

**Partner Reinsurance Company Ltd.**

**Consolidated Financial Statements and  
Independent Auditors' Report**

**December 31, 2017 and 2016**



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## Report of Independent Auditors

The Board of Directors and Shareholder  
Partner Reinsurance Company Ltd.

We have audited the accompanying consolidated financial statements of Partner Reinsurance Company Ltd. (the Company), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations and comprehensive income, shareholder's equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 entity'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 financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Partner Reinsurance Company Ltd. at December 31, 2017 and 2016, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

## **Other Matter**

Accounting principles generally accepted in the United States require that the incurred and paid claims development prior to the most recent year and the average annual percentage payout of incurred claims disclosed on pages 30 through 33 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Financial Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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, 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 financial statements, and other knowledge we obtained during our audit of the 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.

*Ernst & Young Ltd.*

Hamilton, Bermuda  
April 30, 2018

**Partner Reinsurance Company Ltd.**  
**Consolidated Balance Sheets**  
(Expressed in thousands of U.S. dollars, except parenthetical share data)

	December 31, 2017	December 31, 2016
<b>Assets</b>		
Investments:		
Fixed maturities, at fair value (amortized cost: 2017, \$4,139,730; 2016, \$5,484,627)	\$ 4,291,901	\$ 5,563,233
Short-term investments, at fair value (amortized cost: 2017, \$448; 2016, \$7,907)	448	7,904
Equities, at fair value (cost: 2017, \$531,162; 2016, \$28,217)	599,046	38,503
Other invested assets .....	992,888	874,758
<b>Total investments</b> .....	<b>5,884,283</b>	<b>6,484,398</b>
Cash and cash equivalents .....	585,066	1,025,917
Accrued investment income .....	39,675	45,086
Reinsurance balances receivable .....	1,526,602	1,146,726
Reinsurance recoverable on paid and unpaid losses .....	392,536	60,535
Funds held by reinsured companies .....	814,218	682,799
Deferred acquisition costs .....	406,153	297,927
Intercompany loans and balances receivable .....	870,969	336,837
Goodwill .....	26,014	26,014
Net tax assets .....	19,536	17,250
Other assets .....	4,433	4,866
<b>Total assets</b> .....	<b>\$ 10,569,485</b>	<b>\$ 10,128,355</b>
<b>Liabilities</b>		
Non-life reserves .....	\$ 4,606,631	\$ 3,668,786
Life and health reserves .....	1,323,795	1,089,238
Unearned premiums .....	1,023,319	745,939
Other reinsurance balances payable .....	143,543	138,012
Accounts payable, accrued expenses and other .....	152,575	655,987
<b>Total liabilities</b> .....	<b>7,249,863</b>	<b>6,297,962</b>
<b>Shareholder's Equity</b>		
Common shares (par value \$1.00; issued: 2017 and 2016, 3,000 shares) .....	3,000	3,000
Additional paid-in capital .....	1,515,898	1,515,898
Accumulated other comprehensive loss .....	(50,887)	(104,875)
Retained earnings .....	1,851,611	2,416,370
<b>Total shareholder's equity</b> .....	<b>3,319,622</b>	<b>3,830,393</b>
<b>Total liabilities and shareholder's equity</b> .....	<b>\$ 10,569,485</b>	<b>\$ 10,128,355</b>

*See accompanying Notes to Consolidated Financial Statements.*

**Partner Reinsurance Company Ltd.**  
**Consolidated Statements of Operations and Comprehensive Income**  
(Expressed in thousands of U.S. dollars)

	For the year ended December 31, 2017	For the year ended December 31, 2016
<b>Revenues</b>		
Gross premiums written.....	\$ 3,082,873	\$ 2,550,629
Net premiums written .....	\$ 2,919,727	\$ 2,386,231
(Increase) decrease in unearned premiums.....	(231,905)	24,365
Net premiums earned.....	2,687,822	2,410,596
Net investment income .....	158,455	205,931
Interest income on intercompany loans .....	6,053	10,000
Net realized and unrealized investment gains .....	194,211	33,505
Other income .....	5,047	6,939
<b>Total revenues.....</b>	<b>3,051,588</b>	<b>2,666,971</b>
<b>Expenses</b>		
Losses and loss expenses .....	2,168,911	1,514,370
Acquisition costs.....	736,335	687,005
Other operating expenses.....	33,579	41,313
Net foreign exchange losses (gains) .....	250,965	(150,318)
<b>Total expenses.....</b>	<b>3,189,790</b>	<b>2,092,370</b>
<b>(Loss) income before taxes and interest in earnings (losses) of equity investments .</b>	<b>(138,202)</b>	<b>574,601</b>
Income tax expense.....	1,465	3,440
Interest in earnings (losses) of equity investments .....	74,908	(34,214)
<b>Net (loss) income .....</b>	<b>\$ (64,759)</b>	<b>\$ 536,947</b>
Net income attributable to noncontrolling interests.....	—	(119)
<b>Net (loss) income attributable to Partner Reinsurance Company Ltd.....</b>	<b>\$ (64,759)</b>	<b>\$ 536,828</b>
<b>Comprehensive (loss) income</b>		
Net (loss) income attributable to Partner Reinsurance Company Ltd. ....	\$ (64,759)	\$ 536,828
Change in currency translation adjustment.....	53,988	(66,772)
<b>Comprehensive (loss) income attributable to Partner Reinsurance Company Ltd.</b>	<b>\$ (10,771)</b>	<b>\$ 470,056</b>

*See accompanying Notes to Consolidated Financial Statements.*

**Partner Reinsurance Company Ltd.**  
**Consolidated Statements of Shareholder's Equity**  
(Expressed in thousands of U.S. dollars)

	For the year ended December 31, 2017	For the year ended December 31, 2016
<b>Common shares</b>		
Balance at beginning and end of year.....	\$ 3,000	\$ 3,000
<b>Additional paid-in capital</b>		
Balance at beginning of year .....	1,515,898	1,517,097
Stock compensation expense .....	—	(1,199)
Balance at end of year.....	1,515,898	1,515,898
<b>Accumulated other comprehensive loss</b>		
Currency translation adjustment:		
Balance at beginning of year .....	(104,875)	(38,103)
Change in currency translation adjustment.....	53,988	(66,772)
Balance at end of year.....	(50,887)	(104,875)
<b>Retained earnings</b>		
Balance at beginning of year .....	2,416,370	2,002,542
Net (loss) income.....	(64,759)	536,947
Dividends on common shares.....	(500,000)	(123,000)
Net income attributable to noncontrolling interests.....	—	(119)
Balance at end of year.....	1,851,611	2,416,370
<b>Total shareholder's equity</b> .....	<b>\$ 3,319,622</b>	<b>\$ 3,830,393</b>

*See accompanying Notes to Consolidated Financial Statements.*

**Partner Reinsurance Company Ltd.**  
**Consolidated Statements of Cash Flows**  
**(Expressed in thousands of U.S. dollars)**

	For the year ended December 31, 2017	For the year ended December 31, 2016
<b>Cash flows from operating activities</b>		
Net (loss) income .....	\$ (64,759)	\$ 536,947
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred gains .....	11,023	(4,618)
Amortization of net discount on investments .....	(9,168)	21,900
Net realized and unrealized investment gains .....	(194,211)	(33,505)
Changes in:		
Reinsurance balances, net .....	(296,410)	(60,724)
Reinsurance recoverable on paid and unpaid losses, net of ceded premiums payable .....	(332,477)	6,959
Funds held by reinsured companies .....	(53,194)	(23,099)
Deferred acquisition costs .....	(84,311)	6,205
Net tax assets and liabilities .....	(2,824)	(4,220)
Unpaid losses and loss expenses including life policy benefits .....	852,447	148,555
Unearned premiums .....	231,905	(24,365)
Other net changes in operating assets and liabilities .....	177,063	(102,333)
<b>Net cash provided by operating activities</b>	<b>235,084</b>	<b>467,702</b>
<b>Cash flows from investing activities</b>		
Sales of fixed maturities .....	5,939,998	5,124,019
Redemptions of fixed maturities .....	172,103	222,762
Purchases of fixed maturities .....	(5,224,704)	(4,831,707)
Sales and redemptions of short-term investments .....	83,880	50,198
Purchases of short-term investments .....	(74,636)	(48,547)
Sales of equities .....	8,628	142,569
Purchases of equities .....	(516,207)	(3,216)
Net intercompany balances receivable <sup>(1)</sup> .....	(949,050)	640,955
Investments in other invested assets .....	13,753	(550,881)
Other, net .....	126,680	(36,715)
<b>Net cash (used in) provided by investing activities</b>	<b>(419,555)</b>	<b>709,437</b>
<b>Cash flows from financing activities</b>		
Cash dividends paid to Parent <sup>(1)</sup> .....	(77,933)	—
Payments on behalf of Parent .....	(191,453)	(648,197)
Distributions to noncontrolling interests .....	—	(2,569)
<b>Net cash used in financing activities</b>	<b>(269,386)</b>	<b>(650,766)</b>
<b>Effect of foreign exchange rate changes on cash</b> .....	<b>13,006</b>	<b>(42,692)</b>
<b>(Decrease) increase in cash and cash equivalents</b> .....	<b>(440,851)</b>	<b>483,681</b>
<b>Cash and cash equivalents—beginning of year</b> .....	<b>1,025,917</b>	<b>542,236</b>
<b>Cash and cash equivalents—end of year</b> .....	<b>\$ 585,066</b>	<b>\$ 1,025,917</b>
<b>Supplemental cash flow information:</b>		
Taxes paid .....	\$ 4,290	\$ 15,273

(1) The Company declared non-cash dividends to its Parent, PartnerRe Ltd., of \$422 million and \$123 million for the years ended December 31, 2017 and 2016, respectively. These dividends were paid by a reduction of intercompany loans and balances receivable.

*See accompanying Notes to Consolidated Financial Statements.*

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements**

## **1. Organization**

Partner Reinsurance Company Ltd. (the Company) is a 100% owned subsidiary of PartnerRe Ltd. (the Parent). The Parent is a wholly-owned subsidiary of EXOR Nederland N.V. and, as such, a subsidiary of the ultimate parent company, EXOR N.V. The Company commenced operations in November 1993.

The Company predominantly provides reinsurance and certain specialty insurance lines on a worldwide basis. Non-life risks reinsured include agriculture, aviation/space, casualty, catastrophe, energy, engineering, financial risks, marine, motor, multiline, and property. Life and health risks include mortality, longevity, and accident and health. Reinsurance of alternative risk products include weather and credit protection to financial, industrial and service companies on a worldwide basis. The Company also enters into reinsurance contracts with subsidiaries of the Parent, including a 65% quota-share agreement from Partner Reinsurance Europe SE (PartnerRe Europe); a 50% quota-share agreement from Partner Reinsurance Asia Pte. Ltd (PartnerRe Asia), and a 45% quota-share agreement from Partner Reinsurance Company of the U.S. (PartnerRe U.S.) (see Note 16).

On March 18, 2016, following receipt of regulatory approvals, the Parent's publicly held common shares were acquired by Exor N.V., a subsidiary of EXOR S.p.A., one of Europe's leading investment companies controlled by the Agnelli family. In October 2016, Exor N.V. changed its name to EXOR Nederland N.V. In December 2016, EXOR S.p.A. merged with and into EXOR HOLDING N.V., a newly formed entity organized in the Netherlands and, in conjunction with the merger, EXOR HOLDING N.V. changed its name to EXOR N.V. EXOR N.V. is listed on the Milan Stock Exchange.

As a result of the acquisition, the Parent's publicly issued common shares were cancelled and are no longer traded on the NYSE. The Parent's preferred shares continue to be traded on the NYSE.

On April 3, 2017, after receiving regulatory approvals, the Parent completed the acquisition of 100% of the outstanding ordinary shares of Aurigen Capital Limited (Aurigen), a North American life reinsurance company. This acquisition enables the Parent to expand its life reinsurance footprint in Canada and the U.S. with limited overlap in market coverage.

## **2. Significant Accounting Policies**

The Company's Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The Consolidated Financial Statements include the accounts of the Company and its subsidiaries. Intercompany accounts and transactions have been eliminated.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. While management believes that the amounts included in the Consolidated Financial Statements reflect its best estimates and assumptions, actual results could differ from those estimates. The Company's principal estimates include:

- Non-life reserves;
- Life and health reserves;
- Gross and net premiums written and net premiums earned;
- Recoverability of deferred acquisition costs;
- Recoverability of deferred tax assets;
- Valuation of certain assets and derivative financial instruments that are measured using significant unobservable inputs.; and
- Valuation of goodwill.



