Independent auditor's report

To the Board of Directors and Shareholder of Hiscox Insurance Company (Bermuda) Limited

---

Our opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Hiscox Insurance Company (Bermuda) Limited (the Company) as at December 31, 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

What we have audited

The Company's financial statements comprise:

- the statement of financial position as at December 31, 2019;
- the statement of income and comprehensive income for the year then ended;
- the statement of changes in shareholder's equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

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

Independence

We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Chartered Professional Accountants of Bermuda Rules of Professional Conduct (CPA Bermuda Rules) that are relevant to our audit of the financial statements in Bermuda. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the CPA Bermuda Rules.

PricewaterhouseCoopers Ltd., Chartered Professional Accountants, P.O. Box HM 1171, Hamilton HM EX, Bermuda
T: +1 (441) 295 2000, F:+1 (441) 295 1242, www.pwc.com/bermuda

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers Ltd.

Chartered Professional Accountants
Hamilton, Bermuda

May 25, 2020

FINANCIAL STATEMENTS

Hiscox Insurance Company (Bermuda) Limited
Year Ended December 31, 2019
With Independent Auditor's Report

Hiscox Insurance Company (Bermuda) Limited

Financial Statements

Year Ended December 31, 2019

Contents

Independent Auditor's Report..1

Financial Statements:
Statement of Financial Position 2
Statement of Income and Comprehensive Income 3
Statement of Changes in Shareholder's Equity 4
Statement of Cash Flows 5
Notes to the Financial Statements...6

Report of the Independent Auditor

Hiscox Insurance Company (Bermuda) Limited
Statement of Financial Position

As of December 31, 2019
(expressed in thousands of U.S. dollars, except per share and share amounts)

	2019	2018	2017
Assets			
Cash and equivalents (Note 5)	$ 315,550	$ 213,452	$ 111,960
Financial assets carried at fair value (Notes 6,7 and 9)	1,160,560	1,365,873	1,415,589
Loans and receivables including reinsurance receivables (Notes 8 and 14)	606,502	383,466	544,714
Funds withheld (Note 11)	117,255	-	-
Reinsurance recoverable on unpaid claims (Notes 4 and 12)	1,344,011	875,171	553,082
Deferred acquisition costs (Note 10)	97,929	26,872	18,207
Prepaid reinsurance premiums (Note 12)	123,349	104,442	57,015
Total assets	$ 3,765,156	$ 2,969,276	$ 2,700,567
Liabilities			
Loss and loss adjustment expense reserve (Note 12)	$ 2,381,111	$ 1,689,436	$ 1,313,242
Unearned premium reserves (Note 12)	447,617	271,056	299,721
Trade and other payables (Notes 13 and 14)	338,066	314,967	222,807
Dividends payable (Notes 14 and 16)	-	80,000	-
Total liabilities	$ 3,166,794	$ 2,355,459	$ 1,835,770
Shareholder's equity			
Common shares (par value $1.00; authorized, issued and fully paid, 100,000,000)	$ 100,000	$ 100,000	$ 100,000
Contributed surplus	402,000	402,000	402,000
Retained earnings	96,362	111,817	362,797
Total shareholder's equity	598,362	613,817	864,797
Total liabilities and shareholder's equity	$ 3,765,156	$ 2,969,276	$ 2,700,567

The accompanying notes are an integral part of the financial statements

.

Hiscox Insurance Company (Bermuda) Limited
Statement of Income and Comprehensive Income

Year Ended December 31, 2019
(expressed in thousands of U.S. dollars)

	2019	2018
Income		
Gross premiums written	$ 1,154,388	$ 874,507
Change in unearned premium reserves	(111,745)	28,665
Gross premiums earned	1,042,643	903,172
Gross premiums ceded	511,621	471,948
Change in prepaid reinsurance premiums	(18,907)	(47,427)
Earned premiums ceded	492,714	424,521
Net premiums earned (Note 12)	549,929	478,651
Reinsurance commission income (Note 10)	60,204	47,041
Net investment income (Note 6)	54,690	7,975
Total income	664,823	533,667
Expenses		
Loss and loss adjustment expenses incurred	1,230,268	897,063
Reinsurance recoveries	(806,503)	(557,440)
Loss and loss adjustment expenses incurred, net (Note 12)	423,765	339,623
Acquisition costs (Note 10)	180,633	72,118
General and administrative expenses (Note 14)	9,994	9,929
Foreign exchange (gain)/loss	(2,114)	14,977
Total expenses	612,278	436,647
Other comprehensive income	-	-
Total comprehensive income for the year	$ 52,545	$ 97,020

The accompanying notes are an integral part of the financial statements

Hiscox Insurance Company (Bermuda) Limited
Statements of Changes in Shareholder's Equity

Year ended December 31, 2019
(expressed in thousands of U.S. dollars, except per share and share amounts)

	2019	2018
Common Shares		
Balance, beginning and end of year	100,000,000	100,000,000
Common Shares (Note 16)		
Balance, beginning and end of year	$ 100,000	$ 100,000
Contributed surplus (Note 16)		
Balance, beginning and end of year	$ 402,000	$ 402,000
Retained earnings		
Balance, beginning of year	111,817	362,797
Net income	52,545	97,020
Dividends declared (Note 16)	(68,000)	(348,000)
Balance, end of year	$ 96,362	$ 111,817
Total shareholder's equity	$ 598,362	$ 613,817

The accompanying notes are an integral part of the financial statements

Hiscox Insurance Company (Bermuda) Limited
Statements of Cash Flows

Year Ended December 31, 2019
(expressed in thousands of U.S. dollars)

	2019	2018
Operating activities		
Net income	$ 52,545	$ 97,020
Adjustments to reconcile net income to net cash provided by operating activities:		
Share compensation expense	357	(109)
Interest income	(24,526)	(25,604)
Unrealized (gains)/losses on foreign exchange	(4,175)	9,214
Net fair value (gains)/losses on financial assets	(3,362)	15,745
Changes in assets and liabilities:		
Financial assets carried at fair value	239,261	43,323
Loans and receivables including reinsurance receivables	(238,030)	148,866
Funds withheld	(118,697)	-
Prepaid reinsurance premiums	(18,909)	(47,427)
Deferred acquisition costs	(71,057)	(8,665)
Loss and loss adjustment expenses recoverable	(472,124)	(321,517)
Loss and loss adjustment expense reserves	703,320	397,792
Unearned premium reserves	176,561	(28,665)
Trade and other payables	24,625	98,129
Net cash provided by operating activities	245,789	378,102
Financing activities		
Dividends paid	(148,000)	(268,000)
Net cash used in financing activities	(148,000)	(268,000)
Net change in cash and cash equivalents	97,789	110,102
Cash and cash equivalents, beginning of year	213,452	111,960
Effect of exchange rate movements on cash	4,309	(8,610)
Cash and cash equivalents, end of year	$ 315,550	$ 213,452

The accompanying notes are an integral part of the financial statements

Hiscox Insurance Company (Bermuda) Limited
Notes to the Financial Statements
(expressed in thousands of U.S. dollars)

1. Company Information

Hiscox Insurance Company (Bermuda) Limited (the "Company") was incorporated under the laws of Bermuda on October 21, 2005. The Company is a global provider of property catastrophe and specialty reinsurance coverage to both third party and affiliate insurers and reinsurers. The Company is registered as a Class 4 insurer under The Insurance Act 1978 (Bermuda) and is a wholly owned subsidiary of Hiscox Ltd (the "Parent" or "Group"), a company incorporated in Bermuda and publicly traded on the London Stock Exchange. The Company's registered office is 96 Pitts Bay Road Pembroke, Bermuda.

2. Basis of Presentation

2.1 Statement of compliance

These financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the International Accounting Standards Board ("IASB"). These financial statements were examined by the Board of Directors and adopted at the meeting of the Board of Directors ("the Board") held on May 14, 2020.

2.2 Basis of measurement

The financial statements have been prepared on a going concern basis under the historical cost convention, except for certain financial instruments which are measured at fair value.

2.3 Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The financial statements are presented in United States Dollars, which is also the Company's functional currency.

2.4 Use of significant judgments, estimates and assumptions

The preparation of financial statements requires management to select accounting policies and make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses in the financial statements.

The Board reviews the reasonableness of critical judgments, estimates and assumptions applied and the appropriateness of significant accounting policies.

The following accounting policies are those considered to have a significant impact on the amounts recognised in the financial statements, with those judgments involving estimation summarised thereafter.
– Insurance contract: assessment of the significance of insurance risk transferred to the Company in determining whether a contract should be accounted for as an insurance contract or as a financial instrument;
– Financial assets: classification and measurement of investments including the application of the fair value option.

All estimates are based on management's knowledge of current facts and circumstances, assumptions based on that knowledge and their predictions of future events. Actual results may differ from those estimates, possibly significantly. Estimates are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The following describes items considered particularly susceptible to changes in estimates and assumptions.

The most critical estimate included in the Statement of Financial Position is the estimate for losses incurred but not reported. The total gross estimate as at December 31, 2019 is $1,526,875 (2018: $1,011,312) and is included within Loss and loss adjustment expense reserve in the Statement of Financial Position. The total estimate for the reinsurers' share of losses incurred but not reported as at December 31, 2019 is $955,643 (2018: $534,629).

Estimates of losses incurred but not reported are continually evaluated, based on entity-specific historical experience and contemporaneous developments observed in the wider industry when relevant, and are also updated for expectations of prospective future developments. Although the possibility exists for material changes in estimates to have a critical impact on the Company's reported performance and financial position, it is anticipated that the scale and diversity of the Company's portfolio considerably lessens the likelihood of this occurring. The overall reserving risk is discussed in more detail in Note 4.1 and the procedures used in estimating the cost of settling insured losses at the Statement of Financial Position date including losses incurred but not reported are detailed in Note 12.

The Company carries its financial assets at fair value through profit or loss, with fair values determined using published price quotations in the most active financial markets in which the assets trade, where available. Where quoted market prices are not available, valuation techniques are used to value financial instruments. These include third-party valuation reports and models utilising both observable and unobservable market inputs. The valuation techniques involve judgment with regard to the valuation models used and the inputs to these models, which can lead to a range of plausible valuations for financial assets.

3. Significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below.

3.1 Adoption of IFRS

The Company adopted IFRS in the preparation of its financial statements for the year ended December 31, 2019, which aligns the Company's reporting with that of its Parent. The date of transition to IFRS is January 1, 2019. In connection with the transition to IFRS, the Company has applied IFRS 1 "First-time adoption of International Financial Reporting Standards."

