shares issued by Catlin-Bermuda, par value of $0.01per share, with liquidation preference of $1,000 per share, plus declared and unpaid dividends ("CICL Prefs"). Dividends are payable quarterly at a rate equal to 2.975 percent plus the three-month LIBOR rate of the liquidation preference.

On July 7, 2017, the Company repurchased through a tender offer 46,635 of the outstanding CICL Prefs with a net carrying value of $43.7 million for $45.6 million, inclusive of transaction costs and other consideration. The preference shares were canceled on July 19, 2017. As a result of these repurchases, the Company recorded a loss of $1.9 million through "Non-controlling interests" in the Consolidated Statements of Income.

## 20. Dividends and Return of Surplus

The Company paid dividends to its parent, EXEL Holdings Limited ("EXEL"), an intermediate holding company, of $0.8 billion in cash for 2017. The Company paid a dividend to its parent, EXEL of $0.4 billion in 2016, $0.2 billion was cash and $0.2 billion was investments.

In addition, the Company had no return of capital for 2017, and returned $0.9 billion of additional paid in capital to EXEL during 2016.

## 21. Accumulated Other Comprehensive Income (Loss)

The changes in AOCI, net of tax, by component for the years ended December 31, 2017 and 2016 are as follows:

| *(U.S. dollars in thousands)* | Unrealized Gains (Losses) on Investments (1) | OTTI Losses Recognized in AOCI | Foreign Currency Translation Adjustments | Underfunded Pension Liability | Total |
|---|---|---|---|---|---|
| Balance, net of tax, December 31, 2015 | $ 577,489 | $ (15,899) | $ (36,154) | $ (24,641) | $ 500,795 |
| OCI before reclassifications | 376,199 | — | 103,259 | (1,333) | 478,125 |
| Amounts reclassified from AOCI | (463,014) | 3,719 | — | 3,100 | (456,195) |
| Tax (benefit) expense | 28,537 | (49) | (7,299) | (2,014) | 19,175 |
| Net current period OCI - net of tax | $ (58,278) | $ 3,670 | $ 95,960 | $ (247) | $ 41,105 |
| Balance, net of tax, December 31, 2016 | $ 519,211 | $ (12,229) | $ 59,806 | $ (24,888) | $ 541,900 |
| OCI before reclassifications (1) | 437,386 | — | 46,845 | 735 | 484,966 |
| Amounts reclassified from AOCI | (274,841) | 2,478 | — | 127 | (272,236) |
| Tax (benefit) expense (2) | (10,646) | (63) | (3,668) | 1,669 | (12,708) |
| Net current period OCI - net of tax | $ 151,899 | $ 2,415 | $ 43,177 | $ 2,531 | $ 200,022 |
| Balance, net of tax, December 31, 2017 | $ 671,110 | $ (9,814) | $ 102,983 | $ (22,357) | $ 741,922 |

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(1) For certain annuity contracts that are subject to the GreyCastle Life Retro Arrangements, policy benefit reserves were historically increased for the impact of changes in unrealized gains on investments supporting such contracts as if the gains had been realized, with a corresponding entry to other comprehensive income ("Shadow Adjustments"). Upon completion of the GreyCastle Life Retro Arrangements, no further Shadow Adjustments were recorded. As of December 31, 2016, the cumulative impact of the Shadow Adjustments was $212.1 million. During the year ended December 31, 2017, net movement of $(27.2) million were recorded, resulting in a total cumulative net impact of Shadow Adjustments on future policy benefit reserves of $184.9 million at December 31, 2017.

(2) During the the year ended December 31, 2017, the Company recorded an out-of-period reduction of $17.4 million to "Foreign currency translation adjustments, net of tax,"
within the Consolidated Statements of Comprehensive Income. This adjustment arose from a previously unrecognized tax liability on foreign exchange movements that should
have been reflected in the comprehensive income of a prior period. The Company has evaluated the quantitative and qualitative aspects of this correction and concluded that the
impact of recognizing it during this year is not material to the Consolidated Financial Statements, nor is it material to any prior period Consolidated Financial Statements.

