

Financial statements for the  
year ended 31 December 2021

# THE LANCASHIRE WAY

Finding the right solutions





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## **INDEPENDENT AUDITOR'S REPORT**

**To the Shareholder and Board of Directors of Lancashire Insurance Company Limited**

### **Report on the audit of the financial statements**

#### **Opinion**

We have audited the financial statements of Lancashire Insurance Company Limited (the "Company"), which comprise the balance sheet as at 31 December 2021, the statements of comprehensive (loss) income, changes in shareholder's equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the balance sheet of the Company as at 31 December 2021, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

#### **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 are independent of the Company in accordance with International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Bermuda and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **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 IFRS, 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 skepticism 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.

*KPMG Audit Limited*

Chartered Professional Accountants  
Hamilton, Bermuda  
February 10, 2022

## STATEMENT OF COMPREHENSIVE (LOSS) INCOME

For the year ended 31 December 2021

	Notes	2021 \$m	2020 \$m
Gross premiums written	2	606.0	337.3
Outwards reinsurance premiums	2	(150.7)	(85.7)
<b>Net premiums written</b>		<b>455.3</b>	251.6
Change in unearned premiums	2	(66.5)	(13.2)
Change in unearned premiums on premiums ceded	2	(3.1)	(1.8)
<b>Net premiums earned</b>		<b>385.7</b>	236.6
Net investment income	3	18.0	20.9
Net other investment income	3	4.9	6.3
Net realised gains (losses) and impairments	3	5.0	11.8
Net other income	17	18.0	3.7
Net foreign exchange gains		2.3	1.1
<b>Total net revenue</b>		<b>433.9</b>	280.4
Insurance losses and loss adjustment expenses	2, 11	426.2	122.4
Insurance losses and loss adjustment expenses recoverable	2, 11	(127.3)	11.2
<b>Net insurance losses</b>		<b>298.9</b>	133.6
Insurance acquisition expenses	2, 4	124.5	89.5
Insurance acquisition expenses ceded	2, 4	(9.5)	(6.5)
Other operating expenses	5, 6, 15, 17	24.7	26.1
Equity based compensation	6, 17	2.4	2.3
<b>Total expenses</b>		<b>441.0</b>	245.0
<b>Results of operating activities</b>		<b>(7.1)</b>	35.4
Financing costs		2.5	2.4
<b>(Loss) profit for the year attributable to equity shareholder</b>		<b>(9.6)</b>	33.0
<b>Other comprehensive (loss) income to be reclassified to profit or loss in subsequent periods</b>			
Net change in unrealised gains/losses on investments	3, 9	(23.4)	16.0
<b>Other comprehensive (loss) income</b>	9	<b>(23.4)</b>	16.0
<b>Total comprehensive (loss) income for the year</b>		<b>(33.0)</b>	49.0

## BALANCE SHEET

As at 31 December 2021

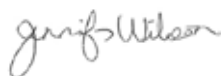
	Notes	2021 \$m	2020 \$m
<b>Assets</b>			
Cash and cash equivalents	8, 13	290.7	203.4
Accrued interest receivable		5.9	6.2
Investments	9, 10, 13	1,674.2	1,474.7
Inwards premiums receivable from insureds and cedants	12	182.8	120.2
Reinsurance assets			
– Unearned premiums on premiums ceded		18.1	21.2
– Reinsurance recoveries	11	197.4	129.0
Other insurance receivables		8.4	4.1
Other receivables	12, 17	83.1	51.0
Property, plant and equipment		0.4	0.1
Right-of-use assets	15	1.8	2.8
Deferred acquisition costs		61.4	43.7
<b>Total assets</b>		<b>2,524.2</b>	<b>2,056.4</b>
<b>Liabilities</b>			
Insurance contracts			
– Losses and loss adjustment expenses	11	753.4	483.4
– Unearned premiums		262.2	195.7
– Other payables		4.3	2.2
Amounts payable to reinsurers		57.9	40.5
Deferred acquisition costs ceded		3.4	4.2
Other payables	17	9.9	41.7
Lease liabilities	15	2.0	3.0
<b>Total liabilities</b>		<b>1,093.1</b>	<b>770.7</b>
<b>Shareholder's equity</b>			
Share capital	14	1.0	1.0
Contributed surplus		1,303.9	1,125.5
Accumulated other comprehensive income	9	2.1	25.5
Retained earnings		124.1	133.7
<b>Total shareholder's equity attributable to equity shareholder</b>		<b>1,431.1</b>	<b>1,285.7</b>
<b>Total liabilities and shareholder's equity</b>		<b>2,524.2</b>	<b>2,056.4</b>