Upon transition to IFRS, the Company has adjusted the amounts in the financial statements that were prepared under US GAAP to prepare an opening IFRS Statement of Financial Position. The impact of the transition from US GAAP to IFRS on the financial position and cash flows is explained in the following reconciliation tables. There was no significant impact to the statement of income and comprehensive income. The adjustments made to the Statement of Financial Position were reclassifications only and had nil impact to shareholder's equity. There was no significant change in the statement of cashflows apart from reclassifications and minimal foreign exchange adjustment.

(expressed in U.S. dollars)

Adjustments to IFRS as of December 31, 2017

Assets	**US GAAP**	**Reclasses by line**	**Gross up derivative instruments**	**IFRS**
Investments in marketable securities	1,415,531	(1,415,531)		-
Cash and equivalents	111,960			111,960
Financial assets carried at fair value		1,415,531	58	1,415,589
Reinsurance balances receivable	279,429	(279,429)		-
Loans and receivables including reinsurance receivables		544,714		544,714
Reinsurance recoverable on unpaid claims	553,082			553,082
Deferred acquisition costs	18,207			18,207
Prepaid reinsurance premiums	57,015			57,015
Accrued interest receivable	6,204	(6,204)		-
Receivable for securities sold	13,102	(13,102)		-
Other assets	245,979	(245,979)		-
Total assets	**2,700,509**	**-**	**58**	**2,700,567**
Liabilities				
Loss and loss adjustment expense reserve	1,311,778	1,464		1,313,242
Unearned premium reserves	299,721			299,721
Reinsurance balances payable	188,453	(188,453)		-
Trade and other payables		222,749	58	222,807
Deferred income	6,989	(6,989)		-
Dividends payable	-			-
Other liabilities	28,771	(28,771)		-
Total liabilities	**1,835,712**	**-**	**58**	**1,835,770**
Shareholder's equity				
Share capital (par value $1.00; authorized, issued and outstanding, 100,000,000)	100,000			100,000
Contributed surplus	402,000			402,000
Retained earnings	362,797			362,797
Total shareholder's equity	**864,797**	**-**	**-**	**864,797**
Total liabilities and shareholder's equity	**2,700,509**	**-**	**58**	**2,700,567**

(expressed in U.S. dollars)

Adjustments to IFRS for the Year Ended December 31, 2018

	US GAAP	Reclasses by line	Remove all unrealised foreign exchange from Balance Sheet	IFRS
Operating activities				
Net income	97,020			97,020
Adjustments to reconcile net income to net cash provided by operating activities:				
Share compensation expense	(109)			(109)
Realized loss on marketable securities	1,884	(1,884)		-
Unrealized loss (gain) on marketable securities	15,745	(15,745)		-
Unrealized loss (gain) on foreign exchange	24,688		(15,474)	9,214
Sale (purchase) of investments, net	15,859	(15,859)		-
Net fair value gains/losses on financial assets		15,745		15,745
Interest income		(25,604)		(25,604)
Changes in operational assets and liabilities:				
Financial assets carried at fair value		43,347	(24)	43,323
Loans and receivables including reinsurance receivables		161,248	(12,382)	148,866
Reinsurance balances receivable	(1,835)	1,835		-
Prepaid reinsurance premiums	(47,427)			(47,427)
Deferred acquisition costs	(8,665)			(8,665)
Reinsurance recoverable on unpaid claims	(322,089)		572	(321,517)
Loss and loss adjustment expense reserves	379,912	(790)	18,670	397,792
Unearned premium reserves	(28,665)			(28,665)
Trade and other payables		88,624	9,505	98,129
Accrued interest receivable	(451)	451		-
Other assets	150,464	(150,464)		-
Receivable for securities sold	13,070	(13,070)		-
Reinsurance balances payable	45,957	(45,957)		-
Deferred income	(1,894)	1,894		-
Other liabilities	43,771	(43,771)		-
Net cash provided by operating activities	377,235	-	867	378,102
Financing activities				
Dividends paid	(268,000)	-		(268,000)
Net cash used in financing activities	(268,000)	-		(268,000)
Net change in cash and cash equivalents	109,235	-		110,102
Cash and cash equivalents, beginning of year	111,960	-		111,960
Effect of exchange rate movements on cash	(7,743)	-	(867)	(8,610)
Cash and cash equivalents, end of year	213,452	-	-	213,452

3.2 New accounting standards, interpretations and amendments to published standards

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2019. They have been applied in preparing these financial statements. There were no new standards, amendments or interpretations that had a material impact on the Company.

The new standards include:

IFRS 16 Leases
IFRS 16 supersedes IAS 17 Leases and sets out the principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 requires lessees to account for leases under a single on-Statement of Financial Position model. Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in IAS 17. The Company has not entered into any lease agreements and therefore there is no impact upon adoption.

Amendment to IAS 19 Plan Amendment, Curtailment or Settlement
The amendment to IAS 19 address the accounting for the current service cost and net interest when a plan amendment, curtailment or settlement occurs during a reporting period. The adoption of these amendments has no impact on the Company's financial statements.

The following new standards and amendment to standards, are effective for annual periods beginning after 1 January 2019 and have not been applied in preparing the financial statements:

IFRS 9 Financial Instruments
This standard incorporates new classification and measurement requirements for financial assets, the introduction of an expected credit loss impairment model which will replace the incurred loss model of IAS 39 and new hedge accounting requirements.

The Company satisfies the criteria set out in IFRS 4 Insurance Contracts for the temporary exemption from IFRS 9. At December 31, 2015 (the date specified by IFRS 4), the carrying value of the Company's liabilities connected with insurance comprised 97% of the total liabilities and the activities of the Company remain predominantly connected with insurance.

Under the current requirements (IAS 39), the Company's investments were designated as at fair value through profit or loss on initial recognition and subsequently remeasured to fair value at each reporting date, reflecting the Company's business model for managing and evaluating the investment portfolio. Adoption of IFRS 9 is not expected to result in any changes to the measurement of the Company's investments, which continues to be at fair value through profit or loss.

Financial assets within the scope of IFRS 17 Insurance Contracts such as premiums receivable and reinsurance and other recoveries on paid claims, which together form the majority of the carrying value of the Company's loans and receivables, and reinsurance recoveries on outstanding claims are outside the scope of IFRS 9 and are unaffected by the new requirements.

In addition to those balances, loans and receivables have other debtors and other accrued income which are within the scope of IFRS 9. Under IFRS 9, these assets continue to be recognised at amortised cost less impairment, with the measurement of impairment reflecting expected as well as incurred credit losses. As these balances are largely due to related parties, the Company does not expect the recognition of significant additional loss allowances under this approach compared to the current approach which will negatively impact equity. The Company will perform a detailed assessment in the future to determine the extent.

IFRS 17 Insurance Contracts
IFRS 17 will replace IFRS 4 and includes a number of significant changes to the measurement, presentation and disclosure of insurance contacts. It prescribes a general measurement model based on the discounted current estimates of future cashflows, including an explicit risk adjustment and a contractual service margin which represents the unearned profit of the contracts. Application of a simplified premium allocation approach, which is similar to the current unearned premium approach, is permitted if it provides a measurement that is not materially different from the general model or if the coverage period is one year or less. IFRS 17 requires any expected losses arising from loss-making contracts to be accounted for in the Statement of Income when the entity determines that losses are expected. The Company is evaluating the impact of adopting IFRS 17 on the financial statements which includes:

- performing a PAA eligibility assessment on group of (re)insurance contracts with coverage period more than one year;
- making initial accounting policy decisions under IFRS17 to continue amortising acquisition expenses and to present insurance finance income and expenses in the Statement of Income.

The Company's implementation programme is progressing in line with expectations. IFRS 17 is currently expected to be effective on January 1, 2023.

3.3 Insurance contracts

Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause the Company to make significant additional payments in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. The Company issues short term casualty and property insurance contracts that transfer significant insurance risk.

Premium revenue recognition

To the extent that the amount of written premium is estimable, the Company estimates the ultimate premiums for the entire contract period and records this estimate at the inception of the contract. For contracts where the full written premium is not estimable at inception, the Company records written premium for the portion of the contract period for which the amount is estimable. These estimates are based primarily on information in the underlying contracts as well as information provided by clients and/or brokers.

Premiums are stated before the deduction of acquisition costs and are earned over the exposure period in proportion to the period of risk covered. Unearned premiums represent the portion of premiums written that relate to the remaining term of the underlying policies in force.

Changes in premium estimates are expected and may result in adjustments in any reporting period. These estimates change over time as additional information regarding the underlying business volume is obtained. Any subsequent adjustments arising on such estimates are recorded in the period in which they are determined.

Where coverage is reinstated under pre-defined contract terms after the occurrence of a loss event, reinstatement premiums are recognized as written and recorded in the period in which they are determined. Accruals for reinstatement premiums are based on contractual terms applied to amounts of losses incurred with the only element of management judgment involved being with respect to the amount of loss reserves. Changes in estimates of reinstatement premiums are reflected in the period that changes in loss estimates are determined.

Reinsurance premiums ceded

The Company reduces the risk of losses on business written by reinsuring certain risks and exposures with other reinsurers. The Company remains liable to the extent that any retrocessionaire may fail to meet its obligations and to the extent that the Company does not hold sufficient security for their unpaid obligations. Ceded premiums are written during the period in which the risks incept and are expensed over the contract period in proportion to the period of risk covered. Prepaid reinsurance premiums consist of the unexpired portion of reinsurance ceded.

Reinsurance transactions that transfer risk but are retroactive are included in reinsurance assets. The excess of estimated liabilities for claims and claim expenses over the consideration paid is established as a deferred credit at inception. The deferred amounts are subsequently amortized using the recovery method over the settlement period of the reserves and reflected through the loss and loss adjustment expenses line in the Statements of Income. In transactions where the consideration paid exceeds the estimated liabilities for loss and loss adjustment expenses a loss is recognized immediately. If the adverse development exceeds the original loss, deferred gains are recorded. The deferred gains are subsequently recognized into earnings over the settlement period of the reserves.

Profit commissions on reinsurance ceded are calculated and accrued based on the expected loss experience for contracts and recorded when the current loss estimate indicates that a profit commission is probable under the contract terms. This is reported in Reinsurance commission income in the Statement of Income.