The reclassifications out of AOCI along with the associated Consolidated Statements of Income line items affected by component, and the total related tax (expense) benefit for indicated years ended December 31, 2017 and 2016, are as follows:

| **Details About AOCI Components** *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| **Unrealized gains and losses on investments:** | | |
| Net realized gains (losses) on investments sold | $ (234,579) | $ (459,979) |
| OTTI on investments | 14,422 | 81,595 |
| Net realized and unrealized gains (losses) on life retrocession embedded derivative and derivative instruments - Life Funds Withheld Assets | (54,684) | (51,100) |
| Income (loss) from investment affiliates | — | (33,530) |
| Total before tax | $ (274,841) | $ (463,014) |
| Provision (benefit) for income tax | 3,161 | 10,084 |
| Net of tax | $ (271,680) | $ (452,930) |
| | | |
| **OTTI losses recognized in OCI:** | | |
| Net realized gains (losses) on investments sold | $ 2,119 | $ 4,158 |
| OTTI on investments transferred to (from) OCI | 359 | (439) |
| Total before tax | $ 2,478 | $ 3,719 |
| Provision (benefit) for income tax | (4) | — |
| Net of tax | $ 2,474 | $ 3,719 |
| | | |
| **Underfunded Pension Liability:** | | |
| Operating Expenses | $ 127 | $ 3,100 |
| Provision (benefit) for income tax | (45) | (1,085) |
| Net of tax | $ 82 | $ 2,015 |
| | | |
| **Total reclassifications for the period, gross of tax** | $ (272,236) | $ (456,195) |
| Tax (benefit) expense | 3,112 | 8,999 |
| Total reclassifications for the period, net of tax | $ (269,124) | $ (447,196) |

## 22. Taxation

The Company conducts global operations through its subsidiaries in various jurisdictions around the world, including but not limited to Bermuda, the U.S., the U.K., Switzerland, Ireland, France, Germany, Italy, and Spain. The Company is subject to tax in accordance with the relevant tax laws and regulations governing taxation in the jurisdictions in which it operates.

The Company, and its Bermuda subsidiaries, are not subject to any income or capital gains taxes under current Bermuda law. In the event that there is a change such that these taxes are imposed, the Bermuda subsidiaries would be exempted from any such tax until March 2035 pursuant to the Bermuda Exempted Undertakings Tax Protection Act 1966, and the Exempted Undertakings Tax Protection Amendment Act 2011.

The Company's U.S. subsidiaries are subject to federal, state and local corporate income taxes, as well as premium, excise and other taxes applicable to U.S. corporations. The U.S. related provision for federal income taxes has been determined under the principles of the consolidated tax provisions of the IRS Code and Regulations thereunder.

On December 22, 2017, the U.S Tax Cuts and Jobs Act was enacted. The new law, which takes effect for taxable years beginning on or after January 1, 2018, includes numerous changes in tax law, including: (1) a reduction in the federal corporate income tax rate from 35% to 21%; (2) repeal of the corporate Alternative Minimum Tax, with existing credit carryforwards refundable no later than 2021; (3) limitations on the deductibility of certain elements of executive compensation; and (4) a number of base erosion provisions designed to reduce the ability of multinational companies to reduce the U.S. tax base through payments to offshore affiliates.

On December 22, 2017, the U.S. Securities and Exchange Commission issued Staff Accounting Bulletin No. 118 ("SAB 118"), which provides guidance on accounting for the income tax effects of the U.S. Tax Cuts and Jobs Act. SAB 118 provides scenarios where the measurement of the income tax effects is complete, incomplete, or incomplete but for which a reasonable provisional amount can be estimated, and provides a twelve month measurement period from the enactment date to complete the accounting.

Based on its initial analysis of the provisions of the new tax law, and associated guidance issued to date, the Company recorded a net income tax expense of $100.5 million in the period ended December 31, 2017, primarily to reduce the value of its net deferred tax assets to reflect the reduction in the U.S. federal corporate income tax rate. In accordance with SAB 118, the accounting for the income tax effects of the rate change on the net deferred tax asset is complete.