**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

The following are the Company's significant accounting policies:

***(a) Premiums***

Gross premiums written and earned are based upon reports received from ceding companies, supplemented by the Company's own estimates of premiums written and earned for which ceding company reports have not been received. The determination of premium estimates requires a review of the Company's experience with cedants, familiarity with each market, an understanding of the characteristics of each line of business and management's assessment of the impact of various other factors on the volume of business written and ceded to the Company. Premium estimates are updated as new information is received from cedants and differences between such estimates and actual amounts are recorded in the period in which the estimates are changed or the actual amounts are determined. Net premiums written and earned are presented net of ceded premiums, which represent the cost of retrocessional protection purchased by the Company. Premiums are earned on a basis that is consistent with the risks covered under the terms of the reinsurance contracts, which is generally one to two years. For U.S. and European wind and certain other risks, premiums are earned commensurate with the seasonality of the underlying exposure. Reinstatement premiums are recognized as written and earned at the time a loss event occurs, where coverage limits for the remaining life of the contract are reinstated under pre-defined contract terms. The accrual of reinstatement premiums is based on management's estimate of losses and loss expenses associated with the loss event. Unearned premiums represent the portion of premiums written which is applicable to the unexpired risks under contracts in force.

Premiums related to individual life and annuity business are recorded over the premium-paying period on the underlying policies. Premiums on annuity and universal life contracts for which there is no significant mortality or critical illness risk are accounted for in a manner consistent with accounting for interest-bearing financial instruments and are not reported as revenues, but rather as direct deposits to the contract. Amounts assessed against annuity and universal life policyholders are recognized as revenue in the period assessed.

***(b) Losses and Loss Expenses and Non-life and Life and Health Reserves***

The reserves for non-life business include amounts determined from loss reports on individual treaties (case reserves), additional case reserves when the Company's loss estimate is higher than reported by the cedants (ACRs) and amounts for losses incurred but not yet reported to the Company (IBNR). Such reserves are estimated by management based upon reports received from ceding companies, supplemented by the Company's own actuarial estimates of reserves for which ceding company reports have not been received, and based on the Company's own historical experience. To the extent that the Company's own historical experience is inadequate for estimating reserves, such estimates may be determined based upon industry experience and management's judgment. The estimates are continually reviewed and the ultimate liability may be in excess of, or less than, the amounts provided. Any adjustments are reflected in the periods in which they are determined, which may affect the Company's operating results in future periods.

The life and health reserves have been established based upon information reported by ceding companies, supplemented by the Company's actuarial estimates, which for life include mortality, critical illness, persistency and future investment income, with appropriate provision to reflect uncertainty. Future policy benefit reserves for annuity and universal life contracts are carried at their accumulated values. Reserves for policy claims and benefits include both mortality and critical illness claims in the process of settlement, and claims that have been incurred but not yet reported.

The Company purchases retrocessional contracts to reduce its exposure to risk of losses on reinsurance assumed. Reinsurance recoverable on paid and unpaid losses involves actuarial estimates consistent with those used to establish the associated liabilities for non-life and life and health reserves.

***(c) Deferred Acquisition Costs***

Acquisition costs, comprising incremental brokerage fees, commissions and excise taxes, which vary directly with, and are related to, the acquisition of reinsurance contracts, are capitalized and charged to expense as the related premium is earned. All other acquisition related costs, including indirect costs, are expensed as incurred.

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

Acquisition costs related to individual life and annuity contracts are deferred and amortized over the premium-paying periods in proportion to anticipated premium income, allowing for lapses, terminations and anticipated investment income. Acquisition costs related to universal life and single premium annuity contracts for which there is no significant mortality or critical illness risk are deferred and amortized over the lives of the contracts as a percentage of the estimated gross profits expected to be realized on the contracts.

The Company establishes a premium deficiency reserve to the extent the deferred acquisition costs are insufficient to cover the excess of expected losses and loss expenses, settlement costs and deferred acquisition costs over the related unearned premiums.

Actual and anticipated losses and loss expenses, other costs, and investment income related to underlying premiums are considered in determining the recoverability of deferred acquisition costs for the Company's short-duration contracts. Actual and anticipated loss experience, together with the present value of future gross premiums, the present value of future benefits, and settlement and maintenance costs are considered in determining the recoverability of deferred acquisition costs related to the Company's Life business.

***(d) Funds Held by Reinsured Companies (Cedants)***

The Company writes certain business on a funds held basis. Under such contractual arrangements, the cedant retains the premiums that would have otherwise been paid to the Company and the Company earns interest on these funds. The Company generally earns investment income on the funds held balances based upon a predetermined interest rate, either fixed contractually at the inception of the contract or based upon a recognized index (e.g. LIBOR). However, in certain circumstances, the Company may receive an investment return based upon either the result of a pool of assets held by the cedant, generally used to collateralize the funds held balance, or the investment return earned by the cedant on its entire investment portfolio. In these arrangements, gross investment returns are typically reflected in net investment income with a corresponding increase or decrease (net of a spread) being recorded in losses and loss expenses in the Company's Consolidated Statements of Operations. In these arrangements, the Company is exposed, to a limited extent, to the underlying credit risk of the pool of assets inasmuch as the underlying life policies may have guaranteed minimum returns. In such cases, an embedded derivative exists and its fair value is recorded by the Company as an increase or decrease to the funds held balance.

***(e) Deposit Assets and Liabilities***

In the normal course of its operations, the Company writes certain contracts that do not meet the risk transfer provisions of U.S. GAAP. While these contracts do not meet risk transfer provisions for accounting purposes, there is a remote possibility that the Company will suffer a loss. The Company accounts for these contracts using the deposit accounting method, originally recording deposit liabilities for an amount equivalent to the consideration received. The consideration to be retained by the Company, irrespective of the experience of the contracts, is earned over the expected settlement period of the contracts, with any unearned portion recorded as a component of deposit liabilities. Actuarial studies are used to estimate the final liabilities under these contracts and the appropriate accretion rates to increase or decrease the liabilities over the term of the contracts. The change for the period is recorded in other income or loss in the Consolidated Statements of Operations.

Under some of these contracts, cedants retain the assets on a funds-held basis. In those cases, the Company records those assets as deposit assets and records the related income in net investment income in the Consolidated Statements of Operations.

***(f) Investments***

The Company elects the fair value option for its fixed maturities, short-term investments, equities and certain other invested assets (except for those that are accounted for using the cost or equity methods of accounting). All changes in the fair value of investments are recorded in net realized and unrealized investment gains or losses in the Consolidated

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

Statements of Operations. The Company defines fair value as the price received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company measures the fair value of financial instruments according to a fair value hierarchy that prioritizes the information used to measure fair value into three broad levels. The Company's policy is to recognize transfers between the hierarchy levels at the beginning of the period. Short-term investments comprise securities with a maturity greater than three months but less than one year from the date of purchase.

Investments in real estate are recorded at cost less accumulated depreciation. Real estate assets held for investment are reviewed for impairment at least annually, or more frequently when events or changes in circumstances indicate the carrying value may not be recoverable and exceeds its estimated fair value.

Other invested assets consist primarily of investments in non-publicly traded companies, private placement equity and fixed maturity investments, corporate loans, derivative financial instruments and other specialty asset classes. Non-publicly traded entities in which the Company has significant influence, including an ownership of more than 20% and less than 50% of the voting shares, and limited partnerships in which the Company has more than a minor interest (typically more than 3 to 5%), are accounted for using either the equity method or the fair value option. Corporate loans are recorded under the fair value option. The remaining other invested assets are recorded at fair value or cost depending on the nature of the assets. The valuation techniques used by the Company are generally commensurate with standard valuation techniques for each asset class.

Net investment income includes interest and dividend income, amortization of premiums and discounts on fixed maturities and short-term investments, rental income on investments in real estate as well as investment income on funds held and funds held-directly managed, and is net of investment expenses and withholding taxes. Investment income is recognized when earned. Realized gains or losses on the disposal of investments are determined on a first-in, first-out basis. Investment purchases and sales are recorded on a trade-date basis.

***(g) Cash and Cash Equivalents***

Cash equivalents are carried at fair value and include fixed income securities that, at purchase, have a maturity of three months or less.

***(h) Goodwill***

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a historical acquisition by PartnerRe Europe, which was re-allocated from PartnerRe Europe to the Company during 2012. The Company assesses the appropriateness of its valuation of goodwill on at least an annual basis or more frequently if events or changes in circumstances indicate that the carrying amount may not be recoverable. If, as a result of the assessment, the Company determines that the value of its goodwill is impaired, goodwill will be written down in the period in which the determination is made. In 2016, the Company changed its annual impairment testing date from September 30 to December 31, primarily due to the key inputs and assumptions used to assess the fair value of reporting units being based on the Company's annual business plan which is approved by the Parent's Board in November each year.

***(i) Income Taxes***

Certain subsidiaries and branches of the Company operate in jurisdictions where they are subject to taxation. Current and deferred income taxes are charged or credited to net income or loss or, in certain cases, to accumulated other comprehensive income or loss, based upon enacted tax laws and rates applicable in the relevant jurisdiction in the period in which the tax becomes accruable or realizable. Deferred income taxes are provided for all temporary differences between the bases of assets and liabilities used in the Consolidated Balance Sheets and those used in the various jurisdictional tax returns. When management's assessment indicates that it is more likely than not that deferred tax assets will not be realized, a valuation allowance is recorded against the deferred tax assets.

The Company recognizes a tax benefit relating to uncertain tax positions only where the position is more likely than not to be sustained assuming examination by tax authorities. A liability is recognized for any tax benefit (along with any

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

interest and penalty, if applicable) claimed in a tax return in excess of the amount recognized in the financial statements under U.S. GAAP. Any changes in amounts recognized are recorded in the period in which they are determined.

***(j) Translation of Foreign Currencies***

The reporting currency of the Company is the U.S. dollar. The functional currency of the Company's subsidiaries and branches is the U.S. dollar, except for its wholly owned subsidiary, Partner Reinsurance Life Company of Bermuda Ltd., and its Canadian Life branch (Canadian branch), whose functional currencies are the Canadian dollar, and its wholly owned subsidiary, Partner Re Corporate Member Limited, whose functional currency is the British Pound. In translating the financial statements of these subsidiaries and branch, assets and liabilities are converted into U.S. dollars using the rates of exchange in effect at the balance sheet dates, and revenues and expenses are converted using the average foreign exchange rates for the period. The effect of translation adjustments is reported in the Consolidated Balance Sheets as a currency translation adjustment, a separate component of accumulated other comprehensive loss.

In recording foreign currency transactions, revenue and expense items are converted into the functional currency at the average rates of exchange for the period. Assets and liabilities originating in currencies other than the functional currency are translated into the functional currency at the rates of exchange in effect at the balance sheet dates. The resulting foreign exchange gains or losses are included in net foreign exchange gains and losses in the Consolidated Statements of Operations.

***(k) Derivatives***

*Derivatives Used in Hedging Activities*

The Company utilizes derivative financial instruments as part of its overall currency risk management strategy. The Company recognizes all derivative financial instruments, including embedded derivative instruments, as either assets or liabilities in the Consolidated Balance Sheets and measures those instruments at fair value. On the date the Company enters into a derivative contract, Management designates whether the derivative is to be used as a hedge of an identified underlying exposure (a designated hedge). The accounting for gains and losses associated with changes in the fair value of a derivative and the effect on the Consolidated Financial Statements depends on its hedge designation and whether the hedge is highly effective in achieving offsetting changes in the fair value of the asset or liability being hedged.

The derivatives employed by the Company to hedge currency exposure related to fixed income securities and other reinsurance assets and liabilities are not designated as hedges. The changes in fair value of these derivatives not designated as hedges are recognized in net foreign exchange gains and losses in the Consolidated Statements of Operations.

*Other Derivatives*

The Company's investment strategy allows for the use of derivative instruments, subject to strict limitations. The Company utilizes various derivative instruments such as foreign exchange forward contracts, foreign currency option contracts, futures contracts, to-be-announced mortgage-backed securities (TBAs) and credit default swaps for the purpose of managing overall currency risk, market exposures and portfolio duration, for hedging certain investments, or for enhancing investment performance that would be allowed under the Company's investment policy if implemented in other ways. These instruments are recorded at fair value as assets and liabilities in the Consolidated Balance Sheets. Changes in fair value are included in net realized and unrealized investment gains or losses in the Consolidated Statements of Operations, except changes in the fair value of foreign currency option contracts and foreign exchange forward contracts which are included in net foreign exchange gains or losses in the Consolidated Statements of Operations. Margin balances required by counterparties, which are equal to a percentage of the total value of open futures contracts, are included in cash and cash equivalents.

The Company enters from time to time into weather and longevity related transactions that are structured as derivatives, which are recorded at fair value with the changes in fair value reported in net realized and unrealized investment gains or losses in the Consolidated Statements of Operations.

The Company enters from time to time into total return and interest rate swaps. Margins related to these swaps are included in other income or loss in the Consolidated Statements of Operations and any changes in the fair value of the swaps are included in net realized and unrealized investment gains or losses in the Consolidated Statements of Operations.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

***(l) Variable Interest Entities and Noncontrolling Interests***

The Company is involved in the normal course of business with variable interest entities (VIEs). An assessment is performed as of the date the Company becomes initially involved in the VIE followed by a reassessment upon certain events related to its involvement in the VIE. The Company consolidates a VIE when it is the primary beneficiary having a controlling financial interest as a result of having the power to direct the activities that most significantly impact the economic performance of the VIE and the obligation to absorb losses, or right to receive benefits, that could potentially be significant to the VIE.