3.4 Fair Value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique.

This presumes that the transaction takes place in the principal (or most advantageous) market under current market conditions. Fair value is a market-based measure and in the absence of observable market prices in an active market, it is measured using the assumptions that market participants would use when pricing the asset or liability.

The fair value of a non-financial asset is determined based on its highest and best use from a market participant's perspective. When using this approach, the Company takes into account the asset's use that is physically possible, legally permissible and financially feasible. The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received.

If an asset or a liability measured at fair value has a bid price and an ask price, the price within the bid-ask spread that is most representative of fair value in the circumstances is used to measure fair value. An analysis of fair values of financial instruments and further details as to how they are measured are provide in Note 9.

3.5 Financial assets and liabilities including loans and receivables

The Company classifies its financial assets as: a) financial assets at fair value through profit and loss and b) loans and receivables. Management determines the classification of its financial assets based on the purpose for which the financial assets are held at initial recognition. The decision by the Company to designate debt and fixed income securities, equities and shares in unit trusts and deposits with credit institutions, at fair value through profit or loss reflects the fact that the investment portfolios are managed and their performance evaluated, on a fair value basis.

Purchases and sales of investments are accounted for at the trade date. Financial assets and liabilities are initially recognized at fair value. Subsequent to initial recognition financial assets and liabilities are measured as described below. Financial assets are derecognized when the right to receive cash flows from them expires or where they have been transferred and the Company has also transferred substantially all risks and rewards of ownership.

a) Financial assets at fair value through profit or loss
   A financial asset is classified into this category at inception if it is managed and evaluated on a fair value basis, if acquired principally for the purpose of selling in the short term, or if it forms part of a portfolio of financial assets in which there is evidence of short-term profit taking.

   The Company's investment portfolio comprises fixed income securities, certain traded mutual funds and other investments. These are carried at fair value with unrealized gains and losses included in the Statement of Income. Realised gains and losses are recognised in the Statement of Income using the specific identification method.

b) Loans and receivables
   Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Receivables arising from insurance contracts are included in this category and are reviewed for impairment as part of the impairment review of loans and receivables. Loan and receivables are carried at amortised cost less any provision for impairment value.

c) Netting of financial instruments

Financial assets and liabilities are only netted and recognized in the appropriate net amount if a corresponding legal claim (reciprocity, similarity and maturity) exists or is expressly agreed by the contract.

d) Derivative financial instruments
Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently valued at fair value at each Statement of Financial Position date. Fair values are obtained from quoted market values and, if these are not available, valuation techniques including option pricing models as appropriate. The method for recognising gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

None of the Company's derivatives have been designated as hedging instruments and; as such, fair value changes are recognized immediately in the Statement of Income.

3.6 Cash and cash equivalents

The Company has classified cash deposits and short-term highly liquid investments as cash and cash equivalents. These assets are readily convertible into known amounts of cash and are subject to inconsequential changes in value. Cash equivalents are financial investments with less than three months to maturity at the date of acquisition.

3.7 Funds withheld

Funds withheld are receivables from (re)insurers in the amount of their contractually withheld cash deposits and investments values. They are recognised at their nominal amount.

3.8 Receivables and Payables Related to Insurance Contracts

Receivables and payables are recognised when due and are carried at nominal value. If there is objective evidence that premiums receivables are impaired, the Company reduces the carrying amount of the insurance receivable accordingly and recognize the impairment loss in the Statement of Income.

3.9 Deferred acquisition costs (DAC)

Acquisition costs consist of commissions, brokerage and excise taxes that are related directly to the successful acquisition of new or renewal reinsurance contracts. These costs are deferred and amortized over the period in which the related premiums are earned.

At each Statement of Financial Position date, the Company performs a liability adequacy test to ensure the adequacy of the contract liabilities net of related DAC. In performing this test, the current best estimate of future contractual cash flows and claims handling and administration expenses, as well as the investment income from the assets backing the liabilities are used. Any deficiency is charged to profit and loss initially by writing off DAC and by establishing a provision for losses arising from the liability adequacy test.

3.10 Deferred Commission Income

Reinsurance commission income represents acquisition costs earned from ceding companies and is earned over the terms of the underlying reinsurance contracts. The unearned portion of the reinsurance commission income is recognized as Reinsurer's share of deferred acquisition costs under Trade and other payables.

3.11 Impairment of assets

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). For financial assets, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the value of the estimated future cash flows discounted at the financial asset's original effective interest rate. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior periods. A reversal of an impairment loss is recognised as income immediately. Impairment losses recognised in respect of goodwill are not subsequently reversed.

3.12 Loss and loss adjustment expense reserves and Reinsurance recoverable on unpaid claims

The Company's loss and loss adjustment expense reserves include case reserves and reserves for losses incurred but not yet reported ("IBNR reserves"). Case reserves are established for losses that have been reported, but not yet paid. IBNR reserves represent the estimated loss and loss adjustment expenses that have been incurred by insureds and reinsureds but not yet reported to the insurer or reinsurer, including unknown future developments on loss and loss adjustment expenses that are known to the insurer or reinsurer. IBNR reserves are established by management based on the methods described in Note 12.

Inherent in the estimate of ultimate loss and loss adjustment expenses are expected trends in claim severity and frequency and other factors that may vary significantly as claims are settled. Accordingly, ultimate loss and loss adjustment expenses may differ materially from the amounts recorded in the financial statements. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments, if any, are recorded in the Statement of Income in the period in which they become known.

As of December 31, 2019 and 2018, the Company did not deem any losses recoverable from reinsurers as uncollectible. Please refer to the section on credit risk for further discussion.

3.13 Related party transactions

IAS 24 defines related parties, among others, as parent companies and subsidiaries, subsidiaries of a common parent company, associated companies, legal entities under the influence of management and the management of the company itself.

All related party transactions have been recorded in accordance with IAS 24 and include business both assumed and ceded under usual market conditions. Please refer to Note 14 for related party disclosures.

3.14 Foreign currency translation

The Company's functional currency is the U.S. dollar. Transactions in foreign currencies are translated to U.S. dollars at the exchange rate in effect on the transaction date. Monetary assets and liabilities in foreign currencies are remeasured at the exchange rates in effect at the reporting date and foreign exchange gains and losses are included in the Statement of Income.

3.15 Income taxes and uncertain tax positions

Under current Bermuda law, the Company is not subject to any income or capital gains taxes. In the event that such taxes are imposed, the Company would be exempted from any such taxes until March 2035 pursuant to the Tax Assurance Certificates issued to such entities pursuant to the Bermuda Exempted Undertakings Tax Protection Act of 1966, as amended.

As of December 31, 2019 and 2018, the Company did not have any uncertain tax liabilities.

4. Management of risks

The Company adheres to the Group's overall appetite for accepting and managing varying classes of risk is defined by the Group's Board of Directors (the "Board"). The Board has developed a governance framework and has set Group-wide risk management policies and procedures which include risk identification, risk management and mitigation and risk reporting. The objective of these policies and procedures is to protect the Group's shareholders, policyholders and other stakeholders from negative events that could hinder the Group's delivery of its contractual obligations and its achievement of sustainable profitable economic and social performance.

The Board exercises oversight of the development and operational implementation of its risk management policies and procedures through the Group Risk Committee and ongoing compliance therewith, through a dedicated internal audit function, which has operational independence, clear terms of reference influenced by the Board's Non-Executive Directors and a clear upwards reporting structure back into the Board. The Group and the Company, in common with the non-life insurance industry generally, is fundamentally driven by a desire to originate, retain and service insurance contracts to maturity. The Company's cash flows are funded mainly through advance premium collections and the timing of such premium inflows is reasonably predictable. In addition, the majority of material cash outflows are typically triggered by the occurrence of insured events, although the timing, frequency and severity of claims can fluctuate.

The principal sources of risk relevant to the Company's operations and its financial statements fall into two broad categories: insurance risk and financial risk, which are described in Notes 4.1 and 4.2 below. The Company also actively manages its capital risks as detailed in Note 4.3.

The proliferation of COVID 19 during 2020 (see Note 18), has caused a heightened level of risk across various aspects of the insurance, financial and capital risks described below. The Company continues to manage these risks within its existing risk management framework.

4.1 Insurance Risk

The predominant risk to which the Company is exposed is insurance risk which is assumed through the underwriting process. Insurance risk can be sub-categorised into i) underwriting risk including the risk of catastrophe and systemic reinsurance losses and the reinsurance competition and cycle, and ii) reserving risk.

i) Underwriting risk
The Board sets the Company's underwriting strategy and risk appetite seeking to exploit identified opportunities in light of other relevant anticipated market conditions. The Board requires the Company's underwriters to operate within an overall Group appetite for individual events. This defines the maximum exposure that the Company is prepared to retain on its own account for any one potential catastrophe event or disaster.

Consistent with the Group, the Company's underwriting risk appetite seeks to ensure that it should not lose more than 40% of core capital, defined as NAV less expected dividend, plus expected investment income, as a result of a one in 200 aggregate bad underwriting year.

Specific underwriting objectives such as aggregation limits, reinsurance protection thresholds and geographical disaster event risk exposures are prepared and reviewed by the Chief Underwriting Officer in order to translate the Board's summarised underwriting strategy into specific measurable actions and targets. These actions and targets are reviewed and approved by the Board in advance of each underwriting year. The Board continually reviews its underwriting strategy throughout each underwriting year in light of the evolving market pricing and loss conditions and as opportunities present themselves. The underwriters and management consider underwriting risk at an individual contract level, and also from a portfolio perspective where the risks assumed in similar classes of policies are aggregated and the exposure evaluated in light of historical portfolio experience and prospective factors.

To assist with the process of pricing and managing underwriting risk the Group routinely performs a wide range of activities including the following:
– regularly updating the Group's risk models;
– documenting, monitoring and reporting on the Group's strategy to manage risk;
– developing systems that facilitate the identification of emerging issues promptly;
– utilising sophisticated computer modelling tools to simulate catastrophes and measure the resultant potential losses before and after reinsurance;
– monitoring legal developments and amending the wording of policies when necessary;
– regularly aggregating risk exposures across individual underwriting portfolios and known accumulations of risk;
– examining the aggregated exposures in advance of underwriting further large risks; and
– developing processes that continually factor market intelligence into the pricing process.