The Company has recorded provisional amounts that are incomplete, but have been reasonably estimated, related to the re-computation of its insurance reserves and the transition adjustment from the existing laws. The Company may reflect adjustments to its provisional amounts upon issuance of additional guidance with respect to the operation of the new tax law provisions, or by obtaining, preparing, or analyzing additional information about facts and circumstances that existed as of the enactment date that, if known, would have affected the income tax effects initially reported as provisional amounts. The Company does not expect these adjustments to be material to its financial position.

With the exception of the U.S., deferred income taxes have not been accrued with respect to certain undistributed earnings of subsidiaries located outside of Bermuda. If the earnings were to be distributed, as dividends or otherwise, such amounts may be subject to withholding taxation in the jurisdiction of the paying entity. The Company does not assert that all earnings arising in the U.S. will be permanently reinvested in the U.S., and accordingly, the Company provides for withholding taxes arising in respect of current period U.S. earnings. No withholding taxes are accrued with respect to the earnings of the Company's subsidiaries arising outside the U.S. However, if there is a change in tax law, interpretation of existing law, or change in way in which the Company conducts its business, then the company would accrue the required withholding tax.

The Company's current corporate structure is such that distribution of earnings from subsidiaries located outside of the United States would not be subject to significant incremental taxation. It is not practicable to estimate the amount of additional withholding taxes that might be payable on such earnings due to a variety of factors, including the timing, extent and nature of any repatriation.

The table below details the tax years that are open to assessment and under examination by local tax authorities, by major tax jurisdictions. While the Company cannot estimate with certainty the outcome of these examinations, the Company does not believe that adjustments from open tax years will result in a significant change to the Company's financial results.

| **Jurisdiction** | **Tax Years Open to Assessment** | **Tax Years Under Examination** |
|---|---|---|
| France | 2013 - 2017 | 2013 - 2014 |
| Germany | 2014 - 2017 | |
| Ireland | 2013 - 2017 | |
| Italy | 2013 - 2017 | |
| Spain | 2011 - 2017 | 2011 - 2012 |
| Switzerland | 2013 - 2017 | |
| U.K. | 2013 - 2017 | 2013 - 2015 |
| U.S. | 2013 - 2017 | 2013 - 2015 |

The Company's income (loss) before income tax and non-controlling interests for the years ended December 31, 2017 and 2016 was distributed between U.S. and non-U.S. jurisdictions as follows:

| **Income (loss) before income tax and non-controlling interest:** *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| U.S. | $ 115,086 | $ 68,970 |
| Non U.S. | (334,762) | 770,833 |
| **Total** | $ (219,676) | $ 839,803 |

The income tax provisions for the years ended December 31, 2017 and 2016 are as follows:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Current expense: (benefit)** | | |
| U.S. | $ 715 | $ (12,201) |
| Non U.S. | 103,339 | 59,282 |
| **Total current expense (benefit)** | $ 104,054 | $ 47,081 |
| **Deferred expense (benefit):** | | |
| U.S. | $ 100,126 | $ 8,502 |
| Non U.S. | (145,110) | (13,203) |
| **Total deferred expense (benefit)** | $ (44,984) | $ (4,701) |
| **Total tax expense (benefit)** | $ 59,070 | $ 42,380 |

The applicable statutory tax rates for the current year of the most significant jurisdictions contributing to the overall taxation of the Company are:

| Jurisdiction | Applicable Statutory Corporate Income Tax Rates |
|---|---|
| Bermuda | —% |
| France (1) | 33.33% |
| Germany (2) | 15.00% |
| Ireland (3) | 12.50% |
| Switzerland (4) | 21.15% |
| U.K. (5) | 19.25% |
| U.S. (6) | 35.00% |

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(1) The statutory corporate income tax rate is 33.33%. However, with the mandatory social surcharge, the combined statutory rate would increase to 34.43%.