The Company has also formed a subsidiary with other third party investors, Lorenz Re Ltd. (Lorenz Re), that is considered to be a VIE. At inception, the Company determined that it was the primary beneficiary as it has the power to direct and had more than an insignificant economic interest in the activities of Lorenz Re. From inception until April 22, 2016 Lorenz Re was consolidated by the Company and all inter-company balances and transactions were eliminated and the net income or loss and shareholders' equity attributable to Lorenz Re's third party investors are recorded in the Consolidated Financial Statements as noncontrolling interests (see Note 9).

***(m) Recent Accounting Pronouncements***

In August 2017, the Financial Accounting Standards Board (FASB) issued updated guidance on accounting for hedging activities. This update expands and refines hedge accounting for both nonfinancial and financial risk components and aligns the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. The amendments also make certain targeted improvements to simplify the application of hedge accounting guidance and ease the administrative burden of hedge documentation requirements and for assessing hedge effectiveness. The guidance is effective for annual periods beginning after December 15, 2019, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on its Consolidated Financial Statements and disclosures.

In January 2017, the FASB issued updated guidance on the accounting for goodwill impairment. This update removes the second step of the goodwill impairment test and requires entities to apply a one-step quantitative test and record the amount of goodwill impairment as the excess of a reporting unit's carrying amount over its fair value, not to exceed the total amount of goodwill allocated to the reporting unit. The new guidance does not amend the optional qualitative assessment of goodwill impairment. The guidance is effective for annual impairment tests performed after December 15, 2020, with early adoption permitted. The Company does not expect the adoption of this guidance to have a significant impact on its Consolidated Financial Statements and disclosures.

In March 2017, the FASB issued updated guidance on presentation of net periodic pension cost and net periodic postretirement benefit cost. This update requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the employees during the period. It also requires the other components of net periodic pension cost and net periodic post retirement benefit cost to be presented in income separately from the service cost component. Additionally, only the service cost component is eligible for capitalization, when applicable. The guidance is effective for annual periods beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on its Consolidated Financial Statements and disclosures.

In February 2016, the FASB issued updated guidance on the accounting for leases. This update requires the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance and expands required disclosures. The guidance is effective for annual periods beginning after December 15, 2019, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on its Consolidated Financial Statements and disclosures.

In August 2016, the FASB issued updated guidance on the classification of certain cash receipts and payments. This update addresses the presentation and classification of certain cash receipts and cash payments in the statement of cash flows. The guidance is effective for fiscal periods beginning after December 15, 2018, with early adoption permitted. The adoption of this guidance for the year ended December 31, 2019 is not expected to have a significant impact on the Company's Consolidated Financial Statements.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

In October 2016, the FASB issued updated guidance on income taxes with respect to intra-entity transfers of assets. This update requires recognition of the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. The guidance is effective for fiscal periods beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on the Company's Consolidated Financial Statements. The adoption of this guidance for the year ended December 31, 2019 is not expected to have a significant impact on the Company's Consolidated Financial Statements.

In October 2016, the FASB issued updated guidance on consolidation with respect to interests held through related parties that are under common control. This update requires that a reporting entity, in determining whether it satisfies the primary beneficiary criteria, include all of its direct variable interests in a VIE as well as its indirect variable interests on a proportionate basis in a VIE held through related parties, including related parties that are under common control with the reporting entity. The guidance is effective for fiscal years beginning after December 15, 2016, with early adoption permitted. The adoption of this guidance on January 1, 2017 did not have a significant impact on the Company's Consolidated Financial Statements and disclosures.

### **3. Fair Value**

#### ***(a) Fair Value of Financial Instrument Assets***

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value by maximizing the use of observable inputs and minimizing the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing an asset or liability based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company's assumptions about what market participants would use in pricing the asset or liability based on the best information available in the circumstances. The level in the hierarchy within which a given fair value measurement falls is determined based on the lowest level input that is significant to the measurement.

The Company determines the appropriate level in the hierarchy for each financial instrument that it measures at fair value. In determining fair value, the Company uses various valuation approaches, including market, income and cost approaches. The hierarchy is broken down into three levels based on the observability of inputs as follows:

- Level 1 inputs—Unadjusted, quoted prices in active markets for identical assets or liabilities that the Company has the ability to access.

The Company's financial instruments that it measures at fair value using Level 1 inputs generally include: equities and exchange traded derivatives, including futures that are actively traded.

- Level 2 inputs—Quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets and significant directly or indirectly observable inputs, other than quoted prices, used in industry accepted models.

The Company's financial instruments that it measures at fair value using Level 2 inputs generally include: U.S. government issued bonds; U.S. government sponsored enterprises bonds; U.S. state, territory and municipal entities bonds; non-U.S. sovereign government, supranational and government related bonds; investment grade and high yield corporate bonds; asset-backed securities; mortgage-backed securities; short-term investments; certain common and preferred equities; notes and loans receivable; foreign exchange forward contracts and over-the-counter derivatives such as interest rate swaps and TBAs.

- Level 3 inputs—Unobservable inputs.

The Company's financial instruments that it measures at fair value using Level 3 inputs generally include: inactively traded fixed maturities including U.S. state, territory and municipal bonds; special purpose financing asset-backed bonds; unlisted or private equities; certain other mutual fund or exchange traded fund equities; notes and loan receivables; notes securitizations; and certain other derivatives, including inactively traded weather derivatives; longevity insurance-linked securities and total return swaps included in other invested assets.

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

At December 31, 2017 and 2016, the Company's financial instruments measured at fair value were categorized between Levels 1, 2 and 3 as follows (in thousands of U.S. dollars):

December 31, 2017	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Fixed maturities				
U.S. government and government sponsored enterprises.....	\$ —	\$ 615,788	\$ —	\$ 615,788
U.S. states, territories and municipalities .....	—	—	128,806	128,806
Non-U.S. sovereign government, supranational and government related .....	—	468,028	—	468,028
Corporate .....	—	2,706,018	—	2,706,018
Asset-backed securities.....	—	22,187	20,738	42,925
Residential mortgage-backed securities .....	—	330,336	—	330,336
Fixed maturities.....	\$ —	\$ 4,142,357	\$ 149,544	\$ 4,291,901
Short-term investments.....	\$ —	\$ 448	\$ —	\$ 448
Equities				
Finance.....		—	21,792	\$ 21,792
Technology .....		—	10,960	\$ 10,960
Insurance.....	\$ —	\$ 7,558	\$ —	\$ 7,558
Mutual funds and exchange traded funds .....			558,736	558,736
Equities	\$ —	\$ 7,558	\$ 591,488	\$ 599,046
Other invested assets				
Derivative assets				
Foreign exchange forward contracts .....	—	5,726	—	5,726
Insurance-linked securities.....	—	—	11,985	11,985
Futures contracts .....	3,367	—	—	3,367
Total return swaps .....	—	—	2,505	2,505
TBAs .....		81	—	81
Other				
Notes and loan receivables and notes securitization .....	—	3,425	108,563	111,988
Private equities.....	—	—	213,038	213,038
Derivative liabilities				
Interest rate swaps.....	—	(12,298)	—	(12,298)
Foreign exchange forward contracts .....	—	(15,215)	—	(15,215)
Total return swaps.....	—	—	(3,269)	(3,269)
TBAs .....	—	(64)	—	(64)
Other invested assets .....	\$ 3,367	\$ (18,345)	\$ 332,822	\$ 317,844
Total.....	\$ 3,367	\$ 4,132,018	\$ 1,073,854	\$ 5,209,239

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

December 31, 2016	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Fixed maturities				
U.S. government and government sponsored enterprises.....	\$ —	\$ 1,589,944	\$ —	\$ 1,589,944
U.S. states, territories and municipalities .....	—	—	123,827	123,827
Non-U.S. sovereign government, supranational and government related .....	—	335,633	—	335,633
Corporate .....	—	2,762,886	—	2,762,886
Asset-backed securities.....	—	24,709	27,684	52,393
Residential mortgage-backed securities .....	—	698,550	—	698,550
Other mortgage-backed securities .....	—	—	—	0
Fixed maturities .....	\$ —	\$ 5,411,722	\$ 151,511	\$ 5,563,233
Short-term investments.....	\$ —	\$ 7,904	\$ —	\$ 7,904
Equities				
Finance.....	973	4,959	20,817	\$ 26,749
Technology .....	\$ —	—	9,800	\$ 9,800
Insurance.....	\$ —	\$ 1,800	\$ —	\$ 1,800
Mutual funds and exchange traded funds .....	—	—	154	154
Equities .....	\$ 973	\$ 6,759	\$ 30,771	\$ 38,503
Other invested assets				
Derivative assets				
Foreign exchange forward contracts .....	—	5,263	—	5,263
Insurance-linked securities.....	—	—	10,130	10,130
Total return swaps .....	—	—	1,989	1,989
TBAs .....	—	342	—	342
Other				
Notes and loan receivables and notes securitization .....	—	1,500	141,693	143,193
Private equities .....	—	—	174,855	174,855
Derivative liabilities				
Interest rate swaps.....	—	(13,402)	—	(13,402)
Insurance-linked securities.....	—	—	(97)	(97)
Foreign exchange forward contracts .....	—	(6,122)	—	(6,122)
Total return swaps .....	—	—	(3,217)	(3,217)
TBAs .....	—	(57)	—	(57)
Other invested assets .....	\$ —	\$ (12,476)	\$ 325,353	\$ 312,877
Total.....	\$ 973	\$ 5,413,909	\$ 507,635	\$ 5,922,517

At December 31, 2017 and 2016, the aggregate carrying amounts of items included in other invested assets that the Company did not measure at fair value were \$675.0 million and \$561.9 million, respectively, which related to the Company's investments that are accounted for using the cost method of accounting or equity method of accounting.

At December 31, 2017 and 2016, substantially all of the accrued investment income in the Consolidated Balance Sheets related to the Company's investments for which the fair value option was elected.

During the years ended December 31, 2017 and 2016, there were no transfers between Level 1 and Level 2.

Disclosures about the fair value of financial instruments that the Company does not measure at fair value exclude insurance contracts and certain other financial instruments. At December 31, 2017 and 2016, the fair values of financial instrument assets recorded in the Consolidated Balance Sheets not described above, approximate their carrying values.



**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

The reconciliations of the beginning and ending balances for all financial instruments measured at fair value using Level 3 inputs for the years ended December 31, 2017 and 2016, were as follows (in thousands of U.S. dollars):

<b>For the year ended December 31, 2017</b>	<b>Balance at beginning of year</b>	<b>Realized and unrealized investment gains (losses) included in net income</b>	<b>Purchases and issuances <sup>(1)</sup></b>	<b>Settlements and sales <sup>(2)</sup></b>	<b>Net transfers into/ (out of) Level 3</b>	<b>Balance at end of year</b>	<b>Change in unrealized investment gains (losses) relating to assets held at end of year</b>
Fixed maturities							
U.S. states, territories and municipalities .....	\$ 123,827	\$ 5,804	\$ —	\$ (825)	\$ —	\$ 128,806	\$ 5,804
Asset-backed securities.....	27,684	1,327	—	(8,273)	—	20,738	1,316
Fixed maturities.....	<u>\$ 151,511</u>	<u>\$ 7,131</u>	<u>\$ —</u>	<u>\$ (9,098)</u>	<u>\$ —</u>	<u>\$ 149,544</u>	<u>\$ 7,120</u>
Equities							
Finance.....	\$ 20,817	\$ 975	\$ —	\$ —	\$ —	\$ 21,792	\$ 858
Technology .....	9,800	1,610	—	(450)	—	10,960	1,611
Mutual funds and exchange traded funds.....	154	51,475	507,250	(143)	—	558,736	51,486
Equities.....	<u>\$ 30,771</u>	<u>\$ 54,060</u>	<u>\$ 507,250</u>	<u>\$ (593)</u>	<u>\$ —</u>	<u>\$ 591,488</u>	<u>\$ 53,955</u>
Other invested assets							
Derivatives, net.....	\$ 8,805	\$ 5,977	\$ 1,793	\$ (5,354)	\$ —	\$ 11,221	\$ 3,231
Notes and loan receivables and notes securitization ...	141,693	2,744	2,040	(37,914)	—	108,563	6,977
Private equities .....	174,855	38,907	14,633	(15,357)	—	213,038	36,996
Other invested assets .....	<u>\$ 325,353</u>	<u>\$ 47,628</u>	<u>\$ 18,466</u>	<u>\$ (58,625)</u>	<u>\$ —</u>	<u>\$ 332,822</u>	<u>\$ 47,204</u>
Total.....	<u>\$ 507,635</u>	<u>\$ 108,819</u>	<u>\$ 525,716</u>	<u>\$ (68,316)</u>	<u>\$ —</u>	<u>\$ 1,073,854</u>	<u>\$ 108,279</u>

(1) There were no issuances.