The delegation of underwriting authority to specific individuals is subject to regular review. All underwriting staff are set strict parameters in relation to the levels and types of business they can underwrite, based on individual levels of experience and competence. These parameters cover areas such as the maximum sums insured per insurance contract, maximum gross premiums written and maximum aggregated exposures per geographical zone and risk class. Regular meetings are held between the Chief Underwriting Officer and a specialist team in order to monitor claim development patterns and discuss individual underwriting issues as they arise.

The Group compiles estimates of losses arising from realistic disaster events using statistical models alongside input from its underwriters. These require significant management judgment. Realistic disaster scenarios are extreme hypothetical events selected to represent major events occurring in areas with large insured values. They also reflect the areas that represent significant exposures for the Company.

The selection of realistic disaster scenario events is adjusted each year and they are not therefore necessarily directly comparable from one year to the next. The events are extreme and unprecedented, and as such these estimates may prove inadequate as a result of incorrect assumptions, model deficiencies, or losses from unmodelled risks. This means that should a realistic disaster actually eventuate, the Company's final ultimate losses could materially differ from those estimates modelled by management. The Company's insurance contracts include provisions to contain losses, such as the ability to impose deductibles and demand reinstatement premiums in certain cases. In addition, in order to manage the Company's exposure to repeated catastrophic events, relevant policies frequently contain payment limits to cap the maximum amount payable from these insured events over the contract period.

Underwriting risk is also managed by purchasing reinsurance. Reinsurance protection may be in the form of quota share reinsurance or excess of loss cover and is purchased at an entity level but is also considered at an overall Group level to mitigate the effect of catastrophes and unexpected concentrations of risk. However, the scope and type of reinsurance protection purchased may change depending on the extent and competitiveness of cover available in the market.

Below is a summary of the gross and net insurance liabilities. The estimated liquidity profile to settle the gross claims liabilities is given in Note 12.

Estimated concentration of gross and net insurance liabilities:

	Property	Casualty and Others	Total
		($ in thousands)	
December 31, 2019			
Gross	$ 1,513,176	$ 867,935	$ 2,381,111
Recoverable	1,272,851	71,160	1,344,011
Net	$ 240,325	$ 796,775	$ 1,037,100
December 31, 2018			
Gross	$ 1,003,474	$ 685,962	$ 1,689,436
Recoverable	834,659	40,512	875,171
Net	$ 168,815	$ 645,450	$ 814,265

The Company's property reinsurance inwards acceptances are primarily focused on large commercial property, homeowner and crop exposures held by other insurance companies predominantly in North America and other developed economies. This business is characterised more by large claims arising from individual events or catastrophes. Multiple insured losses can periodically arise out of a single natural or man-made occurrence. The main circumstances that result in claims against the reinsurance inwards book are conventional catastrophes, such as earthquakes or storms, and other events including fires and explosions. The occurrence and impact of these events are very difficult to model over the short term which complicates attempts to anticipate loss frequencies on an annual basis. In those years where there is a low incidence of severe catastrophes, loss experience on the reinsurance inwards book can be relatively low.

A significant proportion of the reinsurance inwards business provides cover on an excess of loss basis for individual events. The Company agrees to reimburse the cedant once their losses exceed a minimum level. Consequently, the frequency and severity of reinsurance inwards claims are related not only to the number of significant insured events that occur but also to their individual magnitude. If numerous catastrophes occurred in any one year, but the cedant's individual loss on each was below the minimum stated, then the Company would have no liability under such contracts. Maximum gross line sizes and aggregate exposures are set for each type of programme.

The Company writes reinsurance risks for periods of mainly one year so that contracts can be assessed for pricing and terms and adjusted to reflect any changes in market conditions.

The Company also writes casualty reinsurance on a quota share basis from affiliates and the strategy attempts to ensure that the underwritten risks are well diversified in terms of type and amount of potential hazard, industry and geography. However, the Company's exposure is more focused towards professional, general and technological liability risks rather than human bodily injury risks, which are only accepted under limited circumstances. Claims typically arise from incidents such as errors and omissions attributed to the insured, professional negligence and specific losses suffered as a result of electronic or technological failure of software products and websites.

The provision of insurance to cover allegations made against individuals acting in the course of fiduciary or managerial responsibilities, including directors' and officers' insurance is one example of a casualty insurance risk.

The Company's casualty reinsurance contracts mainly experience low severity attritional losses. By nature, some of these losses may take longer to settle than the other categories of business. In addition, there is increased potential for accumulation in casualty risk due to the growing complexity of business, technological advances, and greater interconnectivity and interdependency across the world due to globalisation.

The market for cyber insurance is still a relatively immature one, complicated by the fast-moving nature of the threat, as the world becomes more connected. The risks associated with cyber insurance are multiplying in both diversity and scale, with associated financial and reputational consequences of failing to prepare for them. The volume of cyber-related claims are relatively small at present but are only going to grow.

ii) Reserving risk

The Company's procedures for estimating the outstanding costs of settling insured losses at the Statement of Financial Position date, including claims incurred but not yet reported, are detailed in Note 12.

The Company's provision estimates are subject to rigorous review by senior management from all areas of the business. The final provision is approved by the Board on the recommendation of the reserving committee.

The short-tailed property reinsurance claims are normally mostly notified and settled within 12 to 24 months of the insured event occurring. There is often a time lag between the establishment and re-estimate of case reserves and reporting to the Company. The Company works closely with the reinsured to ensure timely reporting and also centrally analyses industry loss data to verify the reported reserves.

Those claims taking the longest time to develop and settle typically relate to casualty risks where legal complexities occasionally develop regarding the insured's alleged omissions or negligence. The length of time required to obtain definitive legal judgments and make eventual settlements exposes the Company to a degree of reserving risk in an inflationary environment.

The final quantum for casualty claims may not be established for many years after the event. Consequently, a significant proportion of the casualty insurance amounts reserved on the Statement of Financial Position may not be expected to settle within 24 months of the Statement of Financial Position date. This has been considered in the reserving process.

4.2 Financial Risk

The Company is exposed to financial risk through its ownership of financial instruments including financial liabilities which collectively represent a significant element of the shareholder equity. The Company invests in financial assets in order to fund obligations arising from its insurance contracts and financial liabilities.

The key financial risk for the Company is that the proceeds from its financial assets and investment result generated thereon are not sufficient to fund the obligations. The most important elements and economic variables that could result in such an outcome relate to the reliability of fair value measures, equity price risk, interest rate risk, credit risk, liquidity risk and currency risk. The Company's policies and procedures for managing exposure to these specific categories of risk are detailed below.

i) Market risk

The Company has elected to carry loans and receivables at amortised cost and all financial investments at fair value through profit or loss as they are managed and evaluated on a fair value basis in accordance with a documented strategy. With the exception of unquoted equity investments shown in Note 9, all of the financial investments held by the Company are available to trade in markets and the Company therefore seeks to determine fair value by reference to published prices or as derived by pricing vendors using observable quotations in the most active financial markets in which the assets trade. The fair value of financial assets is measured primarily with reference to their closing market prices at the Statement of Financial Position date. The ability to obtain quoted market prices may be reduced in periods of diminished liquidity. In addition, those quoted prices that may be available may represent an unrealistic proportion of market holdings or individual trade sizes that could not be readily available to the Company. In such instances fair values may be determined or partially supplemented using other observable market inputs such as prices provided by market makers such as dealers and brokers, and prices achieved in the most recent regular transaction of identical or closely related instruments occurring before the Statement of Financial Position date but updated for relevant perceived changes in market conditions.

At 31 December 2019, the Company holds asset-backed and mortgage-backed fixed income instruments in its investment portfolio, but has minimal direct exposure to sub-prime asset classes. Together with the Group's investment managers, management continues to monitor the potential for any adverse development associated with this investment exposure through the analysis of relevant factors such as credit ratings, collateral, subordination levels and default rates in relation to the securities held. The Company did not experience any material defaults on debt securities during the year.

Valuation of these securities will continue to be impacted by external market factors including default rates, rating agency actions, and liquidity. The Company will make adjustments to the investment portfolio as appropriate as part of its overall portfolio strategy, but its ability to mitigate its risk by selling or hedging its exposures may be limited by the market environment. The Company's future results may be impacted, both positively and negatively, by the valuation adjustments applied to these securities.

Note 9 provides an analysis of the measurement attributes of the Company's financial instruments.

ii) Equity price risk

The Company is exposed to equity price risk through its holdings of equity and unit trust investments. This is limited to a relatively small and controlled proportion of the overall investment portfolio and the equity and unit trust holdings involved are diversified over a number of companies and industries. The fair value of equity assets in the Statement of Financial Position at 31 December 2019 was $135,487 (2018: $128,565).

(expressed in U.S. dollars)

These may be analysed as follows:

Nature of equity and unit trust holdings	**2019 % weighting**	**2018 % weighting**
Directly held equity securities	0%	0%
Units held in funds – traditional long only	19%	44%
Units held in funds – long and short and special strategies	81%	56%
Geographic focus		
Specific UK mandates	8%	0%
Global mandates	92%	100%

The allocation of equity risk is not heavily confined to any one market index so as to reduce the Company's exposure to individual sensitivities. The Company makes an allocation to less volatile, absolute return strategies within its risk assets, so as to balance its desire to maximise returns with the need to ensure capital is available to support underwriting throughout any downturn in financial markets. A 10% downward correction in equity prices at 31 December 2019 would have been expected to reduce the Company's equity and profit after tax for the year by approximately $13.5 million (2018: $12.9 million) assuming that the only area impacted was equity financial assets. A 10% upward movement is estimated to have an equal but opposite effect.

iii) Interest rate risk

Fixed income investments represent a significant proportion of the Company's assets and the Board continually monitors investment strategy to minimise the risk of a fall in the portfolio's market value which could affect the amount of business that the Company is able to underwrite or its ability to settle claims as they fall due. The fair value of the Company's investment portfolio of debt and fixed income securities is normally inversely correlated to movements in market interest rates. If market interest rates rise, the fair value of the Company's debt and fixed income investments would tend to fall and vice versa if credit spreads remained constant. Debt and fixed income assets are predominantly invested in high-quality corporate, government and asset-backed bonds. The investments typically have relatively short durations and terms to maturity. The portfolio is managed to minimise the impact of interest rate risk on anticipated Company cash flows.

The Company may also, from time to time, enter into interest rate future contracts in order to reduce interest rate risk on specific portfolios. The fair value of debt and fixed income assets in the Company's Statement of Financial Position at 31 December 2019 was $1,023,655 (2018: $1,235,858).