The financial statements were approved by the Board of Directors on 10 February 2022 and signed on its behalf by:



Hayley Johnston

Director/Chief Executive Officer



Jennifer Wilson

Director/Chief Financial Officer

## STATEMENT OF CHANGES IN SHAREHOLDER'S EQUITY

For the year ended 31 December 2021

	Notes	Share capital \$m	Contributed surplus \$m	Accumulated other comprehensive income \$m	Retained earnings \$m	Total shareholder's equity \$m
<b>Balance as at 31 December 2019</b>		1.0	840.5	9.5	100.7	951.7
Total comprehensive income for the year		—	—	16.0	33.0	49.0
Shareholder contribution		—	285.0	—	—	285.0
<b>Balance as at 31 December 2020</b>		1.0	1,125.5	25.5	133.7	1,285.7
Total comprehensive loss for the year		—	—	(23.4)	(9.6)	(33.0)
Shareholder contribution	17	—	178.4	—	—	178.4
<b>Balance as at 31 December 2021</b>		1.0	1,303.9	2.1	124.1	1,431.1

## STATEMENT OF CASH FLOWS

For the year ended 31 December 2021

	Notes	2021 \$m	2020 \$m
<b>Cash flows from operating activities</b>			
(Loss) profit		(9.6)	33.0
<b>Adjustments for:</b>			
Depreciation	5, 15	1.2	1.1
Interest expense on lease liabilities	15	0.2	0.2
Interest income	3	(27.2)	(28.0)
Net amortisation of fixed maturity securities		5.6	4.2
Foreign exchange gains		(2.9)	(5.4)
Net other investment income		(5.8)	(7.2)
Net realised (gains) losses and impairments	3	(5.0)	(11.8)
<b>Changes in operational assets and liabilities</b>			
– Insurance and reinsurance contracts		225.4	60.6
– Other assets and liabilities		(76.4)	(23.4)
<b>Net cash flows from operating activities</b>		<b>105.5</b>	<b>23.3</b>
<b>Cash flows used in investing activities</b>			
Interest received		35.2	31.0
Purchase of property, plant and equipment		(0.5)	—
Purchase of investments		(1,125.9)	(920.2)
Proceeds on sale of investments		898.1	644.1
<b>Net cash flows used in investing activities</b>		<b>(193.1)</b>	<b>(245.1)</b>
<b>Cash flows from financing activities</b>			
Lease liabilities paid	15	(1.2)	(1.1)
Dividends paid		—	(0.5)
Loan to parent		—	(22.8)
Shareholder contribution	17	178.4	285.0
<b>Net cash flows from financing activities</b>		<b>177.2</b>	<b>260.6</b>
<b>Net increase in cash and cash equivalents</b>		<b>89.6</b>	<b>38.8</b>
Cash and cash equivalents at beginning of year		203.4	162.7
Effect of exchange rate fluctuations on cash and cash equivalents		(2.3)	1.9
<b>Cash and cash equivalents at end of year</b>	8	<b>290.7</b>	<b>203.4</b>

## ACCOUNTING POLICIES

For the year ended 31 December 2021

### SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basis of preparation, use of judgements and estimates and significant accounting policies adopted in the preparation of these financial statements are set out below.

#### BASIS OF PREPARATION

##### GOING CONCERN BASIS OF ACCOUNTING

The financial statements are prepared on a going concern basis in accordance with IFRS.

In assessing the Company's going concern position as at 31 December 2021, the Directors have considered a number of factors. These include the current balance sheet and liquidity position, the level and composition of the Company's capital and solvency ratios, the current performance against the Group's strategic and financial business plan, the current market environment including consideration of the ongoing COVID-19 pandemic and climate change.