(2) Settlements and sales of fixed maturities, equities and other invested assets include sales of \$nil, \$0.6 million and \$nil, respectively.

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

<b>For the year ended December 31, 2016</b>	<b>Balance at beginning of year</b>	<b>Realized and unrealized gains (losses) included in net income</b>	<b>Purchases and issuances <sup>(1)</sup></b>	<b>Settlements and sales <sup>(2)</sup></b>	<b>Net transfers into/ (out of) Level 3</b>	<b>Balance at end of year</b>	<b>Change in unrealized investment gains (losses) relating to assets held at end of year</b>
Fixed maturities							
U.S. states, territories and municipalities .....	\$ 138,847	\$ (14,240)	\$ —	\$ (780)	\$ —	\$ 123,827	\$ (14,240)
Asset-backed securities.....	302,407	2,213	184,480	(461,416)	—	27,684	(2,435)
Fixed maturities.....	<u>\$ 441,254</u>	<u>\$ (12,027)</u>	<u>\$ 184,480</u>	<u>\$ (462,196)</u>	<u>\$ —</u>	<u>\$ 151,511</u>	<u>\$ (16,675)</u>
Equities							
Finance.....	\$ 22,637	\$ 3,444	\$ —	\$ (5,264)	\$ —	\$ 20,817	\$ 3,216
Technology .....	8,207	1,143	450	—	—	9,800	1,143
Communications.....	1,985	209	—	(2,194)	—	—	55
Mutual funds and exchange traded funds.....	4,604	(242)	—	(4,208)	—	154	14
Equities.....	<u>\$ 37,433</u>	<u>\$ 4,554</u>	<u>\$ 450</u>	<u>\$ (11,666)</u>	<u>\$ —</u>	<u>\$ 30,771</u>	<u>\$ 4,428</u>
Other invested assets							
Derivatives, net.....	\$ 5,351	\$ (3,313)	\$ 2,255	\$ 4,512	\$ —	\$ 8,805	\$ (1,772)
Notes and loan receivables and notes securitization ...	125,921	2,599	71,828	(58,655)	—	141,693	2,278
Private equities .....	26,309	43	152,777	(4,274)	—	174,855	(3,608)
Annuities and residuals.....	8,436	262	—	(8,698)	—	—	—
Other invested assets .....	<u>\$ 166,017</u>	<u>\$ (409)</u>	<u>\$ 226,860</u>	<u>\$ (67,115)</u>	<u>\$ —</u>	<u>\$ 325,353</u>	<u>\$ (3,102)</u>
Total.....	<u>\$ 644,704</u>	<u>\$ (7,882)</u>	<u>\$ 411,790</u>	<u>\$ (540,977)</u>	<u>\$ —</u>	<u>\$ 507,635</u>	<u>\$ (15,349)</u>

(1) There were no issuances.

(2) Settlements and sales of fixed maturities, equities and other invested assets include sales of \$276.4 million, \$11.7 million and \$41.8 million, respectively.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

The significant unobservable inputs used in the valuation of financial instruments measured at fair value using Level 3 inputs at December 31, 2017 and 2016 were as follows (fair value in thousands of U.S. dollars):

December 31, 2017	Fair value	Valuation techniques	Unobservable inputs	Range (Weighted average)
Fixed maturities				
U.S. states, territories and municipalities .....	\$128,806	Discounted cash flow	Credit spreads	0.15% – 10.2% (4.7%)
Asset-backed securities .....	20,738	Discounted cash flow	Credit spreads	4.7% – 4.7% (4.7%)
Equities				
Finance .....	21,792	Weighted market comparables	Net income multiple	16.7 (16.7)
			Tangible book value multiple	2.0 (2.0)
			Liquidity discount	25.0% (25.0%)
			Comparable return	4.1% (4.1%)
Technology .....	10,960	Reported market value	Tangible book value multiple	100% (100%)
Other invested assets				
Total return swaps, net .....	(764)	Discounted cash flow	Credit spreads	2.4% – 30.8% (18.5%)
Insurance-linked securities - longevity swaps .....	11,962	Discounted cash flow	Credit spreads	1.7% (1.7%)
Notes and loan receivables .....	102,906	Discounted cash flow	Credit spreads	3.9% – 39.3% (6.1%)
Notes and loan receivables .....	4,265	Discounted cash flow	Credit spreads	17.5% (17.5%)
			Gross revenue/fair value	1.1 (1.1)
Notes securitization .....	1,392	Discounted cash flow	Credit spreads	1.5% (1.5%)
Private equity – direct .....	3,011	Discounted cash flow and weighted market comparables	Tangible book value multiple	0.8 (0.8)
			Recoverability of intangible assets	0% (0%)

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

December 31, 2016	Fair value	Valuation techniques	Unobservable inputs	Range (Weighted average)
Fixed maturities				
U.S. states, territories and municipalities .....	\$123,827	Discounted cash flow	Credit spreads	1.5% – 10.5% (6.3%)
Asset-backed securities .....	27,684	Discounted cash flow	Credit spreads	4.1% – 5.7% (5.3%)
Equities				
Finance .....	20,817	Weighted market comparables	Net income multiple	20.3 (20.3)
			Tangible book value multiple	1.9 (1.9)
			Liquidity discount	25.0% (25.0%)
			Comparable return	36.9% (36.9%)
Technology .....	9,800	Reported market value	Tangible book value multiple	100% (100%)
Other invested assets				
Total return swaps, net.....	(1,228)	Discounted cash flow	Credit spreads	2.9% – 29.4% (19.3%)
Insurance-linked securities - longevity swaps .....	9,218	Discounted cash flow	Credit spreads	2.6% (2.6%)
Notes and loan receivables .....	131,176	Discounted cash flow	Credit spreads	4.2% – 24.4% (5.2%)
Notes and loan receivables .....	8,953	Discounted cash flow	Credit spreads	17.5% (17.5%)
			Gross revenue/fair value	1.2 (1.2)
Notes securitization .....	1,563	Discounted cash flow	Credit spreads	3.3% (3.3%)
Private equity – direct.....	5,019	Discounted cash flow and weighted market comparables	Net income multiple	8.6 (8.6)
			Tangible book value multiple	2.0 (2.0)
			Recoverability of intangible assets	0% (0%)

The tables above do not include financial instruments that are measured using unobservable inputs (Level 3) where the unobservable inputs were obtained from external sources and used without adjustment. These financial instruments include mutual fund and exchange traded fund investments (included within equities), certain private equity funds (included within private equities), and certain derivatives (included within other invested assets).

The Parent has established a Valuation Committee which is responsible for determining the invested asset valuation policy and related procedures for the Parent and its subsidiaries, including the Company, for reviewing significant changes in the fair value measurements of securities classified as Level 3 ensuring that there is an appropriate independent internal peer analysis, on at least an annual basis, on the fair value measurements of significant securities that are classified as Level 3. The Valuation Committee is comprised of members of the Parent's senior management team. The Parent's Group Enterprise Risk Management Financial Risk Policy which covers, amongst other items, invested asset valuation, is monitored by the Parent's Board of Directors.

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

Changes in the fair value of the Company's financial instruments subject to the fair value option during the years ended December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	2017	2016
Fixed maturities and short-term investments .....	\$ 72,883	\$ (8,562)
Equities .....	57,599	(37,241)
Other invested assets .....	40,145	3,800
Total .....	\$ 170,627	\$ (42,003)

The above changes in fair value are included in the Consolidated Statements of Operations under the caption Net realized and unrealized investment gains.

The following methods and assumptions were used by the Company in estimating the fair value of each class of financial instrument recorded in the Consolidated Balance Sheets. There have been no material changes in the Company's valuation techniques during the periods presented.

*Fixed maturities*

- *U.S. government and government sponsored enterprises*—U.S. government and government sponsored enterprises securities consist primarily of bonds issued by the U.S. Treasury and corporate debt securities issued by government sponsored enterprises and federally owned or established corporations. These securities are generally priced by independent pricing services. The independent pricing services may use actual transaction prices for securities that have been actively traded. For securities that have not been actively traded, each pricing source has its own proprietary method to determine the fair value, which may incorporate option adjusted spreads (OAS), interest rate data and market news. The Company generally classifies these securities in Level 2.
- *U.S. states, territories and municipalities*—U.S. states, territories and municipalities securities consist primarily of bonds issued by U.S. states, territories and municipalities and the Federal Home Loan Mortgage Corporation. These securities are generally priced by independent pricing services using the techniques described for U.S. government and government sponsored enterprises above. The Company generally classifies these securities in Level 2. Certain of the bonds that are issued by municipal housing authorities and the Federal Home Loan Mortgage Corporation are not actively traded and are priced based on internal models using unobservable inputs. Accordingly, the Company classifies these securities in Level 3. The significant unobservable input used in the fair value measurement of these U.S. states, territories and municipalities securities classified as Level 3 is credit spreads. A significant increase (decrease) in credit spreads in isolation could result in a significantly lower (higher) fair value measurement.
- *Non-U.S. sovereign government, supranational and government related*—Non-U.S. sovereign government, supranational and government related securities consist primarily of bonds issued by non-U.S. national governments and their agencies, non-U.S. regional governments and supranational organizations. These securities are generally priced by independent pricing services using the techniques described for U.S. government and government sponsored enterprises above. The Company generally classifies these securities in Level 2.
- *Corporate*—Corporate securities consist primarily of bonds issued by U.S. and foreign corporations covering a variety of industries and issuing countries. Corporate securities also include real estate investment trusts, catastrophe bonds, longevity and mortality bonds and government guarantee corporate debt. These securities are generally priced by independent pricing services and brokers. The pricing provider incorporates information including credit spreads, interest rate data and market news into the valuation of each security. The Company generally classifies these securities in Level 2. When a corporate security is inactively traded or the valuation model uses unobservable inputs, the Company classifies the security in Level 3.
- *Asset-backed securities*—Asset-backed securities primarily consist of bonds issued by U.S. and foreign corporations that are predominantly backed by student loans, automobile loans, credit card receivables, equipment leases, and special purpose financing. With the exception of special purpose financing securities, these asset-backed securities are generally priced by independent pricing services and brokers. The pricing provider applies dealer quotes and other available trade information, prepayment speeds, yield curves and credit spreads to

## Partner Reinsurance Company Ltd.

### Notes to Consolidated Financial Statements - (Continued)

the valuation. The Company generally classifies these securities in Level 2. Special purpose financing securities are generally inactively traded and are priced based on valuation models using unobservable inputs. The Company generally classifies these securities in Level 3. The significant unobservable input used in the fair value measurement of these asset-backed securities classified as Level 3 is credit spreads. A significant increase (decrease) in credit spreads in isolation could result in a significantly lower (higher) fair value measurement.

- *Residential mortgage-backed securities*—Residential mortgage-backed securities primarily consist of bonds issued by the Government National Mortgage Association, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, as well as private, non-agency issuers. These residential mortgage-backed securities are generally priced by independent pricing services and brokers. When current market trades are not available, the pricing provider or the Company will employ proprietary models with observable inputs including other trade information, prepayment speeds, yield curves and credit spreads. The Company generally classifies these securities in Level 2.

In general, the methods employed by the independent pricing services to determine the fair value of the securities that have not been actively traded primarily involve the use of “matrix pricing” in which the independent pricing source applies the credit spread for a comparable security that has traded recently to the current yield curve to determine a reasonable fair value. The Company generally uses one pricing source per security and uses a pricing service ranking to consistently select the most appropriate pricing service in instances where it receives multiple quotes on the same security. When fair values are unavailable from these independent pricing sources, quotes are obtained directly from broker-dealers who are active in the corresponding markets. Most of the Company’s fixed maturities are priced from the pricing services or dealer quotes. The Company will typically not make adjustments to prices received from pricing services or dealer quotes; however, in instances where the quoted external price for a security uses significant unobservable inputs, the Company will classify that security as Level 3. The methods used to develop and substantiate the unobservable inputs used are based on the Company’s valuation policy and are dependent upon the facts and circumstances surrounding the individual investments which are generally transaction specific. The Company’s inactively traded fixed maturities are classified as Level 3. For all fixed maturity investments, the bid price is used for estimating fair value.

To validate prices, the Company compares the fair value estimates to its knowledge of the current market and will investigate prices that it considers not to be representative of fair value. The Company also reviews an internally generated fixed maturity price validation report which converts prices received for fixed maturity investments from the independent pricing sources and from broker-dealers quotes and plots OAS and duration on a sector and rating basis. The OAS is calculated using established algorithms developed by an independent risk analytics platform vendor. The OAS on the fixed maturity price validation report are compared for securities in a similar sector and having a similar rating, and outliers are identified and investigated for price reasonableness. In addition, the Company completes quantitative analyses to compare the performance of each fixed maturity investment portfolio to the performance of an appropriate benchmark, with significant differences identified and investigated.