One method of assessing interest rate sensitivity is through the examination of duration-convexity factors in the underlying portfolio. Using a duration-convexity-based sensitivity analysis, if market interest rates had risen by 100 basis points at the Statement of Financial Position date, the Company equity and profit after tax for the year might have been expected to decrease by approximately $32.2 million (2018: $42.5 million) assuming that the only Statement of Financial Position area impacted was debt and fixed income financial assets. Duration is the weighted average length of time required for an instrument's cash flow stream to be recovered, where the weightings involved are based on the discounted present values of each cash flow. A closely related concept, modified duration, measures the sensitivity of the instrument's price to a change in its yield to maturity. Convexity measures the sensitivity of modified duration to changes in the yield to maturity. Using these three concepts, scenario modelling derives the above estimated impact on instruments' fair values for a 100-basis point change in the term structure of market interest rates.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest-bearing. The Company's debt and fixed income assets are further detailed at Note 9.

iv) Credit risk

The Company has exposure to credit risk, which is the risk that a counterparty will suffer a deterioration in perceived financial strength or be unable to pay amounts in full when due. The concentrations of credit risk exposures held by insurers may be expected to be greater than those associated with other industries, due to the specific nature of reinsurance markets and the extent of investments held in financial markets. In both markets, the Company interacts with a number of counterparties who are engaged in similar activities with similar customer profiles, and often in the same geographical areas and industry sectors. Consequently, as many of these counterparties are themselves exposed to similar economic characteristics, one single localised or macroeconomic change could severely disrupt the ability of a significant number of counterparties to meet the Company's agreed contractual terms and obligations.

Key areas of exposure to credit risk include:
– reinsurers' share of reinsurance liabilities;
– amounts due from reinsurers in respect of claims already paid;
– amounts due from reinsurance contract holders; and
– counterparty risk with respect to cash and cash equivalents, and investments including deposits and derivative transactions

The Company's maximum exposure to credit risk is represented by the carrying values of financial assets and reinsurance assets included in the Statement of Financial Position at any given point in time. The Company does not use credit derivatives or other products to mitigate maximum credit risk exposures on reinsurance assets, but collateral may be requested to be held against these assets. The Company structures the levels of credit risk accepted by placing limits on its exposure to a single counterparty, or groups of counterparties, and having regard to geographical locations. Such risks are subject to an annual or more frequent review. There is no significant concentration of credit risk with respect to loans and receivables, as the Company has a large number of internationally dispersed debtors with unrelated operations. Retrocession is used to contain insurance risk. This does not, however, discharge the Company's liability as primary reinsurer. If a retrocessionaire fails to pay a claim for any reason, the Company remains liable for the payment to the reinsured. The creditworthiness of retrocessionaires is therefore continually reviewed throughout the year.

The Credit Committee assesses the creditworthiness of all reinsurers by reviewing credit grades provided by rating agencies and other publicly available financial information detailing their financial strength and performance as well as detailed analysis from the Group's internal credit analysis team. The Committee considers the reputation of its reinsurance partners and also receives details of recent payment history and the status of any ongoing negotiations between Group companies and these third parties. This information is used to update the reinsurance purchasing strategy.

The financial analysis of retrocession partners produces an assessment categorised by S&P rating (or equivalent when not available from S&P). Despite the rigorous nature of this assessment exercise, and the resultant restricted range of counterparties with acceptable strength and credit credentials that emerges therefrom, some degree of credit risk concentration remains inevitable.

A credit risk exists should any of our retrocessionaires be unable to fulfill their contractual obligations with respect to the payment of reinsurance balances due to the Company. As at December 31, 2019, of the $1,344.0m (2018: $875.2) of loss and loss adjustment expenses recoverable, approximately 23% (2018: 25%) or $307.9m (2018: $213.4) are due from cedants who are not required to provide collateral and are rated ‘A’ or above. Of the remaining 77% (2018: 75%) or $1,036.1m (2018: $661.8), we hold collateral of $1,010.7m (2018: $657.2) in trusts for which we are the beneficiary or trade with the counterparty on a funds withheld basis.

As at December 31, 2019 of the Company’s total Reinsurance Balances Receivable of $560.8m (2018: $170.2m), $400.3m (2018: $281.3) were due from Hiscox affiliates. External reinsurance balances receivable of $160.5m (2018: $111.1) have been evaluated and at December 31, 2019, the Company does not deem any of its reinsurance balances receivable as uncollectible.

The Company also mitigates counterparty credit risk by concentrating debt and fixed income investments in high-quality instruments, including a particular emphasis on government bonds issued mainly by North American countries and the European Union. The Company has no direct exposure to sovereign debt in Spain, Italy, Ireland, Greece or Portugal. For the current and prior period, the Company did not experience any material defaults on debt securities.

An analysis of the Company’s exposure to counterparty credit risk in its portfolio of fixed income securities, based on S&P or equivalent rating is presented below:

	2019	**2018**
	($ in thousands)	
Government and government agencies		
U.S.	$ 424,775	$ 557,157
Non-U.S.	105,037	174,198
AAA	78,724	113,491
AA	69,290	46,665
A	188,958	197,532
BBB	155,671	144,578
Non-investment grade *	1,200	2,237
Total investments in fixed income securities	$ 1,023,655	$ 1,235,858

* *Fixed income securities with a rating of below BBB*

Of cash and cash equivalents, 16% (2018: 9%) are held at a U.S. financial institution rated A+ by Fitch Ratings, 67% (2018: 79%) at a Bermuda financial institution rated A- by Standard & Poor's, 9% (2018: 6%) represent U.S. and Japanese Government Treasury Bills and Corporate Debt classified as cash equivalents due to their short duration, rated A-1+ by Standard & Poor's, 8% (2018: 0%) at a S&P AAA rated liquidity fund and 0% (2018: 4%) of cash and cash equivalents are held at a U.S. financial institution rated A1 by Moody's. The Company's management evaluates the financial strength and stability of these institutions on a periodic basis. The Company's investment portfolio is managed by external investment managers in accordance with the Company's investment guidelines.

v) Liquidity Risk

The Company is exposed to daily calls on its available cash resources, mainly from claims arising from its reinsurance contracts. Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Board sets limits on the minimum level of cash and maturing funds available to meet such calls.

A significant proportion of the Company's investments is in highly liquid assets which could be converted to cash in a prompt fashion and at minimal expense. The Company's exposure to equities is concentrated on shares and funds that are traded on internationally recognised stock exchanges.

The main focus of the investment portfolio is on high-quality, short-duration debt and fixed income securities and cash. There are no significant holdings of investments with specific repricing dates. Notwithstanding the regular interest receipts and also the Company's ability to liquidate these securities and the majority of its other financial instrument assets for cash in a prompt and reasonable manner, the contractual maturity profile of the fair value of these securities at 31 December is disclosed in Note 6.

The available headroom of working capital is monitored through the use of a detailed Company cash flow forecast which is reviewed by management quarterly or more frequently as required.

The following is an analysis of the estimated timing of net cash outflows based on the gross claims liabilities held. The Company does not discount claims liabilities. The estimated phasing of settlement is based on current estimates and historical trends and the actual timing of future settlement cash flows may differ materially from the disclosure below.

	2019	**2018**
	($ in thousands)	
Within one year	$ 1,261,989	$ 895,401
Between one and two years	571,467	405,465
Between two and five years	428,600	304,098
Over five years	119,055	84,472
Total claims liabilities	$ 2,381,111	$ 1,689,436

vi) Currency risk

Currency risk is the risk of loss resulting from fluctuations in exchange rates. The Company's exposures to foreign exchange risk arise mainly with respect to the Pound Sterling and the Japanese Yen, which arises from the conversion of foreign currency transactions resulting from the activities of entering into reinsurance, investment and operational contracts in a currency that is different to its functional currency.

Operational foreign exchange risk is principally managed by broadly matching assets and liabilities by currency and liquidity. Due attention is paid to local regulatory solvency and risk-based capital requirements. All foreign currency derivative transactions with external parties are managed centrally.

The Company does not hedge operational foreign exchange risk arising from the accounting mismatch due to the translation of monetary and non-monetary items. Non-monetary items including unearned premiums, deferred acquisition costs and reinsurers' share of unearned premiums, are recorded at historical transaction rates and are not remeasured at the reporting date. Monetary items including claims reserves, reinsurers' share of claims reserves, and investments are remeasured at each reporting date at the closing rates.

The Company's use of currency derivatives is disclosed in Note 7.

4.3 Capital Risk Management

The Company's primary objectives when managing its capital position are:
– to safeguard its ability to continue as a going concern
– to provide an adequate return to the Group by pricing its insurance products and services commensurately with the level of risk;
– to maintain an efficient cost of capital;
– to comply with all regulatory requirements by an appropriate margin;
– to settle policyholders' claims as they arise.
Additionally, the Company complies with all capital requirements set by its regulator, the Bermuda Monetary Authority ("the Authority"). Please refer to Note 17 for additional disclosures on statutory requirements.

5. Cash and cash equivalents

	2019	2018
	($ in thousands)	
Cash at bank	$ 285,696	$ 196,449
Short-term deposits	29,854	17,003
Total cash and cash equivalents	$ 315,550	$ 213,452

Cash includes overnight deposits and money market funds. Short-term deposits represent debt securities with an original maturity date of less than three months.

6. Financial assets and liabilities and net investment income

Financial assets designated at fair value through profit or loss are measured at fair values, with all changes from one accounting period to the next being recorded through the Statement of Income.

	2019	2018
	($ in thousands)	
Debt and fixed income securities	$ 1,023,655	$ 1,235,858
Equities and shares in unit trusts	135,487	128,565
Total investments	1,159,142	1,364,423
Derivative assets	1,418	1,450
Total financial assets carried at fair value	$ 1,160,560	$ 1,365,873

The effective maturity of debt and fixed income securities due within and after one year are as follows:

	2019	2018
	($ in thousands)	
Less than one year	$ 379,117	$ 399,292
Between one and two years	240,143	270,508
Between two and five years	269,793	416,139
Over five years	134,602	149,919
Total debt and fixed income securities	$ 1,023,655	$ 1,235,858

The Company’s equities and shares in unit trusts and other non-dated instruments have no contractual maturity terms but could also be liquidated in an orderly manner for cash in a prompt and reasonable time frame within one year of the Statement of Financial Position date.