The Company's financial forecasts reflect the outcomes that the Directors consider most likely, based on the information available at the date of signing these financial statements. To assess the Company's going concern, the financial stability of the Company was modelled for a period of at least 12 months and a number of sensitivity, stress and scenario tests were applied. This included, among other analysis, a best estimate forecast as well as various scenarios. This incorporated different magnitudes of reserve releases and, attritional, large and catastrophe loss events plus optimistic and pessimistic investment return scenarios. To further stress the financial stability of the Company, additional stress testing was performed. This included modelling the breakeven capital requirements of our regulators and rating agencies, the impact of potential management actions to reduce the Company's exposure to climate change-related risks, an operational risk stress of the main input assumption to the base case, the occurrence of a number of high severity loss events impacting the Company in 2022 alongside an investment shock and finally a reverse stress test scenario designed to render the business model unviable. The testing identified that even under the more severe but plausible stress scenarios, the Company had more than adequate liquidity and solvency headroom.

Based on the going concern assessment performed as at 31 December 2021, the Directors consider there to be no material uncertainties that may cast significant doubt over the Company's ability to continue to operate as a going concern. The Directors have formed a judgement that there is a reasonable expectation that the Company has adequate resources to continue in operational existence in the foreseeable future, a period of at least 12 months from the date of signing these financial statements.

##### USE OF JUDGEMENTS AND ESTIMATES

The preparation of the Company's financial statements requires management to make judgements and estimates that affect the reported amounts of revenue, expenses, assets, liabilities and the accompanying financial statement disclosures. In the course of preparing the financial statements no key judgements have been made in the process of applying the Company's accounting policies that do not include a related element of estimation uncertainty.

The key assumptions and other sources of estimation uncertainty at 31 December 2021, that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities in the next financial year, are described below. Assumptions and estimates are based on parameters available when the financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change or circumstances may arise that are beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

The most significant estimate made by management is in relation to losses and loss adjustment expenses, both gross and net of outwards reinsurance recoverable. This is discussed on page 9, within the risk disclosures section from pages 17 and 18 and within note 11.

Less significant estimates are made in determining the fair value of certain financial instruments and management judgement is applied in determining impairment charges. The estimation of the fair value, specifically "Level (iii)" investments, is discussed on page 10 and in note 9.

A portion of gross premiums written is based on estimates of the ultimate premiums expected to be received (see premium and acquisition costs accounting policy on page 9). Judgement is involved in determining the ultimate estimates in order to establish the appropriate premium value and, ultimately, the cash to be received.

##### OTHER BASIS OF PREPARATION

Where IFRS 4, Insurance Contracts is silent, as it is in respect of certain aspects relating to the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, the Company's management determines appropriate measurement bases, to provide the most useful information to users of the financial statements, using their judgement and considering U.S. GAAP.

The balance sheet of the Company is presented in order of decreasing liquidity. All amounts, excluding share data or where otherwise stated, are in millions of U.S. dollars.

##### CHANGES IN ACCOUNTING STANDARDS

There were no new standards that became effective in the year ended 31 December 2021 that have had a material impact on the Company.

##### FUTURE ACCOUNTING CHANGES

###### IFRS 17, Insurance Contracts

IFRS 17, issued in May 2017, specifies the financial reporting for insurance contracts and supersedes IFRS 4, Insurance Contracts. IFRS 17 will be effective for accounting periods beginning on or after 1 January 2023.

The Company is currently in the build phase of its IFRS 17 project with parallel testing of systems and processes due to commence in 2022. The standard includes a number of significant changes regarding the measurement and disclosure of insurance contracts both in terms of liability measurement and profit recognition.



## ACCOUNTING POLICIES CONTINUED

The IFRS 17 general measurement model requires insurance contract liabilities to be measured using:

- probability-weighted estimates of future cash flows;
- discounting;
- a risk adjustment for non-financial risk; and
- a contractual service margin representing the unearned profit that will be recognised over the coverage period.