#### *Short-term investments*

Short-term investments are valued in a manner similar to the Company’s fixed maturity investments and are generally classified in Level 2.

#### *Equities*

Equity securities include U.S. and foreign common and preferred stocks, mutual funds and exchange traded funds. Equities classified as Level 2 are generally common and preferred stocks traded in inactive markets. Equities classified as Level 3 are generally mutual funds invested in securities other than the common stock of publicly traded companies, where the net asset value is not provided on a daily basis, and inactively traded common stocks. The significant unobservable inputs used in the fair value measurement of inactively traded common stocks classified as Level 3 include market return information, weighted using management’s judgment, from comparable selected publicly traded companies in the same industry, in a similar region and of a similar size, including net income multiples, tangible book value multiples, comparable returns, revenue multiples, adjusted earnings multiples and projected return on equity ratios. Significant increases (decreases) in any of these inputs could result in a significantly higher (lower) fair value measurement. Significant unobservable inputs used in measuring the fair value measurement of inactively traded common stocks also include a liquidity discount. A significant increase (decrease) in the liquidity discount could result in a significantly lower (higher) fair value measurement.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

To validate prices, the Company completes quantitative analyses to compare the performance of each equity investment portfolio to the performance of an appropriate benchmark, with significant differences identified and investigated.

*Other invested assets*

The Company's exchange traded derivatives, such as futures are generally classified as Level 1 as their fair values are quoted prices in active markets. The Company's foreign exchange forward contracts, interest rate swaps and TBAs are generally classified as Level 2 within the fair value hierarchy and are priced by independent pricing services.

Included in the Company's Level 3 classification, in general, are certain inactively traded weather derivatives, including weather derivative insurance-linked securities and total return swaps; notes and loan receivables and notes securitizations; and private equities. For Level 3 instruments, the Company will generally (i) receive a price based on a manager's or trustee's valuation for the asset; (ii) develop an internal discounted cash flow model to measure fair value; or (iii) use market return information, adjusted if necessary and weighted using management's judgment, from comparable selected publicly traded equity funds in a similar region and of a similar size. Where the Company receives prices from the manager or trustee, these prices are based on the manager's or trustee's estimate of fair value for the assets and are generally audited on an annual basis. Where the Company develops its own discounted cash flow models, the inputs will be specific to the asset in question, based on appropriate historical information, adjusted as necessary, and using appropriate discount rates. The significant unobservable inputs used in the fair value measurement of other invested assets classified as Level 3 include credit spreads, gross revenue to fair value ratios, net income multiples, effective yields, tangible book value multiples and other valuation ratios. Significant increases (decreases) in any of these inputs in isolation could result in a significantly lower (higher) fair value measurement. Significant unobservable inputs used in the fair value measurement of other invested assets classified as Level 3 also include an assessment of the recoverability of intangible assets and market return information, weighted using management's judgment, from comparable selected publicly traded companies in the same industry, in a similar region and of a similar size. Significant increases (decreases) in these inputs in isolation could result in a significantly higher (lower) fair value measurement. As part of the Company's modeling to determine the fair value of an investment, the Company considers counterparty credit risk as an input to the model, however, the majority of the Company's counterparties are investment grade rated institutions and the failure of any one counterparty would not have a significant impact on the Company's consolidated financial statements.

To validate prices, the Company will compare them to benchmarks, where appropriate, or to the business results generally within that asset class and specifically to those particular assets.

***(b) Fair Value of Financial Instrument Liabilities***

At December 31, 2017 and 2016, the fair values of financial instrument liabilities recorded in the Consolidated Balance Sheets approximate their carrying values. Disclosures about the fair value of financial instrument liabilities exclude insurance contracts and certain other financial instruments.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**4. Investments**

**(a) Net Realized and Unrealized Investment (Losses) Gains**

The components of the net realized and unrealized investment gains (losses) for the years ended December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	2017	2016
Net realized investment gains on fixed maturities and short-term investments.....	\$ 31,162	\$ 29,655
Net realized investment gains on equities .....	(4,883)	30,105
Net realized gains (losses) on other invested assets .....	(8,180)	3,401
Change in net unrealized gains on other invested assets.....	45,630	16,147
Change in net unrealized investment losses on fixed maturities and short-term investments .....	72,883	(8,562)
Change in net unrealized investment losses on equities .....	57,599	(37,241)
Total net realized and unrealized investment gains (losses).....	\$ 194,211	\$ 33,505

**(b) Net Investment Income**

The components of net investment income for the years ended December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	2017	2016
Fixed maturities.....	\$ 166,613	\$ 204,113
Short-term investments, cash and cash equivalents .....	2,425	741
Equities.....	(6)	2,759
Funds held and other .....	16,538	24,378
Investment expenses .....	(27,115)	(26,060)
Net investment income.....	\$ 158,455	\$ 205,931

The Company generally earns investment income on funds held by reinsured companies, including the 50% quota-share agreement with PartnerRe Europe (see Note 16), based upon a predetermined interest rate, either fixed contractually at the inception of the contract or based upon a recognized index (e.g., LIBOR). Interest rates ranged from 1.2% to 4.5% for the year ended December 31, 2017 and from 2.4% to 4.9% for the year ended December 31, 2016.

**(c) Pledged and Restricted Assets**

At December 31, 2017 and 2016, approximately \$102.2 million and \$84.3 million, respectively, of cash and cash equivalents and approximately \$1,254.6 million and \$900.8 million, respectively, of securities were deposited, pledged, held in trust or escrow accounts in favor of ceding companies and other counterparties or government authorities to comply with reinsurance contract provisions and insurance laws. The increase during the year was a result of collateral required to secure payment for claims related to hurricanes Harvey, Irma and Maria in 2017.

The Company operates a multi-beneficiary U.S. reinsurance trust (the trust) to enable its U.S. cedants to take statutory financial statement credit without the need to post contract-specific security. The trust is required to maintain sufficient assets to support both its liabilities related to some of its U.S. cedants, for contracts incepting after June 2010, and a minimum surplus of \$20.0 million. At December 31, 2017 and 2016, assets held by the trust exceeded liabilities and minimum surplus by \$143.2 million and \$225.2 million, respectively. The Company is currently approved to utilize the trust in all U.S. jurisdictions.



**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

***(d) Net (Payable)/Receivable for Securities Purchased/Sold***

Included within Accounts payable, accrued expenses and other in the Consolidated Balance Sheet at December 31, 2017 and 2016 were amounts of gross payable balances for securities purchased and gross receivable balances for securities sold as follows (in thousands of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Payable for securities purchased.....	\$ (82,714)	\$ (554,838)
Receivable for securities sold .....	52,911	11,117
Net payable for securities purchased .....	\$ (29,803)	\$ (543,721)

***(e) Variable Interest Entities***

The Company holds variable interests in VIEs including certain limited liability companies or partnerships, fixed maturity investments and asset-backed securities. The holdings in these VIEs are reported within fixed maturities and other invested assets in the Company's Consolidated Balance Sheets. The Company's involvement in these entities is, for the most part, passive in nature. The Company's maximum exposure to loss with respect to these investments is limited to the amounts invested in and advanced to the VIEs, and any unfunded commitments. The Company's non-consolidated VIEs include variable interests in catastrophe bonds within fixed maturity investments and certain other invested assets.

***(f) Summarized Financial Information***

The Company has an investment in an equity method investee, Almacantar Group S.A. (Almacantar) that is considered significant in terms of the interest in earnings of this investee exceeding 10% of the consolidated net loss before income tax expense of the Company as at December 31, 2017. The summarized balance sheet and income statement of Almacantar S.A. is as follows:

<b>As at December 31,</b>	<u>2017</u>	<u>2016</u>
Current assets .....	\$ 906,085	\$ 698,835
Noncurrent assets .....	\$ 1,877,519	\$ 1,510,632
Current liabilities .....	\$ 553,219	\$ 372,677
Noncurrent liabilities .....	\$ 690,935	\$ 624,970
 <b>For the year ended December 31,</b>	 <u>2017</u>	 <u>2016</u>
Revenues .....	\$ 130,333	\$ 24,646
Operating profit.....	\$ 190,613	\$ (47,082)
Net income .....	\$ 213,241	\$ (37,059)

The summarized balance sheet has been included as at the years ended December 31, 2017 and 2016 and the summarized income statement has been included for the years ended December 31, 2017 and 2016. Operating profit referred to in the table above includes revenues, cost of sales, and unrealized gains on properties.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**5. Derivatives**

The Company's derivative instruments are recorded in the Consolidated Balance Sheets at fair value, with changes in fair value recognized in either net foreign exchange gains and losses or net realized and unrealized investment gains and losses in the Consolidated Statements of Operations, depending on the nature of the derivative instrument. The Company's objectives for holding or issuing these derivatives are as follows:

**Foreign Exchange Forward Contracts**

The Company utilizes foreign exchange forward contracts as part of its overall currency risk management and investment strategies.

**Futures Contracts**

The Company uses exchange traded treasury note futures contracts to manage portfolio duration and equity futures to hedge certain investments.

**Insurance-Linked Securities**

The Company enters into various weather derivatives for which the underlying risks reference parametric weather risks in addition to longevity total return swaps for which the underlying risks reference longevity risks.

**Total Return and Interest Rate Swaps**

The Company enters into total return swaps referencing various project, investment and principal finance obligations. The Company enters into interest rate swaps to mitigate the interest rate risk on certain of the total return swaps and certain fixed maturity investments.

**To-Be-Announced Mortgage-Backed Securities**

The Company utilizes TBAs as part of its overall investment strategy and to enhance investment performance.

The net fair values and the related net notional values of derivatives included in the Company's Consolidated Balance Sheets at December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	Asset derivatives at fair value	Liability derivatives at fair value	Net derivatives	
			Net notional exposure	Fair value
<b>December 31, 2017</b>				
Foreign exchange forward contracts .....	\$ 5,726	\$ (15,215)	\$ 3,013,294	\$ (9,489)
Insurance-linked securities <sup>(1)</sup> .....	11,985	—	138,840	11,985
Total return swaps .....	2,505	(3,269)	42,147	(764)
Interest rate swaps <sup>(2)</sup> .....	—	(12,298)	192,215	(12,298)
TBAs .....	81	(64)	122,840	17
<b>Total derivatives</b> .....	<b>\$ 23,664</b>	<b>\$ (30,846)</b>		<b>\$ (7,182)</b>

	Asset derivatives at fair value	Liability derivatives at fair value	Net derivatives	
			Net notional exposure	Fair value
<b>December 31, 2016</b>				
Foreign exchange forward contracts .....	\$ 5,263	\$ (6,122)	\$ 2,787,665	\$ (859)
Insurance-linked securities (1) .....	10,130	(97)	145,011	10,033
Total return swaps .....	1,989	(3,217)	42,304	(1,228)
Interest rate swaps (2) .....	—	(13,402)	194,585	(13,402)
TBAs .....	342	(57)	93,278	285
<b>Total derivatives</b> .....	<b>\$ 17,724</b>	<b>\$ (22,895)</b>		<b>\$ (5,171)</b>

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

- (1) *Insurance-linked securities include longevity swaps for which the notional amount is not reflective of the overall potential exposure of the swap. The net notional exposure above included the Company's best estimate of the present value of future expected claims for December 31, 2017 and, the Company's probable maximum loss for December 31, 2016.*
- (2) *The Company enters into interest rate swaps to mitigate notional exposures on certain total return swaps and certain fixed maturities. The net notional exposure for interest rate swaps above relates to fixed maturities.*

The fair value of derivatives is recorded in other invested assets in the Company's Consolidated Balance Sheets. There were no derivatives designated as hedges at December 31, 2017 and 2016.