Investments at 31 December are denominated in the following currencies at fair value:

	2019	2018
	($ in thousands)	
Debt and fixed income securities		
US Dollars	$ 819,295	$ 927,202
Sterling	204,359	217,430
Other currencies	1	91,226
	$ 1,023,655	$1,235,858
Equities and shares in unit trusts		
US Dollars	$ 135,487	$ 128,565
	$ 135,487	$ 128,565
Total investments	$ 1,159,142	$ 1,364,423

The financial liabilities carried at fair value is comprised of derivative instruments amounting to $340 (2018: $775) and is all due within one year. This is included within Trade and other payables.

The following table summarises the Company's net investment results:

	2019	2018
	($ in thousands)	
Investment income including interest receivable	$ 24,526	$ 25,604
Net realised gains/(losses) on investments at fair value through profit or loss	28,865	(2,164)
Net fair value gains/(losses) on investments at fair value through profit or loss	3,041	(16,074)
Investment income-financial assets	56,432	7,366
Net fair value gains/(losses) on derivative instruments	(1,742)	609
Total net investment income	$ 54,690	$ 7,975

7. Derivative financial instruments

The Company entered into both exchange-traded and over-the-counter derivative contracts for a number of purposes during 2019 and 2018. The Group had the right and intention to settle each contract on a net basis. The assets and liabilities of these contracts at December 31, 2019 all mature within one year of the Statement of Financial Position date and are detailed below:

31 December 2019

	Gross Contract Notional Amount	**Fair Value of Assets**	**Fair value of liabilities**	**Net**
		($ in thousands)		
Foreign exchange forward contracts	140,953	$ 1,418	$ (340)	$ 1,078
Interest rate future contracts	-	-	-	-
		$ 1,418	$ (340)	$ 1,078

The foreign exchange forward contracts are represented by gross fair value of assets and liabilities as detailed below:

	Fair Value of Assets	**Fair value of liabilities**	**Net**
	($ in thousands)		
Gross fair value of assets	$ 124,362	$ 16,439	$ 140,801
Gross fair value of liabilities	(122,944)	(16,779)	(139,723)
	$ 1,418	$ (340)	$ 1,078

31 December 2018

	Gross Contract Notional Amount	**Fair Value of Assets**	**Fair value of liabilities**	**Net**
		($ in thousands)		
Foreign exchange forward contracts	92,514	$ 1,450	$ (560)	$ 890
Interest rate future contracts	16,334	-	(215)	(215)
		$ 1,450	$ 775	$ 675

The foreign exchange forward contracts are represented by gross fair value of assets and liabilities as detailed below:

	Fair Value of Assets	Fair value of liabilities	Net
	($ in thousands)		
Gross fair value of assets	$ 71,744	$ 20,789	$ 92,533
Gross fair value of liabilities	(70,294)	(21,349)	(91,643)
	$ 1,450	$ (560)	$ 890

Derivative investments comprise Japanese Yen, Pound Sterling, Euro and Australian Dollar forward contracts as well as interest rate futures contracts, collectively with notional amounts of $140.9m (2018: $108.9m). The Company recognized in the Statement of Income, within Net investment income, a net exchange loss of $1.4m (2018: $0.7m gain) on its forward contract holdings and a net loss of $0.3m (2018: $0.1m loss) on its interest rate futures holdings. None of the Company's derivatives have been designated as hedging instruments and; as such, fair value changes are recognized immediately in the Statement of Income.

8. Loans and receivables including insurance receivables

	2019	2018
	($ in thousands)	
Reinsurance balances receivable	$ 560,849	$ 281,264
Other debtors including related party	25,485	85,491
Receivables for investments sold	15,018	32
Accrued interest	5,150	6,655
Subscriptions paid in advance and other assets	-	10,024
Total loans and receivables including insurance receivables	$ 606,502	$ 383,466

Included in Reinsurance balances receivable is $215m (2018: $Nil) related to our assumed quota share arrangement with an affiliate which is withheld by the affiliate. Under this arrangement, cash and investments of $117.3m are also held by the affiliate as disclosed in Note 11. These assets will be settled net of outstanding claims of $272.5m (2018: $Nil) as presented within the Loss and loss adjustment expense reserve on the statement of financial position.

The amounts expected to be recovered before and after one year are estimated as follows:

	2019	2018
	($ in thousands)	
Within one year	$ 372,471	$ 371,042
After one year	234,031	12,424
Total loans and receivables including insurance receivables	$ 606,502	$ 383,466

There is no significant concentration of credit risk with respect to loans and receivables as the Company has a large number of internationally dispersed debtors. No impairment allowance on loans and receivables were required as of the Statement of Financial Position dates.

9. Fair value measurements

In accordance with IFRS 13 Fair Value Measurement, the fair value of financial instruments based on a three-level fair value hierarchy that reflects the significance of the inputs used in measuring the fair value, is set out below.

2019	**Level 1**	**Level 2**	**Level 3**	**Total**
		($ in thousands)		
Government and government agencies				
U.S.	$ 351,720	$ 73,054	$ -	$ 424,774
Non-U.S.	69,697	35,340	-	105,037
Corporate securities	-	422,955	-	422,955
Asset-backed securities	-	38,864	-	38,864
Mortgage-backed securities - residential	-	28,112	-	28,112
Mortgage-backed securities - commercial	-	3,913	-	3,913
Derivative instruments	-	1,418	-	1,418
Other investments	-	134,698	789	135,487
Total financial assets carried at fair value	$ 421,417	$ 738,354	$ 789	$ 1,160,560

2018

	Level 1	Level 2	Level 3	Total
		($ in thousands)		
Government and government agencies				
U.S.	$ 487,237	$ 69,920	$ -	$ 557,157
Non-U.S.	95,282	78,916	-	174,198
Corporate securities	-	420,040	-	420,040
Asset-backed securities	-	47,092	-	47,092
Mortgage-backed securities - residential	-	20,220	-	20,220
Mortgage-backed securities - commercial	-	17,151	-	17,151
Derivative instruments	-	1,450	-	1,450
Other investments	-	127,452	1,113	128,565
Total financial assets carried at fair value	$ 582,519	$ 782,241	$ 1,113	$ 1,365,873

The levels of the fair value hierarchy are defined by the standard as follows:
– Level 1 – fair values measured using quoted prices (unadjusted) in active markets for identical instruments;
– Level 2 – fair values measured using directly or indirectly observable inputs or other similar valuation techniques for which all significant inputs are based on market observable data;
– Level 3 – fair values measured using valuation techniques for which significant inputs are not based on market observable data.

The fair values of the Company's financial assets are based on prices provided by investment managers who obtain market data from numerous independent pricing services. The pricing services used by the investment manager obtain actual transaction prices for securities that have quoted prices in active markets. For those securities which are not actively traded, the pricing services use common market valuation pricing models. Observable inputs used in common market valuation pricing models include, but are not limited to, broker quotes, credit ratings, interest rates and yield curves, prepayment speeds, default rates and other such inputs which are available from market sources.

Included within Level 1 of the fair value hierarchy are certain government bonds, treasury bills, long-term debt which are measured based on quoted prices in active markets.

Level 2 of the hierarchy contains certain government bonds, US government agencies, corporate securities, asset backed securities and mortgage-backed securities, derivatives, equities and shares in unit trusts. The fair value of these assets is based on the prices obtained from both investment managers and investment custodians as discussed above. The Group records the unadjusted price provided and validates the price through a number of methods including a comparison of the prices provided by the investment managers with the investment custodians and the valuation used by external parties to derive fair value. Quoted prices for US government agencies and corporate securities are based on a limited number of transactions for those securities and as such the Company considers these instruments to have similar characteristics to those instruments classified as Level 2. Also included within Level 2 are units held in traditional long funds and long and short special funds and over-the-counter derivatives.

Level 3 contains an investment in a limited partnership which has limited observable inputs on which to measure fair value. Fair value is determined to be net asset value for the limited partnership. The effect of changing one or more inputs used in the measurement of fair value of this instrument to another reasonably possible assumption would not be significant.

The Company's policy is to recognise transfers into and transfers out of fair value hierarchy levels at the end of the relevant reporting period during which the transfers are deemed to have occurred. During the year, there were no transfers made between Level 1, Level 2 or Level 3 of the fair value hierarchy.

The following table sets forth a reconciliation of opening and closing balances for financial instruments classified under Level 3 of the fair value hierarchy:

	2019	2018
	($ in thousands)	
Balance at January 1	$ 1,113	$ 2,191
Fair value losses through profit or loss	(324)	(1,078)
Purchases	-	-
Settlements	-	-
Balance at December 31	$ 789	$ 1,113

10. Deferred Acquisition Costs

	2019			2018		
	Gross	**Attributable to Reinsurers**	**Net**	**Gross**	**Attributable to Reinsurers**	**Net**
			($ in thousands)			
Balance deferred at January 1	26,872	(21,185)	5,687	18,207	(11,238)	6,969
Acquisition costs incurred in relation to reinsurance contracts written	228,351	(63,478)	164,873	80,783	(55,459)	25,324
Acquisition costs expense in the Statement of Income	(180,633)	60,204	(120,429)	(72,118)	47,041	(25,077)
Part VII transfer	23,339	-	23,339	-	-	-
Other adjustments	-	(1,215)	(1,215)	-	(1,529)	(1,529)
Balance deferred at December 31	97,929	(25,674)	72,255	26,872	(21,185)	5,687

The deferred amount of reinsurance contract acquisition costs attributable to reinsurers of $25,674 (2018: $21,185) is not eligible for offset against the gross Statement of Financial Position asset and is included separately within Trade and other payables.

The Part VII adjustment of $23,339 (2018: $0) is related to the Company's additional quota share participation in the insurance contracts covering EU risks transferred from HIC to HSA at January 1, 2019. Please refer to Notes 12 for further information.

The net amounts expected to be recovered before and after one year are estimated as follows:

	2019	2018
	($ in thousands)	
Within one year	$ 48,534	$ 4,708
After one year	23,721	979
Total	$ 72,255	$ 5,687

11. Funds withheld

The funds withheld of $117,255 (2018: nil) represents the cash and investments furnished by the Company to a related party cedant to collateralise business assumed and cannot be accessed by the cedant without the Company's consent. Total interest earned on the funds withheld in the year amounted to $1,058.