IFRS 17 is a principals-based accounting standard. There are a number of accounting policy choices that are allowed under the standard and this will require the application of judgement and an increased use of estimation techniques. The Company has performed an assessment and currently anticipates that it will be eligible to apply the simplified model (premium allocation approach) to its portfolios and groups of contracts. This will continue to be assessed through 2022.

IFRS 17 will result in a number of presentation differences compared to the existing IFRS 4 financial statements. The insurance service result will comprise insurance revenue, insurance service expense and insurance finance income or expense. Reinsurance contracts held are required to be presented separately from insurance contracts issued. Reinstatement premiums will be considered contingent on claims and therefore recognised against insurance service expense while commissions paid to cedants will be recognised as a deduction from insurance revenue. Non-distinct investment components, which are defined as amounts that are repayable in all circumstances, are required to be excluded from insurance revenue and expenses.

Under IFRS 17, Insurance contracts that are subject to similar risks and that are managed together are classified into a portfolio of insurance contracts. Each portfolio of insurance contracts is then divided into a minimum of three groups.

- A group of contracts that are onerous at initial recognition;
- A group of contracts that at initial recognition have no significant possibility of becoming onerous; and
- A group of the remaining contracts in the portfolio.

A group of contracts that are considered onerous on initial recognition will result in a loss being recognised immediately in the statement of comprehensive (loss) income. In the balance sheet, we would be required to recognise a loss component in the liability for remaining coverage. The Company is currently reviewing its portfolios and groups of contracts to determine if there are any onerous contracts that may result in a transition adjustment on adoption of IFRS 17.

IFRS 17 requires that all future cash flows related to the fulfilment of insurance contracts be captured within portfolios and applied to groups of insurance contracts. The Company anticipates recognising a liability for the future expenses expected to be incurred in the servicing of insurance contracts. This will form part of the transition adjustment recognised by the Company on adoption of IFRS 17.

The Company currently anticipates that it will apply the fully retrospective transition approach when adopting IFRS 17.

In December 2021, the IASB issued Initial application of IFRS 17 and IFRS 9 - Comparative Information (Amendment to IFRS 17). The amendment was made to address possible accounting mismatches between financial assets and insurance contract liabilities in the comparative information presented on initial application of IFRS 9 and IFRS 17.

The Company will continue to assess the impact that IFRS 17 will have on its results and its presentation and disclosure requirements.

### IFRS 9, Financial Instruments: Classification and Measurement

IFRS 9 is effective for annual periods beginning on or after 1 January 2018. The amendments to IFRS 4, Insurance Contracts, issued in 2016, provide a temporary exemption from applying IFRS 9. The Company continues to qualify for, and has elected to apply, the temporary exemption available to companies whose predominant activity is to issue insurance contracts. The exemption lasts until the implementation date of IFRS 17 and addresses the accounting consequences of applying IFRS 9 to insurers prior to the adoption of IFRS 17. IFRS 9 introduces new classification and measurement requirements for financial instruments, an expected credit loss impairment model that replaces the IAS 39 incurred loss model and new hedge accounting requirements. Applying the new requirements of IFRS 9, the Company currently anticipates that all investments held by the Company will be classified as at FVTPL mandatory, because they are managed on a fair value basis. As a result, all investments currently disclosed in note 10 as AFS will be reclassified as at FVTPL mandatory with changes in unrealised gains (losses) currently recorded within other comprehensive (loss) income to be reclassified and recorded within net investment income in profit or loss. The reclassification from AFS to FVTPL mandatory will not result in a change in the carrying value of the investments disclosed in note 9 of the financial statements. The change in classification from AFS to FVTPL mandatory will result in balances within accumulated other comprehensive income being reclassified to retained earnings on the date of transition.

## FOREIGN CURRENCY

### FUNCTIONAL CURRENCY

Items included in the financial statements are measured using the currency of the primary economic environment in which operations are conducted (the 'functional currency'). The financial statements are presented in U.S. dollars (the "presentation currency").