The gains and (losses) in the Consolidated Statements of Operations for derivatives for the years ended December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	2017	2016
Foreign exchange forward contracts.....	\$ (200,666)	\$ 39,289
Foreign currency option contracts .....	—	1,858
<b>Total included in net foreign exchange gains and losses.....</b>	<b>\$ (200,666)</b>	<b>\$ 41,147</b>
Futures contracts .....	(11,683)	(4,850)
Insurance-linked securities.....	(563)	3,813
Total return swaps.....	464	(1,096)
Interest rate swaps.....	1,105	10,981
TBAs.....	1,450	2,127
Options.....	—	—
<b>Total included in net realized and unrealized investment gains and losses.....</b>	<b>\$ (9,227)</b>	<b>\$ 10,975</b>
<b>Total (losses) gains on derivatives not designated as hedges.....</b>	<b>\$ (209,893)</b>	<b>\$ 52,122</b>

*Offsetting of Derivatives*

The gross and net fair values of derivatives that are subject to offsetting in the Consolidated Balance Sheets at December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	Gross amounts recognized (1)	Gross amounts offset in the balance sheet	Net amounts of assets / liabilities presented in the balance sheet	Gross amounts not offset in the balance sheet		Net amount
				Financial instruments	Cash collateral received / pledged	
<b>December 31, 2017</b>						
Total derivative assets.....	\$ 23,664	\$ —	\$ 23,664	\$ (816)	\$ (43,943)	\$ (21,095)
Total derivative liabilities	\$ (30,846)	\$ —	\$ (30,846)	\$ 816	\$ 24,319	\$ (5,711)
<b>December 31, 2016</b>						
Total derivative assets.....	\$ 17,724	\$ —	\$ 17,724	\$ (666)	\$ (34,120)	\$ (17,062)
Total derivative liabilities	\$ (22,895)	\$ —	\$ (22,895)	\$ 666	\$ 15,979	\$ (6,250)

- (1) *Amounts include all derivative instruments, irrespective of whether there is a legally enforceable master netting arrangement in place.*

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

**6. Non-life and Life and Health Reserves**

**(a) Non-life Reserves**

Non-life reserves are categorized into three types of reserves: case reserves, ACRs and IBNR reserves. Case reserves represent unpaid losses reported by the Company's cedants and recorded by the Company. ACRs are established for particular circumstances where, on the basis of individual loss reports, the Company estimates that the particular loss or collection of losses covered by a treaty may be greater than those advised by the cedant. IBNR reserves represent a provision for claims that have been incurred but not yet reported to the Company, as well as future loss development on losses already reported, in excess of the case reserves and ACRs.

The reconciliation of the beginning and ending gross and net liability for unpaid losses and loss expenses, excluding policy benefits for life and annuity contracts, for the years ended December 31, 2017 and 2016 was as follows (in thousands of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Gross liability at beginning of year .....	\$ 3,668,786	\$ 3,683,794
Reinsurance recoverable at beginning of year .....	<u>56,129</u>	32,261
Net liability at beginning of year.....	<u>3,612,657</u>	3,651,533
Net incurred losses related to:		
Current year .....	<b>1,804,804</b>	1,355,270
Prior years .....	<u>(205,771)</u>	(283,623)
	<b>1,599,033</b>	1,071,647
Net paid losses related to:		
Current year .....	<b>266,585</b>	150,546
Prior years .....	<u>912,774</u>	843,712
	<b>1,179,359</b>	994,258
Effects of foreign exchange rate changes.....	<u>209,346</u>	(116,265)
Net liability at end of year.....	<b>4,241,677</b>	3,612,657
Reinsurance recoverable at end of year.....	<u>364,954</u>	56,129
Gross liability at end of year .....	\$ <b>4,606,631</b>	\$ 3,668,786

During the years ended December 31, 2017 and 2016, the Company's Non-life business reported net favorable loss development of \$205.8 million and \$283.6 million for prior accident years, respectively. Losses reported by cedants during 2017 and 2016 regarding prior accident years were lower than the Company expected in most lines of business, which led the Company to decrease its expected ultimate loss ratios and estimates.

***Asbestos and Environmental Claims***

The Company's net reserves for unpaid losses and loss expenses at December 31, 2017 and 2016 included \$24 million and \$32 million, respectively, that represent estimates of its net ultimate liability for asbestos and environmental claims.

Ultimate loss estimates for such claims cannot be estimated using traditional reserving techniques and there are significant uncertainties in estimating the amount of the Company's potential losses for these claims. In view of the legal and tort environment that affect the development of such claims, the uncertainties inherent in estimating asbestos and environmental claims are not likely to be resolved in the near future. There can be no assurance that the reserves established by the Company will not be adversely affected by development of other latent exposures, and further, there can be no assurance that the reserves established by the Company will be adequate. The Company does, however, actively evaluate potential exposure to asbestos and environmental claims and establishes additional reserves as appropriate. The Company believes that it has made a reasonable provision for these exposures and is unaware of any specific issues that would materially affect its unpaid losses and loss expense reserves related to this exposure.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

***Reserving methods***

The reserving methods commonly employed by the Company are summarized as follows:

*Chain Ladder (CL) Development Methods (Reported or Paid)*

These methods use the underlying assumption that losses reported (paid) for each underwriting year at a particular development stage follow a stable pattern. The CL development method assumes that on average, every underwriting year will display the same percentage of ultimate liabilities reported by the Company's cedants at 24 months after the inception of the underwriting year. The percentages reported (paid) are established for each development stage after examining historical averages from the loss development data. These are sometimes supplemented by external benchmark information. Ultimate liabilities are estimated by multiplying the actual reported (paid) losses by the reciprocal of the assumed reported (paid) percentage. Reserves are then calculated by subtracting paid claims from the estimated ultimate liabilities.

*Expected Loss Ratio (ELR) Method*

This method estimates ultimate losses for an underwriting year by applying an estimated loss ratio to the earned premium for that underwriting year. Although the method is insensitive to actual reported or paid losses, it can often be useful at the early stages of development when very few losses have been reported or paid, and the principal sources of information available to the Company consist of information obtained during pricing and qualitative information supplied by the cedant. However, the lack of sensitivity to reported or paid losses means that the method is usually inappropriate at later stages of development.

*Bornhuetter-Ferguson (B-F) Methods (Reported or Paid)*

These methods aim to address the variability at early stages of development and incorporates external information such as pricing. The B-F methods are more sensitive to reported and paid losses than the ELR method, and can be seen as a blend of the ELR and CL development methods. Unreported (unpaid) claims are calculated using an expected reporting (payment) pattern and an externally determined estimate of ultimate liabilities (usually determined by multiplying an *a priori loss* ratio with estimates of premium volume). The accuracy of the *a priori loss* ratio is a critical assumption in this method. Usually *a priori loss* ratios are initially determined on the basis of pricing information, but may also be adjusted to reflect other information that subsequently emerges about underlying loss experience.

*Benktander (B-K) Methods (Reported or Paid)*

These methods can be viewed as a blend between the CL Development and the B-F methods described above. The blend is based on predetermined weights at each development stage that depend on the reported (paid) development patterns.

*Loss Event Specific Method*

The ultimate losses estimated under this method are derived from estimates of specific events based on reported claims, client and broker discussions, review of potential exposures, market loss estimates, modeled analysis and other event specific criteria.

*Method Weights*

In determining the loss reserves, the Company often relies on a blend of the results from two or more methods (e.g., weighted averages). The judgment as to which of the above method(s) is most appropriate for a particular underwriting year and reserving cell could change over time as new information emerges regarding underlying loss activity and other data issues. Furthermore, as each line is typically composed of several reserving cells, it is likely that the reserves for the line will be dependent on several reserving methods. This is because reserves for a line are the result of aggregating the reserves for each constituent reserving cell and that a different method could be selected for each reserving cell.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

The principal reserving methods used for Specialty and P&C were ELR, Reported/Paid B-F, Reported/Paid B-K and Reported/Paid CL, with the exception of catastrophe risks within the P&C segment where the principal reserving methods used were ELR based on exposure analysis and Loss event specific methods.

**(b) Life and Health Reserves**

The Company's Life and Health business reported net adverse loss development for prior accident years of \$8.6 million and net favourable loss development of \$7.5 million for the years ended December 31, 2017 and 2016, respectively.

The net adverse prior year loss development of \$8.6 million in 2017 was primarily related to adverse development on other than guaranteed minimum death benefit (GMDB) business and Health business.

The net favorable prior year loss development of \$7.5 million in 2016 was primarily related to favorable development on GMDB and Health business, which was partially offset by adverse development on other than GMDB mortality treaties.

The Company used interest rate assumptions to estimate its liabilities for policy benefits for life and annuity contracts which ranged from 0.0% to 6.8% at December 31, 2017 and 2016.

**(c) Losses and Loss Expenses**

Losses and loss expenses in the Consolidated Statements of Operations for the years ended December 31, 2017 and 2016 was as follows (in thousands of U.S. dollars):

	2017	2016
Net incurred losses related to:		
Non-life .....	\$ 1,599,033	\$ 1,071,647
Life and Health.....	569,878	442,723
Losses and loss expenses.....	\$ 2,168,911	\$ 1,514,370

*Non-life net incurred and paid losses and loss expense development*

The net incurred and paid losses and loss expenses development by accident year for each of the years ended December 31, 2012 through 2017, and the total of IBNR plus expected development on reported claims included within the net incurred claims amounts, as at each of the years ended December 31, 2012 through 2017, are presented in the tables below (in thousands of U.S. dollars).

The information presented below for incurred and paid claims development and the average annual percentage payout of incurred claims by age, net of reinsurance, for each of the years ended December 31, 2012 through 2016 is presented as supplementary information and is unaudited.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**NET INCURRED LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - NON-LIFE**

For the year ended December 31,

December 31, 2017

Accident year	2012	2013	2014	2015	2016	2017	Total of IBNR plus expected development on reported claims
2012	\$ 1,179,016	\$ 1,079,345	\$ 996,466	\$ 940,315	\$ 924,164	\$ 924,999	\$ 55,599
2013		1,308,957	1,219,988	1,133,691	1,105,389	1,093,162	92,865
2014			1,314,517	1,204,582	1,149,679	1,139,241	128,190
2015				1,349,860	1,208,022	1,157,908	214,940
2016					1,378,562	1,260,108	356,169
2017						1,804,016	1,218,671
<b>Total</b>						<b>\$ 7,379,434</b>	<b>\$ 2,066,434</b>

**NET PAID LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - NON-LIFE**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017
2012	\$ 135,248	\$ 472,873	\$ 628,313	\$ 697,420	\$ 737,225	\$ 772,052
2013		120,154	583,559	747,863	838,294	892,061
2014			150,439	622,985	765,482	856,426
2015				146,462	566,566	754,336
2016					152,712	626,095
2017						269,157
<b>Total</b>						<b>\$ 4,170,127</b>

Net reserves for Accident Years and exposures included in the triangles	3,209,307
All outstanding liabilities before Accident Year 2012, net of reinsurance	997,491
Total outstanding net liabilities for unpaid claims	<b>\$ 4,206,798</b>

**AVERAGE ANNUAL PERCENTAGE PAYOUT OF INCURRED CLAIMS BY AGE, NET OF REINSURANCE - NON-LIFE**

Years	1	2	3	4	5	6
Non-life	13%	39%	15%	8%	5%	4%

(1) The table above (and each of the three tables below for property, casualty and specialty) reflects losses incurred and paid losses translated to U.S. dollars at the exchange rate as of the balance sheet date whereas the losses and loss expenses in the Consolidated Statement of Operations reflected losses incurred at the average exchange rate for the period.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**NET INCURRED LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - PROPERTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017	December 31, 2017 Total of IBNR plus expected development on reported claims
2012	\$ 315,751	\$ 330,271	\$ 277,742	\$ 268,028	\$ 261,495	\$ 260,476	\$ 2,977
2013		399,060	332,801	317,933	308,895	305,098	1,507
2014			264,509	233,770	223,398	222,717	2,572
2015				298,657	269,637	257,677	9,759
2016					351,104	319,400	26,465
2017						725,012	372,404
<b>Total</b>						<b>\$ 2,090,380</b>	<b>\$ 415,684</b>

**NET PAID LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - PROPERTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017
2012	\$ 48,359	\$ 169,361	\$ 211,426	\$ 229,263	\$ 235,227	\$ 239,408
2013		46,535	194,986	253,850	273,814	284,418
2014			41,313	159,693	192,304	206,249
2015				43,340	171,343	214,358
2016					57,853	204,807
2017						171,273
<b>Total</b>						<b>\$ 1,320,513</b>

Net reserves for Accident Years and exposures included in the triangles	769,867
All outstanding liabilities before Accident Year 2012, net of reinsurance	124,763
Total outstanding net liabilities for unpaid claims	<b>\$ 894,630</b>

**AVERAGE ANNUAL PERCENTAGE PAYOUT OF INCURRED CLAIMS BY AGE, NET OF REINSURANCE - PROPERTY**

Years	1	2	3	4	5	6
Property	20%	49%	17%	7%	3%	2%



**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**NET INCURRED LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - CASUALTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017	December 31, 2017 Total of IBNR plus expected development on reported claims
2012	\$ 244,303	\$ 237,526	\$ 232,529	\$ 215,765	\$ 207,663	\$ 207,346	\$ 36,404
2013		293,873	298,772	283,719	276,306	269,460	66,102
2014			355,246	351,754	345,852	348,211	95,808
2015				361,448	342,977	335,092	125,906
2016					345,191	334,759	162,846
2017						357,094	278,646
<b>Total</b>						<b>\$ 1,851,962</b>	<b>\$ 765,712</b>

**NET PAID LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - CASUALTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017
2012	\$ 23,296	\$ 57,359	\$ 78,090	\$ 98,313	\$ 113,415	\$ 131,505
2013		24,385	70,289	105,675	130,540	151,902
2014			32,363	94,064	132,125	166,510
2015				31,996	84,819	127,569
2016					13,701	69,120
2017						33,883
<b>Total</b>						<b>\$ 680,489</b>