12. Reinsurance liabilities and associated recoverables

	2019	2018
	($ in thousands)	
Gross		
Claims reported and claim adjustment expenses	$ 854,236	$ 678,124
Claims incurred but not reported	1,526,875	1,011,312
Unearned premiums	447,617	271,056
Total Reinsurance liabilities, gross	$ 2,828,728	$ 1,960,492
Recoverable from reinsurers		
Claims reported and claim adjustment expenses	$ 388,368	$ 340,542
Claims incurred but not reported	955,643	534,629
Unearned premiums	123,349	104,442
Total Reinsurers' share of Reinsurance liabilities	$ 1,467,360	$ 979,613
Net		
Claims reported and claim adjustment expenses	$ 465,868	$ 337,582
Claims incurred but not reported	571,232	476,683
Unearned premiums	324,268	166,614
Total Reinsurance liabilities, net	$ 1,361,368	$ 980,879

The Total Reinsurance liabilities, net expected before and after one year are estimated as follows:

	2019	2018
	($ in thousands)	
Within one year	$ 778,581	$ 558,361
After one year	582,787	422,518
Total	$ 1,361,368	$ 980,879

(a) Process used to decide on assumptions

There are many risks associated with insurance contracts, and this means that there is a considerable amount of uncertainty in estimating the future settlement cost of claims. There is uncertainty in both the amounts and the timing of future claim payment cash flows.

Claims paid are claims transactions settled up to the reporting date including settlement expenses allocated to those transactions.

Unpaid claims reserves are made for known or anticipated liabilities which have not been settled up to the reporting date. Included within the provision is an allowance for the future costs of settling those claims.

The Company relies on actuarial analysis to estimate the settlement cost of future claims. There is close communication between the actuaries and other key stakeholders, such as the underwriters, claims and finance teams when setting and validating the assumptions. The unpaid claims reserve is estimated based on past experience and current expectations of future cost levels. Allowance is made for the current premium rating and inflationary environment.

The claim reserves are estimated on a best estimate basis, taking into account current market conditions and the nature of risks being underwritten.

Under certain reinsurance contracts, the Company may have the right to pursue third parties for payment of some or all costs (for example, subrogation). If it is certain a recovery or reimbursement will be made at the valuation date, specific estimates of these salvage and/or subrogation amounts are included as allowances in the measurement of the reinsurance liability for unpaid claims. This is then recognised in reinsurance receivables when the liability is settled.

Estimates of where claim liabilities will ultimately settle are adjusted each reporting period to reflect emerging claims experience. Changes in expected claims may result in a reduction or an increase in the ultimate claim costs and a release or an increase in reserves in the period in which the change occurs.

Booked reserves are held above the best estimate to help mitigate the uncertainty within the reserve estimates. As the best estimate matures and becomes more certain, the management margin is gradually released in line with the reserving policy.

(b) Claims development tables

The development of reinsurance liabilities provides a measure of the Company's ability to estimate the ultimate value of claims. The Company analyses actual claims development compared with previous estimates on an accident year basis.

The top of each table illustrates how estimates of ultimate claim costs for each accident year have changed at successive year ends and the bottom reconciles the cumulative claim costs to the amounts still recognised as liabilities.

For incurred and paid accident year claims denominated in foreign currency, the Company has revalued using the current period end exchange rate.

The following loss triangles are presented in thousands of U.S. dollars:

Gross Loss

Insurance claims and claims expenses reserves - GROSS											
Accident year	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Total**
Estimate of ultimate claims costs:											
at end of accident year	229,438	478,081	244,409	242,649	250,689	276,852	391,239	967,281	964,814	1,117,739	**5,163,191**
one year later	199,000	447,404	453,333	248,120	233,372	271,057	307,250	928,535	1,218,762		**4,306,833**
two years later	189,499	429,293	437,496	227,929	208,216	220,584	292,336	881,330			**2,886,683**
three years later	179,319	433,871	446,572	214,064	193,441	224,536	289,311				**1,981,112**
four years later	174,368	425,186	436,926	162,298	192,570	220,067					**1,611,414**
five years later	171,898	406,271	205,509	157,259	192,317						**1,133,255**
six years later	162,441	395,690	208,828	165,425							**932,385**
seven years later	158,150	395,495	217,357								**771,002**
eight years later	156,997	392,055									**549,052**
nine years later	159,161										**159,161**
Current estimate of cumulative claims	**159,161**	**392,055**	**217,357**	**165,425**	**192,317**	**220,067**	**289,311**	**881,330**	**1,218,762**	**1,117,739**	**4,853,523**
Cumulative payments to date	**(149,576)**	**(380,305)**	**(186,784)**	**(146,040)**	**(162,352)**	**(165,205)**	**(203,499)**	**(516,445)**	**(489,639)**	**(84,457)**	**(2,484,302)**
Total Gross reserves	**9,585**	**11,749**	**30,574**	**19,385**	**29,965**	**54,862**	**85,812**	**364,885**	**729,123**	**1,033,282**	**2,369,221**
Total Gross reserves on prior accident year											11,890
Total Gross reserves											**2,381,111**

Net Loss

Insurance claims and claims expenses reserves - NET											
Accident year	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Total**
Estimate of ultimate claims costs:											
at end of accident year	233,417	392,705	214,088	226,241	223,473	244,593	315,983	407,217	413,793	424,541	**3,096,051**
one year later	201,050	364,182	192,485	187,564	209,902	231,368	270,234	353,176	476,164		**2,486,125**
two years later	190,434	346,915	177,755	170,256	182,938	210,542	259,087	360,980			**1,898,907**
three years later	179,995	351,370	177,569	153,372	173,321	213,278	262,714				**1,511,617**
four years later	174,858	342,920	169,750	153,088	169,816	211,125					**1,221,556**
five years later	172,357	324,657	184,710	151,935	167,687						**1,001,347**
six years later	162,879	320,272	187,523	161,469							**832,144**
seven years later	158,511	320,348	196,945								**675,804**
eight years later	153,000	322,506									**475,506**
nine years later	155,164										**155,164**
Current estimate of cumulative claims	**155,164**	**322,506**	**196,945**	**161,469**	**167,687**	**211,125**	**262,714**	**360,980**	**476,164**	**424,541**	**2,739,294**
Cumulative payments to date	**(145,513)**	**(311,042)**	**(168,244)**	**(142,313)**	**(138,219)**	**(157,089)**	**(184,452)**	**(205,353)**	**(184,279)**	**(77,580)**	**(1,714,084)**
Total Net reserves	9,651	11,463	28,702	19,156	29,468	54,036	78,262	155,627	291,885	346,961	**1,025,210**
Total Net reserves on prior accident years											11,890
Total Net reserves											**1,037,100**

A reconciliation of reinsurance claims and liabilities is as follows:

	2019	2018
	($ in thousands)	
Gross loss and loss adjustment expenses reserves, beginning of year	$ 1,689,436	$ 1,313,242
Less: loss and loss adjustment expenses recoverable, beginning of year	(875,171)	(553,082)
Net loss and loss adjustment expenses reserves, beginning of year	814,265	760,160
Net loss and loss adjustment expenses incurred in respect of losses occurring in:		
Current year	424,541	408,106
Prior year	(776)	(68,483)
Total net loss and loss adjustment expenses incurred	423,765	339,623
Net loss and loss adjustment expenses paid in respect of losses occurring in:		
Current year	(77,580)	(61,764)
Prior year	(239,353)	(205,383)
Total net paid losses	(316,933)	(267,147)
Effect of foreign exchange and other adjustments	2,994	(18,371)
Effect of Part VII transfer	113,009	-
Net loss and loss adjustment expenses reserves, end of year	1,037,100	814,265
Plus: loss and loss adjustment expenses recoverable, end of year	1,344,011	875,171
Gross loss and loss adjustment expenses reserves, end of year	$ 2,381,111	$ 1,689,436

In response to the UK's decision to leave the European Union, the Hiscox Group made some necessary changes to its business to ensure continuity of cover and settlement of existing claims to all its customers with European risks, so that it can continue to service its policyholders and claimants across Europe post-Brexit. To make these changes the Group used a legal insurance business transfer process known as a Part VII transfer to novate insurance contracts covering EU risks and written by Hiscox Insurance Company Limited (HIC) prior to Brexit to Hiscox Societe Anonyme (HSA), the Group's EU carrier based in Luxembourg. The Company assumes a quota share of the underlying business transferred to HSA, and increased its quota share participation upon the transfer between HIC and HSA occurring on January 1, 2019. Therefore the aforementioned Part VII transfer resulted in an adjustment to reserves for risks assumed from HSA of $113,009.

Reserving Methodology

Reserving methods used include the Bornhuetter-Ferguson ("BF") method and the Expected Loss Ratio method for the most recent year(s). These methods place weight on initial loss expectations and are less volatile to early claims experience. For significant catastrophe exposures, the catastrophe component of the initial expected loss ratio is developed in line with a seasonally adjusted earning pattern rather than a standard triangle runoff pattern. As the years of account become more mature, more weighting is placed on the emerging experience and the projection will move over to a Chain Ladder projection (or blend of the BF and Chain Ladder methods). Over and above the exposure-based methods for assessment of Catastrophe IBNR required specific IBNER is held for known events that have occurred. These IBNER estimates are established through the large loss process which is a robust and well-established process run within the Group. Combining these two approaches the IBNR estimates are determined.

In general, reserves for the Company's more recent loss exposed events are subject to greater uncertainty and, therefore, greater potential variability, and are likely to experience material changes from one period to the next. This is due to the uncertainty as to the size of the industry losses from the event, uncertainty to which contracts have been exposed to the event, uncertainty due to complex legal and coverage issues that can arise out of large complex events, and uncertainty as to the magnitude of claims incurred by the Company's customers. As the Company's claims age, more information becomes available and the Company believes its estimates become more certain.

There have been no significant changes in methodologies and assumptions during the year ended December 31, 2019.

A reconciliation of the unearned premium reserves is as follows:

	2019			**2018**		
	Gross	**Reinsurance**	**Net**	**Gross**	**Reinsurance**	**Net**
	($ in thousands)					
Balance unearned at 1 January	271,056	(104,442)	166,614	299,721	(57,015)	242,706
Premiums written	1,154,388	(511,621)	642,767	874,507	(471,948)	402,559
Premiums earned in the Statements of Income	(1,042,643)	492,714	(549,929)	(903,172)	424,521	(478,651)
Part VII transfer	64,816	-	64,816	-	-	-
Balance unearned at 31 December	447,617	(123,349)	324,268	271,056	(104,442)	166,614

The amounts expected to be recovered before and after one year, based on historical experience, are included in the second table to this note.