(2) The statutory corporate income tax rate is 15% . However, including applicable surcharges and local trade tax, which can vary by location, would increase the combined statutory rate to approximately 33%.

(3) The 12.50% statutory corporate income tax rate applies to active income from the conduct of a trade in Ireland. For passive income or income from other defined activities the statutory rate increases to 25%.

(4) Represents the combined federal and cantonal rate primarily applicable to the Company's Swiss entities.

(5) The statutory rate is 19% effective April 1, 2017. However, from January 1, through March 31, 2017 the statutory rate is 20%. Due to this change of rate, the average statutory tax rate for 2017 is 19.25%.

(6) The statutory tax rate is 35% for the 2017 tax year. Under the Tax Cuts and Jobs Act of 2017, the federal corporate tax rate has been reduced to 21% for taxable years beginning January 1, 2018.

The expected tax provision has been calculated using the pre-tax accounting income (loss) in each jurisdiction multiplied by that jurisdiction's applicable statutory tax rate. A reconciliation of the difference between the provision for income taxes and the expected tax provision for the years ended December 31, 2017 and 2016 is provided below:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Expected tax (benefit) provision | $ (2,534) | $ (15,467) |
| Permanent differences: | | |
| Non-taxable (income) loss | (41,043) | (19,937) |
| Revision to prior year adjustments | 9,428 | (24,121) |
| State, local and foreign taxes | 37,454 | 23,407 |
| Valuation allowance | 2,510 | (9,109) |
| Net allocated investment income | 8,531 | 5,990 |
| Stock awards | (3,132) | 543 |
| Non-deductible expenses | 3,313 | 42,900 |
| Other Investment related adjustments | (1,753) | (905) |
| Adjustments related to GreyCastle Life Retro Arrangements | (9,815) | 21,682 |
| Change in Tax Rate | (8,105) | (6,233) |
| U.S. Tax Cuts and Jobs Act of 2017, net deferred tax asset revaluation | 100,500 | — |
| Uncertain tax positions | (36,284) | 23,630 |
| **Total tax expense (benefit)** | $ 59,070 | $ 42,380 |

Significant components of the Company's deferred tax assets and liabilities at December 31, 2017 and 2016 were as follows:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| **Deferred tax asset:** | | |
| Net unpaid loss reserve discount | $ 82,026 | $ 96,357 |
| Net unearned premiums | 104,168 | 95,676 |
| Compensation liabilities | 56,760 | 95,372 |
| Net operating losses | 285,294 | 263,106 |
| Investment adjustments | 18,570 | 14,030 |
| Pension | 10,770 | 6,816 |
| Bad debt reserve | 14,844 | 12,418 |
| Amortizable goodwill | — | 967 |
| Net unrealized depreciation on investments | 2,719 | 5,915 |
| Stock options | 624 | 5,369 |
| Depreciation | 23,411 | 26,098 |
| Net realized capital losses | 63,757 | 89,568 |
| Deferred intercompany capital losses | 9,997 | 18,221 |
| Untaxed Lloyd's result | 91,056 | — |
| Deferred acquisition costs | 65,432 | 17,820 |
| Tax Credits | 53,304 | 71,651 |
| Other | 27,270 | 32,514 |
| Deferred tax asset, gross of valuation allowance | $ 910,002 | $ 851,898 |
| Valuation allowance | 282,445 | 301,346 |
| Deferred tax asset, net of valuation allowance | $ 627,557 | $ 550,552 |
| **Deferred tax liability:** | | |
| Net unrealized appreciation on investments | $ 16,170 | $ 21,500 |
| Deferred acquisition costs | 62,871 | 10,858 |
| Currency translation adjustments | 13,170 | 12,813 |
| Regulatory reserves | 99,265 | 116,500 |
| Net unearned premiums | 9,270 | 4,380 |
| Investment adjustments | 4,232 | 5,269 |
| Untaxed Lloyd's result | — | 11,940 |
| Depreciation | 11,355 | 15,601 |
| Syndicate capacity | 87,714 | 82,106 |
| Intangible asset | 24,473 | 32,508 |
| Other | 24,587 | 3,806 |
| Deferred tax liability | $ 353,107 | $ 317,281 |
| **Net Deferred Tax Asset** | $ 274,450 | $ 233,271 |