Net reserves for Accident Years and exposures included in the triangles	1,171,473
All outstanding liabilities before Accident Year 2012, net of reinsurance	746,985
Total outstanding net liabilities for unpaid claims	<b>\$ 1,918,458</b>

**AVERAGE ANNUAL PERCENTAGE PAYOUT OF INCURRED CLAIMS BY AGE, NET OF REINSURANCE - CASUALTY**

Years	1	2	3	4	5	6
Casualty	9%	17%	12%	10%	8%	9%

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

**NET INCURRED LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE - SPECIALTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017	December 31, 2017 Total of IBNR plus expected development on reported claims
2012	\$ 618,961	\$ 511,547	\$ 486,195	\$ 456,521	\$ 455,006	\$ 457,177	\$ 16,218
2013		616,024	588,415	532,039	520,189	518,604	25,256
2014			694,763	619,059	580,428	568,313	29,810
2015				689,756	595,407	565,139	79,275
2016					682,267	605,949	166,858
2017						721,910	567,621
<b>Total</b>						<b>\$ 3,437,092</b>	<b>\$ 885,038</b>

**NET PAID LOSSES AND LOSS EXPENSES DEVELOPMENT TABLE -SPECIALTY**

For the year ended December 31,

Accident year	2012	2013	2014	2015	2016	2017
2012	\$ 63,592	\$ 246,153	\$ 338,798	\$ 369,843	\$ 388,582	\$ 401,139
2013		49,234	318,284	388,338	433,939	455,741
2014			76,763	369,227	441,053	483,667
2015				71,126	310,404	412,408
2016					81,157	352,169
2017						64,001
<b>Total</b>						<b>\$ 2,169,125</b>

Net reserves for Accident Years and exposures included in the triangles	1,267,967
All outstanding liabilities before Accident Year 2012, net of reinsurance	125,743
Total outstanding net liabilities for unpaid claims	<b>\$ 1,393,710</b>

**AVERAGE ANNUAL PERCENTAGE PAYOUT OF INCURRED CLAIMS BY AGE, NET OF REINSURANCE - SPECIALTY**

Years	1	2	3	4	5	6
Specialty	12%	46%	16%	8%	4%	3%

The Company is predominantly a reinsurer of other reinsurers and primary insurers and thus does not have access to claim frequency information held by our cedants due to the majority of the Company's business being written on a proportional basis. As such, the Company considers it impracticable to disclose information on the frequency of claims.

The Company has concluded that it is impracticable to provide net incurred and paid losses and loss expenses development data for 10 years and has therefore presented the data for 6 years. An additional year of data for each subsequent year will be included such that by 2021 a full 10 years of data will be disclosed.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

The reconciliation of the net incurred and paid claims development information above to the Non-life reserves in the Consolidated Balance Sheet at December 31, 2017 was as follows (in thousands of U.S. dollars):

	<b>December 31, 2017</b>
Total outstanding liability for unpaid claims.....	
Property .....	894,630
Casualty .....	1,918,458
Specialty .....	1,393,710
Total outstanding liabilities for unpaid claims .....	<b>4,206,798</b>
Other liabilities <sup>(1)</sup> .....	34,879
Net liability at end of year .....	<b>4,241,677</b>
Reinsurance recoverable on unpaid claims .....	
Property .....	354,187
Casualty .....	41
Specialty .....	10,726
Reinsurance recoverable at end of year .....	<b>364,954</b>
Gross liability at end of year .....	<b>4,606,631</b>

*(1) Other liabilities included in the reconciliation relate primarily to unallocated loss expenses.*

**7. Reinsurance**

***(a) Reinsurance Recoverable on Paid and Unpaid Losses***

The Company uses retrocessional agreements to reduce its exposure to risk of loss on reinsurance assumed. These agreements provide for recovery from retrocessionaires of a portion of losses and loss expenses. The Company remains liable to its cedants to the extent that the retrocessionaires do not meet their obligations under these agreements, and therefore the Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk on an ongoing basis. The Company actively manages its reinsurance exposures by generally selecting retrocessionaires having a credit rating of A- or higher. In certain cases where an otherwise suitable retrocessionaire has a credit rating lower than A-, the Company generally requires the posting of collateral, including escrow funds and letters of credit, as a condition to its entering into a retrocession agreement. The Company regularly reviews its reinsurance recoverable balances to estimate an allowance for uncollectible amounts based on quantitative and qualitative factors. There was no allowance for uncollectible reinsurance recoverable at December 31, 2017 deemed necessary based on the quantitative and qualitative analysis as collectability was determined to be reasonably assured and given that any recoverables related to reinsurers with ratings below A- or unrated are collateralized. The allowance for uncollectible reinsurance recoverable was \$2.6 million at December 31, 2016.

***(b) Ceded Reinsurance***

Net premiums written, net premiums earned and losses and loss expenses and life policy benefits are reported net of reinsurance in the Company's Consolidated Statements of Operations. Assumed, ceded and net amounts for the years ended December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

	Premiums Written	Premiums Earned	Losses and Loss Expenses
<b>2017</b>			
Assumed.....	\$ 3,082,873	\$ 2,855,949	\$ 2,551,316
Ceded .....	163,146	168,127	382,405
Net.....	\$ 2,919,727	\$ 2,687,822	\$ 2,168,911
<b>2016</b>			
Assumed.....	\$ 2,550,629	\$ 2,568,546	\$ 1,552,389
Ceded .....	164,398	157,950	38,019
Net.....	\$ 2,386,231	\$ 2,410,596	\$ 1,514,370

### 8. Shareholder's Equity

At December 31, 2017 and 2016, the total authorized and issued shares of the Company were 3,000,000 shares with a par value of \$1.00 per share.

### 9. Noncontrolling Interests

In March 2013, the Company formed, with other third party investors, Lorenz Re Ltd. (Lorenz Re), a Bermuda domiciled special purpose insurer. Lorenz Re is a segregated accounts company under the laws of Bermuda and distinct segregated accounts are formed and capitalized within Lorenz Re in order to enter into reinsurance agreements with the Company on a fully collateralized basis.

In 2017, Lorenz Re issued non-voting redeemable preferred share capital on behalf of a new segregated account to provide additional capacity to the Company for a diversified catastrophe portfolio on a fully collateralized reinsurance basis. The Company determined that it was the primary beneficiary of this segregated account and, accordingly, the segregated account was consolidated by the Company. No noncontrolling interest exists in this new segregated account as at December 31, 2017.

The reconciliation of the beginning and ending balance of the noncontrolling interests in Lorenz Re for the years ended December 31, 2017 and 2016 was as follows (in thousands of U.S. dollars):

	2017	2016
Balance at January 1 .....	\$ —	\$ 2,450
Net income attributable to noncontrolling interests .....	—	119
Distribution to noncontrolling interests .....	—	(2,569)
Balance at December 31 .....	\$ —	\$ —

### 10. Dividend Restrictions and Statutory Requirements

The Company is licensed as a Class 4 and Class E insurer and is therefore authorized to carry on general and long-term insurance business in Bermuda. The Insurance Act 1978, amendments thereto and related regulations, regulates insurance business in Bermuda and requires the Company to maintain minimum levels of solvency and liquidity and to comply with risk-based capital requirements and licensing rules. As at December 31, 2017, the Company's solvency, liquidity and risk-based capital levels were in excess of the minimum levels required.

The Company may declare dividends subject to it continuing to meet these minimum levels of solvency, liquidity, and its risk-based capital requirement, which is to hold statutory capital and surplus equal to or exceeding the Target Capital Level (equivalent to 120% of the Enhanced Capital Requirement (ECR)). The ECR is calculated using the Bermuda Solvency Capital Requirement model which is a risk-based capital model. At December 31, 2017, the maximum dividend that PartnerRe Bermuda could pay out of retained earnings was approximately \$1040 million.

**Partner Reinsurance Company Ltd.**

**Notes to Consolidated Financial Statements - (Continued)**

The Company is required to file annual statements with the Bermuda Monetary Authority (BMA) on an accounting basis as prescribed by the authority. The typical adjustments to insurance statutory basis amounts to convert to U.S. GAAP include deferral of certain acquisition costs, recognition of goodwill, intangible assets and deferred income taxes, and presentation of ceded reinsurance balances gross of assumed balances. The statutory financial return and capital and solvency return of the Company as at, and for the year ended, December 31, 2017 are due to be submitted to the BMA by April 30, 2018. The statutory financial return and capital and solvency return are subject to the review and final approval of the BMA.

The required and actual statutory capital and surplus of the Company at December 31, 2017 and 2016 was as follows (in millions of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Required statutory capital and surplus .....	<b>1,767</b>	\$ 1,578
Actual statutory capital and surplus .....	<b>3,683</b>	4,159

In addition to the required statutory capital and surplus requirements in the table above, the Company assesses its own solvency capital needs taking into account factors which may not be fully reflected in statutory requirements. The Company's solvency capital requirements determined under these self assessments may impact the level of dividends paid to its Parent.

**11. Taxation**

The Company is not subject to Bermuda income or capital gains tax under current Bermuda law. In the event that there is a change in current law such that taxes on income or capital gains are imposed, the Company would be exempt from such tax until March 2035 pursuant to the Bermuda Exempted Undertakings Tax Protection Act of 1966.

The Company has subsidiaries and branches that operate in various other jurisdictions around the world that are subject to tax in the jurisdictions in which they operate. The significant jurisdictions in which the Company's subsidiaries and branches are subject to tax are Canada and the United States.

Income tax returns are open for examination for the tax years 2013 - 2017 in Canada and 2014 - 2017 in the United States. As a global organization, the Company may be subject to a variety of transfer pricing or permanent establishment challenges by taxing authorities in various jurisdictions. While management believes that adequate provision has been made in the Consolidated Financial Statements for any potential assessments that may result from tax examinations for all open tax years, the completion of tax examinations for open years may result in changes to the amounts recognized in the Consolidated Financial Statements.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

Income tax expense for the years ended December 31, 2017 and 2016 was as follows (in thousands of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Current income tax expense (benefit) .....	\$ 3,073	\$ (10,422)
Deferred income tax (benefit) expense .....	<b>(1,608)</b>	13,862
Total income tax expense	<b>\$ 1,465</b>	\$ 3,440

The reconciliation of the actual income tax rate for the years ended December 31, 2017 and 2016 to the amount computed by applying the effective tax rate of 0% under Bermuda law to net (loss) income before taxes was as follows (in thousands of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Net (loss) income .....	\$ (64,759)	\$ 536,947
Income tax expense .....	<b>1,465</b>	3,440
Net (loss) income before taxes .....	<b>\$ (63,294)</b>	\$ 540,387

**Reconciliation of effective tax rate (% of income before taxes)**

Expected tax rate .....	0.0 %	0.0%
Foreign taxes at local expected tax rates .....	(15.8)	1.4
Tax exempt income .....	7.2	(0.7)
Impact of enacted change in tax law .....	4.4	0.0
Ceding commission .....	2.2	0.0
Other .....	(0.3)	(0.1)
Actual tax rate .....	<u>(2.3)%</u>	<u>0.6%</u>

On December 22, 2017, the United States enacted the Tax Cuts and Jobs Act (TCJA) to reduce the corporate income tax rate from 35% to 21% effective for taxable years beginning after December 31, 2017. As a result, income tax expense for the year ended December 31, 2017 was adjusted to reflect the impact of these tax rate changes and resulted in a decrease to income tax expense of \$3 million. This decrease reflects the revaluation of deferred tax assets and liabilities in the United States at December 31, 2017.

The Company continues to review and analyze the provisions of the TCJA and the impact on our financial statements. Given the complexity of the legislation, anticipated guidance from the U.S. Treasury, and the potential for additional guidance from the Securities and Exchange Commission or the Financial Accounting Standards Board, the impact of the TCJA may differ from the estimates booked, in which case, any adjustments will be recorded during 2018.

The net tax assets (liabilities) and their components at December 31, 2017 and 2016 were as follows (in thousands of U.S. dollars):

	<u>2017</u>	<u>2016</u>
Net current tax assets .....	\$ 23,862	\$ 22,750
Net deferred tax liabilities .....	<b>(4,326)</b>	(5,500)
Net tax assets	<b>\$ 19,536</b>	\$ 17,250

Deferred tax liabilities reflect the tax impact of temporary differences between the carrying amounts of assets (liabilities) for financial reporting and income tax purposes. Net deferred tax liabilities of \$4.3 million and \$5.5 million at December 31, 2017 and 2016, respectively, primarily relate to tax loss carryforwards and credits and life and health reserves.

The total amount of unrecognized tax benefits for the years ended December 31, 2017 and 2016 was \$nil.

**12. Share-Based Awards**

The Company's employees participated in the Parent's share-based compensation plans. In accordance with the Parent's share-based award plans and the Merger Agreement, all of the Parent's share-based awards fully vested and were

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

converted into \$137.50 in cash per share plus a special dividend of \$3.00 per common share upon the change in control of the Parent on March 18, 2016. As a result, there are no share-based awards outstanding at December 31, 2017 and 2016.