The Part VII adjustment of $64,816 (2018: $0) is related to the Company's additional quota share participation in the insurance contracts covering EU risks transferred from HIC to HSA at January 1, 2019.

13. Trade and other payables

Trade and other payables are comprised of:

	2019	2018
	($ in thousands)	
Reinsurance balances payable	$ 267,504	$ 234,410
Reinsurers' share of deferred acquisition Costs	25,674	21,185
Deferred income	5,541	5,095
Derivative financial liability	340	775
Payable for investments purchased	29,690	-
Other payables including related party	9,317	53,502
Total	$ 338,066	$ 314,967

Reinsurance balances payable include amounts due for retroceded premiums netted off against amounts recoverable from retrocessionaires for their share of claims paid, as calculated in accordance with individual retrocession arrangements. The carrying amounts approximate fair value due to the short-term nature of the payables.

14. Related party transactions

The Company enters into reinsurance and retrocession agreements with affiliates. The financial statements include the following amounts which are attributable to reinsurance assumed and retrocession related party transactions:

	2019	2018
	($ in thousands)	
Gross premiums written	$ 717,328	$ 509,359
Gross premiums earned	659,154	549,760
Gross premiums ceded	377,366	337,725
Earned premiums ceded	352,764	299,169
Loss and loss adjustment expenses incurred, net	(21,884)	57,446
Acquisition costs, net	99,193	17,395
Loans and receivables including reinsurance receivables	400,323	170,249
Funds withheld	117,255	-
Deferred acquisition costs	74,707	8,994
Loss and loss adjustment expense recoverable	916,445	619,599
Prepaid reinsurance premiums	94,627	70,023
Reinsurance balances payable	337,133	180,624
Unearned premium reserves	328,602	183,372
Loss and loss adjustment expenses reserves	1,221,799	968,210
Reinsurers' share of Deferred acquisition costs	20,629	16,758

During 2019, the Company maintained assets in trust accounts to collateralize obligations under various reinsurance agreements. Cash and marketable securities with an approximate market value of $476.3 million (2018: $611.6 million) were held in trust in respect of internal QS arrangements. Additionally, cash and investments have been provided as funds withheld for an internal quota share as discussed in Note 11.

The losses recoverable from related parties is primarily due from an ILS fund that is managed by an affiliate.

The Company entered into various service agreements with Hiscox Underwriting Group Services Limited ("HUGS") and Hiscox Services Ltd. ("HSL"). HUGS and HSL are wholly owned subsidiaries of Hiscox Ltd. The service agreements with HUGS cover group wide investment management services, claims and legal services, human resources, IT, actuarial, accounting and other general corporate services, modeling services and outwards reinsurance administration services. The service agreements with HSL cover Bermuda general expenses as well as support services such as underwriting, modeling, outwards reinsurance administration, human resources, operations, claims and accounting services.

Transactions and balances with HUGS and HSL have been recorded in the financial statements as follows:

		2019		2018
		($ in thousands)		
HUGS:				
Trade and other payables	$	874	$	43,748
General and administrative expenses	$	11,480	$	12,386
HSL:				
Loans and receivables including reinsurance receivables	$	9,213	$	54,778
General and administrative expenses	$	18,906	$	18,396

Non-reinsurance related party balances with other Hiscox affiliates have been recorded in the financial statements as follows:

		2019		2018
		($ in thousands)		
Loans and receivables including reinsurance receivables	$	16,230	$	30,698
Trade and other payables	$	6,089	$	7,555
Dividends payable	$	-	$	80,000

The expense recognized during the year for the fair value of equity awards made to employees of the Company in the form of share options in the parent company, Hiscox Ltd, is $0.3m (2018: $0.1m).

15. Commitments and security arrangements

The letter of credit facilities held by the Company as at December 31, 2019 and 2018 are as follows:

	2019	2018
	($ in thousands)	
Citibank	$ 125,000	$ 150,000
Commerzbank	225,000	225,000
National Australia Bank	120,000	225,000
	$ 470,000	$ 600,000

Collectively, the secured facility agreements allow the Company to request the issuance of up to $470.0m (2018: $600.0m) in letters of credit. At December 31, 2019, $150.8m (2018: $130.5m) in letters of credit were issued under these facilities, collateralized by cash, U.S. government and corporate securities with a fair value of $172.9m (2018: $152.8m).

During 2019, the Company maintained assets in trust accounts to collateralize obligations under various reinsurance agreements. At December 31, 2019, $651.6m (2018: $622.3m) of marketable securities and $6.9m (2018: $10.7m) of cash were restricted as collateral within various Letter of Credit and trust accounts.

Additionally, as at December 31, 2019, $0.2m (2018: $9.5m) of cash and $35.7m ($2018: $15.3m) of marketable securities were maintained in a trust account for credit enhancement purposes.

Hiscox Plc, a company related by common control, has a letter of credit and revolving credit facility with Lloyds Banking Group, as agent for a syndicate of banks, of $800.0m (2018: $800.0m) which may be drawn in cash (under a revolving credit facility), letter of credit or a combination thereof, providing that the cash portion does not exceed $800.0m. In addition, the terms also provide that upon request the facility may be drawn in a currency other than US Dollars. At December 31, 2019 $50.0m (2018: $50.0m) was utilised by way of letter of credit and no cash drawings were outstanding (2018: nil). The borrower for this letter of credit is initially responsible for repaying the banks for any amounts drawn. However, the facility is guaranteed by Hiscox Ltd and other affiliated companies, including the Company. This guarantee entitles the banks to pursue any of these entities for any sums due. In addition, the banks have share pledges over the shares of Hiscox Insurance Company Limited, an affiliate company, and Hiscox Insurance Company (Bermuda) Limited which can be called in the circumstance of a payment default.

16. Shareholder's equity

The items "common shares" and "contributed surplus" represent amounts paid by the Parent and retained earnings consist of accumulated reinvested net income generated by the Company. Any adjustment from a retrospective change in accounting policies affecting prior periods are recognised in the opening value of retained earnings in the Statement of Financial Position. For distribution restrictions, please refer to Note 17.

During October and December 2019, dividends of $38.0m and $30.0m, respectively, were declared and paid to Hiscox Ltd.

17. Statutory requirements

As a Class 4 insurer, the Company must at all times maintain a solvency margin and an enhanced capital requirement in accordance with the provisions of The Insurance Act 1978. Each year the Company is required to file with the Bermuda Monetary Authority (the "Authority") a capital and solvency return within four months of its relevant financial year end (unless specifically extended).

The prescribed form of capital and solvency return comprises the insurer's Bermuda Solvency Capital Requirement ("BSCR") model, a schedule of fixed income investments by rating category, a schedule of net loss and loss expense provision by line of business, a schedule of premiums written by line of business, a schedule of risk management and a schedule of fixed income securities by security type. The BSCR includes a standardized model used to measure the risk associated with an insurer's assets, liabilities and premiums, and a formula to take account of catastrophe risk exposure. The Authority has provided for the use of pre-approved internally developed company models in lieu of the standardized BSCR. The Authority requires all Class 4 insurers to maintain their capital at a target level which is 120% of the amount calculated in accordance with the BSCR or the company's approved internal model (the Enhanced Capital Requirement or "ECR"). In addition, the Company is required to maintain a minimum solvency margin. Both requirements have been met.

Statutory capital and surplus at December 31, 2019, as determined using statutory accounting principles, was $598.4m (2018: $613.8m). At December 31, 2019 the Company's minimum capital requirement was $321.5m (2018: $327.9m).

The Insurance Act 1978 also requires an insurer engaged in general business to maintain the value of its relevant assets at not less than 75% of the amount of its relevant liabilities. Relevant assets include cash and time deposits, quoted investments, unquoted bonds and debentures, first liens on real estate, investment income due and accrued, accounts and premiums receivable, reinsurance balances receivable and funds held by ceding reinsurers. There are certain categories of assets which, unless specifically permitted by the Authority, do not automatically qualify as relevant assets, such as unquoted equity securities, investments in and advances to affiliates and real estate and collateral loans. The relevant liabilities are total general business insurance reserves and total other liabilities less deferred income tax, sundry liabilities (by interpretation, those not specifically defined) and, letters of credit, guarantees and other instruments. The minimum liquidity ratio has been met.

The Company is prohibited from declaring or paying a dividend if its Class 4 statutory capital and surplus is less than its ECR, or if it is in breach of its solvency margin or minimum liquidity ratio, or if the declaration or payment of such dividend would cause such breach. Further, the Company, as a Class 4 insurer, is prohibited from declaring or paying in any year dividends of more than 25% of its total statutory capital and surplus as shown on its previous year's statutory Statement of Financial Position unless it files (at least seven days before payment of such dividends) with the Authority an affidavit stating that it will continue to meet its solvency margin and minimum liquidity ratio. As of December 31, 2019, the Company could pay dividends of $153.4m (2018: $80.0m) without providing an affidavit to the BMA.

The Company must obtain the Authority's prior approval for a reduction by 15% or more of the total statutory capital as set forth in its previous year's statutory financial statements. These restrictions on declaring or paying dividends and distributions under the Insurance Act are in addition to those under the Companies Act 1981, which apply to all Bermuda companies.

18. Subsequent events

Subsequent events have been evaluated up to and including May 25, 2020, being the date that these financial statements were available to be issued.

During the finalisation of these financial statements COVID-19 has evolved into an unprecedented public health emergency around the world, causing disruption to business and economic activity. The Company considers this outbreak to be a non-adjusting post Statement of Financial Position event.

The unprecedented social distancing measures have resulted in our business activating business continuity plans (BCP) and most colleagues are now working remotely. The investment in technology over recent years has meant the business operates mostly in a paperless environment.

There remains significant uncertainty regarding the financial impact to the Company arising from COVID-19. Plans for the re-opening of economies, and lifting of restrictions on mass gatherings and travel in many countries remains unclear. Management currently estimates net losses for the Company of approximately $45m to $52m. There are additional reinsured exposures for which cedants may be subject to legal challenge which could give rise to significantly different potential outcomes to those currently estimated. The potential impact to the 2020 financial statements, may include the estimates, judgments, and assumptions as disclosed in Note 2.4 of these financial statements.