The deferred tax asset and deferred tax liability balances presented above represent the gross deferred tax asset and liability balances across each tax jurisdiction. As disclosed on the Consolidated Balance Sheets, the deferred tax asset balances of $332.0 million and $310.5 million at December 31, 2017 and 2016, respectively, and deferred tax liability balances of $57.6 million and $77.3 million at December 31, 2017 and 2016, respectively, include netting of certain deferred tax assets and liabilities within a tax jurisdiction to the extent such netting is consistent with ASC 740 "Income Taxes".

At December 31, 2017 and 2016, the valuation allowance of $282.4 million and $301.3 million, respectively, related primarily to net operating loss and realized capital loss carryforwards in the following major tax jurisdictions:

| **Jurisdiction** *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Australia | $ 18,849 | $ 15,120 |
| Austria | 919 | 10,162 |
| Brazil | 14,909 | 12,857 |
| France | 28,656 | 23,523 |
| Germany | 32,566 | 9,563 |
| Hong Kong | 5,749 | 3,780 |
| Ireland | 30,536 | 30,623 |
| Italy | — | 10,313 |
| Luxembourg | 8,025 | 5,648 |
| Singapore | 9,331 | 8,916 |
| Spain | 20,387 | 16,709 |
| Switzerland | 20,935 | 15,025 |
| U.K. | 28,328 | 32,528 |
| U.S. | 53,761 | 92,999 |
| Other | 9,494 | 13,580 |
| Valuation Allowance Total | $ 282,445 | $ 301,346 |

The decrease in the valuation allowance in 2017 of $18.9 million was primarily driven by the revaluation of U.S. capital loss related deferred tax assets, in conformity with U.S. Tax Cuts and Jobs Act, for which a valuation allowance is held. The increase in the valuation allowance in Germany is due to a reduction in deferred tax liabilities that were supporting the recognition of deferred tax assets. This effect was partially offset by valuation allowance decreases in Austria and Italy due to improved profit forecasts.

Management believes it is more likely than not that the tax benefit associated with the Company's deferred tax assets, not offset by a valuation allowance, will be realized.

The following table summarizes the net operating loss carryforwards the Company had at December 31, 2017:

| **Jurisdiction** *(U.S. dollars in thousands)* | **Carryforward Amount** | **Gross Deferred Tax Asset** | **Valuation Allowance** | **Net Deferred Tax Asset** | **Expiration Period** |
|---|---|---|---|---|---|
| Australia | 60,565 | 18,169 | (18,166) | 3 | No Expiration |
| Austria | 33,483 | 8,371 | (837) | 7,534 | No Expiration |
| France | 110,615 | 28,904 | (28,657) | 247 | No Expiration |
| Germany | 177,587 | 49,764 | (32,566) | 17,198 | No Expiration |
| Spain | 103,822 | 11,479 | (11,186) | 293 | No Expiration |
| Switzerland (1) | 181,789 | 20,620 | (20,620) | — | 2018-2025 |
| U.K. | 228,444 | 42,612 | (31,913) | 10,699 | No Expiration |
| U.S. (2) | 305,771 | 64,212 | (1,179) | 63,033 | 2033-2037 |
| Other | 221,893 | 41,163 | (32,977) | 8,186 | Various |
| **Total Net Operating Loss Carryforwards** | 1,423,969 | 285,294 | (178,101) | 107,193 | |

(1) Net operating loss of $4.0 million and $31.8 million will expire in 2018 and 2019, respectively, with the remaining $146.0 million expiring through 2025.

(2) Approximately $47.0 million of the net operating loss carryforwards is subject to restrictions on timing and utilization under §382 of the IRS Code.