### **13. Retirement Benefit Arrangements**

For employee retirement benefits, the Company maintains certain defined contribution plans. Contributions are made by the Company, and in some locations, these contributions are supplemented by the local plan participants. Contributions are based on a percentage of the participant's base salary depending upon competitive local market practice and vesting provisions meeting legal compliance standards and market trends. The accumulated benefits for the majority of these plans vest immediately or over a two-year period. As required by law, certain retirement plans also provide for death and disability benefits and lump sum indemnities to employees upon retirement.

The Company recorded expenses of \$0.8 million and \$0.7 million for the years ended December 31, 2017 and 2016, respectively, within Other Operating Expenses in the Consolidated Statements of Operations and Comprehensive Income related to these defined contribution arrangements.

### **14. Commitments and Contingencies**

#### ***(a) Concentration of Credit Risk***

##### *Fixed maturities*

The Company's investment portfolio is managed following prudent standards of diversification and a prudent investment philosophy. The Company is not exposed to any significant credit concentration risk on its investments, except for debt securities issued by the U.S. government and other highly rated non-U.S. sovereign governments' securities. At December 31, 2017 and 2016, other than the U.S. and Canadian governments, the Company's fixed maturity investment portfolio did not contain exposure to any non-U.S. sovereign government or any other issuer that accounted for more than 10% of the Company's shareholder's equity. The Company keeps cash and cash equivalents in several banks and ensures that there are no significant concentrations at any point in time, in any one bank.

##### *Equities*

During 2017, the Company invested \$500 million in certain Exor managed equity funds. At December 31, 2017 the carrying value of these investments was \$551 million. See Note 16(d).

##### *Other Invested Assets*

In March 2016, the Company purchased from Exor S.A. a 36% shareholding in the privately held United Kingdom real estate investment and development group, Almacantar Group S.A. (Almacantar) for total cash consideration of approximately \$539 million. At December 31, 2017 and 2016, the total carrying value of the Almacantar investment accounted for under the equity method was \$538 million and \$436 million, respectively. See See Note 16(d).

##### *Derivatives*

To a lesser extent, the Company also has credit risk exposure as a party to foreign exchange forward contracts and other derivative contracts. The Company's investment strategy allows the use of derivative investments, subject to strict limitations. The Company imposes a high standard for the credit quality of counterparties in all derivative transactions. To mitigate credit risk, the Company monitors its exposure by counterparty, aims to diversify its counterparty credit risk and ensures that counterparties to these contracts are high credit quality international banks or counterparties. These contracts are generally of short duration (approximately 90 days) and settle on a net basis, which means that the Company is exposed to the movement of one currency against the other, as opposed to the notional amount of the contracts.

##### *Underwriting operations*

The Company is also exposed to credit risk in its underwriting operations, most notably in the credit/surety line. Loss experience in these lines of business is cyclical and is affected by the state of the general economic environment. The Company provides its clients in these lines of business with reinsurance protection against credit deterioration, defaults or other types of financial non-performance of or by the underlying credits that are the subject of the reinsurance provided and, accordingly, the Company is exposed to the credit risk of those credits. The Company mitigates the risks associated with

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

these credit-sensitive lines of business through the use of risk management techniques such as risk diversification, careful monitoring of risk aggregations and accumulations and, at times, through the use of retrocessional reinsurance protection and the purchase of credit default, total return and interest rate swaps.

The Company has exposure to credit risk as it relates to its business written through brokers, if any of the Company's brokers is unable to fulfill their contractual obligations with respect to payments to the Company. In addition, in some jurisdictions, if the broker fails to make payments to the insured under the Company's policy, the Company might remain liable to the insured for the deficiency. The Company's exposure to such credit risk is somewhat mitigated in certain jurisdictions by contractual terms.

The Company has exposure to credit risk related to reinsurance balances receivable, reinsurance recoverable on paid and unpaid losses, and funds held. The credit risk exposure related to these balances is mitigated by several factors, including but not limited to, credit checks performed as part of the underwriting process, monitoring of aged receivable balances and the contractual right to offset premiums receivable or funds held balances against unpaid losses and loss expenses. The Company regularly reviews its reinsurance recoverable balances to estimate an allowance for uncollectible amounts based on quantitative and qualitative factors. At December 31, 2017 and 2016, the Company has recorded a provision for uncollectible premiums receivable of \$1.2 million and \$6.2 million, respectively. The majority of the funds held balances are intercompany or collateralised with cash. See also Note 7 for discussion of credit risk related to reinsurance recoverable on paid and unpaid losses.

The Company is also subject to the credit risk of its cedants in the event of insolvency or the cedant's failure to honor the value of funds held balances for any other reason. However, the Company's credit risk in some jurisdictions is mitigated by a mandatory right of offset of amounts payable by the Company to a cedant against amounts due to the Company. In certain other jurisdictions the Company is able to mitigate this risk, depending on the nature of the funds held arrangements, to the extent that the Company has the contractual ability to offset any shortfall in the payment of the funds held balances with amounts owed by the Company to cedants for losses payable and other amounts contractually due.

**(b) Lease Arrangements**

The Company leases office space under an operating lease expiring in 2018. The lease is renewable at the option of the lessee under certain circumstances. The following is a schedule of future minimum rental payments, exclusive of escalation clauses, on the non-cancelable lease at December 31, 2017 (in thousands of U.S. dollars):

<b>Period</b>	<b>Amount</b>
2018.....	\$ 1,555
2019.....	794
2020.....	810
2021.....	826
2022.....	843
Total future minimum rental payments .....	<u>\$ 4,828</u>

Included in the above future minimum rental payments is a lease that is contractually payable by the Company, while a portion of the lease expense is paid for by the Parent. Rent expense for the years ended December 31, 2017 and 2016 was \$1.4 million and \$1.3 million, respectively.

**(c) Other Agreements**

The Company has entered into strategic investments with unfunded capital commitments. In the next five years, the Company expects to fund capital commitments totaling \$247.3 million, with \$79.9 million, \$64.9 million, \$51.3 million, \$51.3 million and \$nil to be paid during 2018, 2019, 2020, 2021 and 2022, respectively.

The Company has committed to a 10 year structured letter of credit facility issued by a high credit quality international bank, which has a final maturity of December 29, 2020. At December 31, 2017 and 2016, the Company's participation in the facility was \$67 million and \$62 million, respectively. At December 31, 2017, the letter of credit facility has not been drawn down and can only be drawn down in the event of certain specific scenarios, which the Company considers remote. Unless canceled by the bank, the credit facility automatically extends for one year, each year until maturity.



**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

On December 31, 2013, the Company entered into an agreement to guarantee the financial obligations of an affiliated company in the event of non-performance on ceded reinsurance agreements. At December 31, 2017, there were no cedants in default.

On June 2, 2017, the Company entered into an agreement to guarantee and indemnify any and all of the obligations of an affiliated company under reinsurance agreements with third party cedents, in the event of non-payment or non-performance. There were no amounts were due under this guarantee at December 31, 2017.

***(d) Legal Proceedings***

*Litigation*

The Company and its subsidiaries and branch, and the insurance and reinsurance industry in general, are subject to litigation and arbitration in the normal course of their business operations. In addition to claims litigation, the Company and its subsidiaries and branch may be subject to lawsuits and regulatory actions in the normal course of business that do not arise from or directly relate to claims on reinsurance treaties. This category of business litigation typically involves, among other things, allegations of underwriting errors or omissions, employment claims or regulatory activity. While the outcome of business litigation cannot be predicted with certainty, the Company will dispute all allegations against the Company and/or its subsidiaries and branch that Management believes are without merit.

At December 31, 2017, the Company was not a party to any litigation or arbitration that it believes could have a material effect on the financial condition, results of operations or liquidity of the Company.

**15. Credit Agreements**

In the normal course of its operations, the Parent enters into agreements with financial institutions to obtain unsecured and secured credit facilities. At December 31, 2017, the total amount of such credit facilities available to the Company was approximately \$367 million. Under the terms of certain reinsurance agreements, irrevocable letters of credit were issued by the Company on an unsecured and secured basis in the amount of \$10 million and \$18 million, respectively, at December 31, 2017, in respect of reported loss and unearned premium reserves.

**16. Agreements with Related Parties**

***(a) Reinsurance Agreements***

The Company enters into reinsurance contracts with subsidiaries of the Parent. As at December 31, 2017, the Company had the following reinsurance agreements with affiliated companies:

- a 45% quota-share agreement to assume new business from PartnerRe U.S.
- a 65% quota-share agreement to assume existing and new business from PartnerRe Europe.
- a 50% Quota Share agreement to assume new and renewal business from PartnerRe Asia.
- a 90% Quota Share agreement to assume new and renewal business from PartnerRe Corporate Member Limited.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

The activity included in the Consolidated Statements of Operations related to subsidiaries of the Parent for the years ended December 31, 2017 and 2016 was as follows (in thousands of U.S. dollars):

	2017	2016
Gross premiums written.....	\$ 2,475,656	\$ 2,029,367
Net premiums written .....	2,475,656	2,029,367
Net premiums earned .....	2,282,069	2,043,361
Net investment income on funds held.....	7,897	11,111
Losses and loss expenses .....	1,611,097	1,341,246
Acquisition costs.....	736,335	624,725

Included in the Consolidated Balance Sheets at December 31, 2017 and 2016 were the following balances related to subsidiaries of the Parent (in thousands of U.S. dollars):

	2017	2016
Reinsurance balances receivable.....	\$ 1,145,950	\$ 913,342
Funds held by reinsured companies.....	757,798	614,670
Deferred acquisition costs.....	360,616	267,573
Non-life Reserves.....	3,594,299	3,283,624
Life and Health Reserves.....	1,071,187	845,414
Unearned premiums .....	908,844	671,570
Other reinsurance balances payable.....	105,674	107,447

**(b) Loan Agreements**

During 2017, a loan agreement for €167 million with PartnerRe Holdings B.V., an affiliate was settled. The loan accrued interest at 5.4% per annum and the amount of interest income on the loan during 2017 and 2016 amounted to \$4.8 million and \$10.0 million, respectively.

The Company has a loan agreement for \$50 million with Aurigen Capital Limited, an affiliate. The loan was entered into on March 15, 2017 and accrues interest at the 3-month Libor plus 375 basis points per annum and matures on December 31, 2019. At December 31, 2017 the balance of the loan was \$39.4 million. The amount of interest income on the loan during 2017 amounted to \$1.3 million.

The Company has other advances to affiliates totaling \$831.6 million and \$162.3 million at December 31, 2017 and 2016, which are primarily related to amounts advanced to or paid on behalf of its Parent. These amounts bear no interest, have no fixed repayment terms and no collateral has been given.

The Company has other liabilities to affiliates totaling \$22.7 million and \$19.4 million, respectively, at December 31, 2017 and 2016, representing expenses incurred in the normal course of operations. Amounts due to affiliates bear no interest, have no fixed repayment terms and no collateral has been given.

In addition, accounts payable, accrued expenses and other at December 31, 2017 and 2016 also includes a deferred gain of \$85.3 million and \$84.3 million, respectively, related to an Assumption Reinsurance Agreement with the Canadian Life branch of PartnerRe Europe entered into in 2014.

**(c) Service Agreements**

In the normal course of its operations, the Company entered into service agreements with other subsidiaries of the Parent. Revenues earned under the service agreements for the years ended December 31, 2017 and 2016 were \$0.9 million and \$1.5 million, respectively. Expenses incurred under the service agreements for the years ended December 31, 2017 and 2016 were \$9.5 million and \$11.3 million, respectively.

**Partner Reinsurance Company Ltd.**  
**Notes to Consolidated Financial Statements - (Continued)**

*(d) Other*

***Almacantar Group S.A.***

In March 2016, the Company purchased from Exor S.A. a 36% shareholding in the privately held United Kingdom real estate investment and development group, Almacantar Group S.A. (Almacantar) for total cash consideration of approximately \$539 million. At December 31, 2017 and 2016, the total carrying value of the Almacantar investment accounted for under the equity method was \$538 million and \$436 million, respectively, and was included within other invested assets in the Consolidated Balance Sheets.

In March 2016, the Company purchased from Exor S.A. certain financial investments, mainly third-party equity funds, for cash consideration of approximately \$128 million.

These transactions between related parties were entered into at arms-length.

***Exor Funds***

During 2017, the Company invested \$500 million in certain Exor managed equity funds. At December 31, 2017 the carrying value of these investments was \$551 million, and was included within equities in the Consolidated Balance Sheet.

**17. Subsequent Events**

***Reinsurance Agreements with U.S. Affiliates***

Effective January 1, 2018, the Company entered into stop loss agreements with PartnerRe U.S. and PartnerRe America Insurance Company, subsidiaries of the Parent. The Company did not renew the 45% Quota Share agreement with PartnerRe U.S. for the 2018 underwriting year.