The following table summarizes, the net operating loss carryforwards the Company had at December 31, 2017:

| **Jurisdiction** *(U.S. dollars in thousands)* | **Carryforward Amount** | **Gross Deferred Tax Asset** | **Valuation Allowance** | **Net Deferred Tax Asset** | **Expiration Period** |
|---|---|---|---|---|---|
| Ireland | 122,142 | 30,536 | (30,536) | — | No Expiration |
| U.K. | 14,927 | 2,836 | (2,836) | — | No Expiration |
| U.S. (1) | 144,691 | 30,385 | (30,385) | — | 2018 - 2021 |
| **Total Capital Loss Carryforwards** | 281,760 | 63,757 | (63,757) | — | |

(1) Capital loss carryforwards of $41.2 million million will expire at the end of 2018 with another $103.5 million expiring in future years through 2021.

At December 31, 2017, the Company had total tax credits of $53.3 million comprised of : $31.7 million of U.S. Alternative Minimum Tax Credits, which are refundable no later than 2021; (2) $3.0 million of U.S. foreign tax credits that expire through 2021; (3) $3.1 million of U.S.Research and Development tax credits which expire through 2034; and (4) $15.5 million of U.K. foreign tax credits that do not expire.

For the years ended December 31, 2017 and 2016, the Company had unrecognized tax benefits of $65.0 million and $97.8 million, respectively. If recognized, the full amount of these unrecognized tax benefits would generally decrease the current year annual effective tax rate. The Company does not currently anticipate any significant change in unrecognized tax benefits during 2018.

The following table presents a reconciliation of the Company's unrecognized tax benefits:

| *(U.S. dollars in thousands)* | **2017** | **2016** |
|---|---|---|
| Unrecognized tax benefits, beginning of the year | $ 97,780 | $ 80,590 |
| Increases for tax positions taken during the year | 3,290 | 25,250 |
| Increases for tax positions taken in prior years | 15,940 | 11,700 |
| Decreases for tax positions taken in prior years | (35,230) | (6,440) |
| Decreases for settlement with taxing authorities | (16,320) | — |
| Decreases for lapse of the applicable statute of limitations | (500) | (13,320) |
| Unrecognized tax benefits, end of year | $ 64,960 | $ 97,780 |

The Company's policy is to recognize any interest and penalties related to unrecognized tax benefits as a component of tax expense. For the years ended December 31, 2017 and 2016 the Company had accrued interest and penalties of $3.8 million and $0.9 million, respectively.

## 23. Statutory Financial Data

The Company's ability to pay dividends or return capital from shareholders' equity is limited by applicable laws and regulations of the various jurisdictions in which the Company's principal operating subsidiaries operate, certain additional required regulatory approvals and financial covenants contained in the Company's credit facilities and other debt documents. The payment of dividends to XLB by the Company's principal operating subsidiaries is regulated under the laws of various jurisdictions including Bermuda, the U.K., Ireland and Switzerland and certain insurance statutes of various U.S. states in which the principal operating subsidiaries are domiciled and the other jurisdictions where the Company has regulated subsidiaries.

Statutory capital and surplus for the principal operating subsidiaries of the Company for the years ended December 31, 2017 and 2016 are summarized below:

| | **Bermuda (1)** | | **U.S. (2)** | | **U.K., Europe and Other** | |
|---|---|---|---|---|---|---|
| *(U.S. dollars in thousands)* | **2017** | **2016** | **2017** | **2016** | **2017** | **2016** |
| Required statutory capital and surplus | $ 6,431,266 | $ 6,351,874 | $ 821,442 | $ 822,651 | $ 4,551,068 | $ 4,320,140 |
| Actual statutory capital and surplus (3) | $ 11,454,639 | $ 12,333,870 | $ 2,347,380 | $ 2,362,827 | $ 5,711,162 | $ 5,201,602 |

(1) Required statutory capital and surplus at December 31, 2017 represents 100% Bermuda Solvency Capital Requirement ("BSCR") level for the Company, calculated on a consolidated basis (and therefore includes a BSCR requirement for all regions).
(2) Required statutory capital and surplus represents 100% Risk-Based Capital level for principal U.S. operating subsidiaries.
(3) Statutory assets in Bermuda include investments in other U.S. and international subsidiaries reported separately herein.

Statutory net income (loss) for the principal operating subsidiaries of the Company for the years ended December 31, 2017 and 2016 is summarized below:

| *(U.S. dollars in thousands)* | 2017 | 2016 |
|---|---|---|
| Bermuda | $ (309,220) | $ 724,711 |
| U.S. | $ (76,788) | $ 96,481 |
| U.K., Europe and Other | $ (335,422) | $ 366,708 |

The difference between statutory financial statements and statements prepared in accordance with GAAP varies by jurisdiction, however, the primary difference is that statutory financial statements do not reflect deferred policy acquisition costs, deferred income tax net assets, intangible assets, or unrealized appreciation on investments, but they do reflect any unauthorized/authorized reinsurance charges.

Certain restrictions on the payment of dividends from retained earnings by the Company's principal operating subsidiaries are further detailed below.

Management has evaluated the Company and principal operating subsidiaries' ability to maintain adequate levels of statutory capital, liquidity and rating agency capital and believes they will be able to do so. In performing this analysis, management has considered the most recent statutory capital position of each of the principal operating subsidiaries as well as the ability of the holding companies to allocate capital and liquidity around the group as and when needed.

**Bermuda Operations**

In early July 2008, the Insurance Amendment Act of 2008 was passed, which introduced a number of changes to the Bermuda Insurance Act 1978, such as allowing the BMA to prescribe standards for an enhanced capital requirement and a capital and solvency return with which insurers and reinsurers must comply. The BSCR employs a standard mathematical model that can relate more accurately the risks undertaken by (re)insurers to the capital that is dedicated to their business. Insurers and reinsurers may adopt the BSCR model or, where an insurer or reinsurer believes that its own internal model better reflects the inherent risk of its business, an in-house model approved by the BMA. Class 4 (re)insurers, such as the Company, were required to implement the new capital requirements under the BSCR model beginning with fiscal years ending on or after December 31, 2009. The Company's capital requirements for its Bermuda principal operating subsidiaries, XLB and Catlin-Bermuda, under the BSCR are highlighted in the aggregate in the table above. In addition to the BSCR based requirements, the BMA also prescribes minimum liquidity standards that must be met.

Under the Insurance Act 1978, amendments thereto and related regulations of Bermuda, Class 4 (re)insurers are prohibited from declaring or paying dividends of more than 25% of each of their prior year's statutory capital and surplus unless they file with the BMA an affidavit stating that the dividend has not caused the Class 4 (re)insurer to fail to meet its relevant margins. At December 31, 2017 and 2016, the maximum dividend that XLB's Bermuda Class 4 (re)insurers could pay, without a signed affidavit, having met minimum levels of statutory capital and surplus and liquidity requirements, was approximately $3.1 billion and $3.2 billion, respectively. No Class 4 (re)insurer may reduce its total statutory capital by 15% or more unless it has received the prior approval of the BMA, and it must also submit an affidavit stating that the proposed reduction will not cause it to fail to meet its minimum solvency margin or minimum liquidity ratio.

**U.S. Operations**

The Company has two lead property and casualty subsidiaries in the U.S., XLRA and Catlin Specialty Insurance Company ("CSIC"), which are domiciled in the States of New York and Delaware, respectively. Both XLRA and CSIC are the lead companies in their respective insurance pools. Including the pool leaders, these insurance pools include seven and three P&C companies, respectively. The Company also has another property and casualty subsidiary, T.H.E. Insurance Company ("THE"), a Louisiana-domiciled insurer which was acquired as part of the transaction described in Note 3(d), "Acquisitions, Disposals and Contribution from Parent - Allied Acquisition, and exists outside of the existing pools at December 31, 2016.

Unless permitted by the New York Superintendent of Financial Services, XLRA cannot declare or distribute any dividend to shareholders during any twelve month period that exceeds the lesser of 10 percent of XLRA's statutory policyholders' surplus or 100 percent of its "adjusted net investment income," as defined. The New York State insurance laws also provide that any distribution that is a dividend may only be paid out of statutory earned surplus. At December 31, 2017 and 2016, XLRA had negative statutory earned surplus of $138.9 million and an earned surplus of $66.9 million, respectively. At December 31, 2017, XLRA's statutory policyholders' surplus was $2.1 billion, and no dividends can be declared and paid in 2018 without prior regulatory approval. At December 31, 2017 and 2016, five and one, respectively, of the seven P&C members of the XLRA insurance pool had a negative statutory earned surplus.

Unless permitted by the Insurance Commissioner of the State of Delaware, CSIC cannot declare or distribute any dividend to shareholders during any twelve month period that exceeds the greater of 10 percent of statutory policyholders' surplus or 100 percent of net income excluding realized gains. The Delaware State insurance laws also provide that any distribution that is a dividend may only be paid out of statutory earned surplus. At December 31, 2017 and 2016, CSIC had a negative statutory earned surplus of $10.1 million, and an earned surplus of $3.4 million, respectively. At December 31, 2017, CSIC's statutory policyholders' surplus was $243.6 million, and no dividends can be declared and paid in 2018 without prior regulatory approval. At December 31, 2017, all three of the P&C members of the CSIC insurance pool had a negative statutory earned surplus.

Unless permitted by the Insurance Commissioner of the State of Louisiana, THE cannot declare or distribute any dividend to shareholders during any twelve month period that exceeds the greater of 10 percent of statutory policyholders' surplus or 100 percent of net income excluding realized gains. At December 31, 2017, THE's statutory policyholders' surplus was $53.3 million, and no dividends can be declared and paid in 2018 without regulatory approval.

**International Operations**

The Company's international principal operating subsidiaries prepare statutory financial statements based on local laws and regulations. Some jurisdictions impose enhanced regulatory requirements on insurance companies while other jurisdictions impose fewer requirements. In some countries, such subsidiaries must obtain licenses issued by governmental authorities to conduct local insurance business. These licenses may be subject to minimum reserves and minimum capital and solvency tests. Jurisdictions may impose fines, censure, and/or impose criminal sanctions for violation of regulatory requirements. The majority of the actual statutory capital outside of the U.S. and Bermuda is held in the U.K. ($1.2 billion at December 31, 2017), Switzerland ($1.6 billion at December 31, 2017) and Ireland ($1.0.billion at December 31, 2017). The Company also has approximately $1.9 billion of capital available, which is sufficient to meet Funds at Lloyd's requirements.

**Other Restrictions**

The ability to declare and pay dividends may also be restricted by financial covenants in the Company's credit facilities and other debt documents. The Company was in compliance with all covenants at December 31, 2017, and the Company remains in compliance.

**24. Subsequent Events**

XL Group Ltd ("XL"), the ultimate parent of the Company, has entered into a definitive agreement and plan of merger (the "Merger Agreement") with AXA SA ("AXA") dated March 5, 2018, under which AXA would acquire 100% of XL’s common shares in exchange for cash proceeds of $57.60 per common share or approximately $15.3 billion in the aggregate (the "AXA Transaction"). The Merger Agreement provides that, subject to the satisfaction or waiver of certain conditions set forth therein, XL will merge with an existing AXA subsidiary in accordance with the Companies Act 1981 of Bermuda (the "Merger"), with XL surviving the Merger as a wholly owned subsidiary of AXA. All preferred shares issued by subsidiaries of XL will remain issued and outstanding upon completion of the Merger.

The Merger is expected to close during the second half of 2018, subject to approval by the XL shareholders and other customary closing conditions, including the receipt of required regulatory approvals. The Merger Agreement, among other stipulations, permits: (i) XL to pay out regular quarterly cash dividends not to exceed $0.22 per XL common share per quarter, (ii) subsidiaries of XL to pay period cash dividends on preferred shares not to exceed amounts contemplated by the applicable bye-laws or resolutions approving such preferred shares, and (iii) subsidiaries of XL to pay dividends to XL or any subsidiary of XL.

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