### TRANSACTIONS AND BALANCES

Foreign currency transactions are recorded in the functional currency using the exchange rates prevailing at the dates of the transactions, or at the average rate for the period when this is a reasonable approximation. Monetary assets and liabilities denominated in foreign currencies are revalued at period end exchange rates. The resulting exchange differences on revaluation are recorded in the consolidated statement of comprehensive (loss) income within net foreign exchange gains. Non-monetary assets and liabilities denominated in a foreign currency are carried at historic rates. Non-monetary assets and liabilities carried at estimated fair value and denominated in a foreign currency are translated at the exchange rate at the date the estimated fair value was determined.

## ACCOUNTING POLICIES CONTINUED

### INSURANCE CONTRACTS

#### CLASSIFICATION

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Contracts that do not transfer significant insurance risk are accounted for as investment contracts. Insurance risk is transferred when an insurer agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder.

#### PREMIUMS AND ACQUISITION COSTS

Premiums are first recognised as written at the later of a contract's binding or inception date. The Company writes both excess of loss and pro-rata (proportional) contracts. For the majority of excess of loss contracts, premiums written are recorded based on the minimum and deposit or flat premium, as defined in the contract. Subsequent adjustments to the minimum and deposit premium are recognised in the period in which they are determined. For pro-rata contracts and excess of loss contracts where no deposit is specified in the contract, premiums written are recognised based on estimates of ultimate premiums provided by the insureds or ceding companies. Initial estimates of premiums written are recognised in the period in which the contract incepts, or the period in which the contract is bound if later. Subsequent adjustments, based on reports of actual premium by the insureds or ceding companies, or revisions in estimates, are recorded in the period in which they are determined.

Premiums written are earned evenly over the term of the underlying risk period of the insurance contract, except where the period of risk differs significantly from the contract period. In these circumstances, premiums are recognised over the period of risk in proportion to the amount of insurance protection provided. The portion of the premium related to the unexpired portion of the risk period is reflected in unearned premiums.

Where contract terms require the reinstatement of coverage after an insured's or ceding company's loss, the estimated mandatory reinstatement premiums are recorded as premiums written when a specific loss event occurs. Reinstatement premiums are not recorded for losses included within the provision for IBNR that do not relate to a specific loss event.

Inwards premiums receivable from insureds and cedants are recorded net of commissions, brokerage, premium taxes and other levies on premiums, unless the contract specifies otherwise. These balances are regularly reviewed for impairment, with any impairment loss recognised as an expense in the period in which it is determined.

Acquisition costs represent commissions, brokerage, profit commissions and other variable costs that relate directly to the successful securing of new contracts and the renewing of existing contracts. They are generally deferred over the period in which the related premiums are earned to the extent they are recoverable out of expected future revenue margins. All other acquisition costs are recognised as an expense when incurred.

#### OUTWARDS REINSURANCE

Outwards reinsurance premiums comprise the cost of reinsurance contracts held entered into. Outwards reinsurance premiums are accounted for in the period in which the contract incepts, or the period in which the contract is bound if later. The provision for the reinsurers' share of unearned premiums represents that part of reinsurance premiums ceded which are estimated to be earned in future financial periods. Unearned reinsurance commissions are recognised as a liability using the same principles.

Any amounts recoverable from reinsurers are estimated using the same methodology as for the underlying losses. The Company monitors the creditworthiness of its reinsurers on an ongoing basis and assesses any reinsurance assets for impairment, with any impairment loss recognised as an expense in the period in which it is determined.

#### LOSSES

Losses comprise losses and loss adjustment expenses paid in the period and changes in the provision for outstanding losses and ACR, including the provision for IBNR and related expenses. Losses and loss adjustment expenses are charged to profit or loss as they are incurred.

Losses and loss adjustment expenses represent the estimated ultimate cost of settling all insurance claims arising from events which have occurred up to the balance sheet date, including a provision for IBNR. The Company does not discount its liabilities for unpaid losses. Outstanding losses are initially set on the basis of reported losses received from third parties. ACR are determined where management's best estimate of the reported loss is greater than that reported and are allocated with IBNR in the Company's financial reporting. Estimated IBNR reserves may also consist of a provision for additional development in excess of losses reported by insureds or ceding companies, as well as a provision for losses which have occurred but which have not yet been reported by insureds or ceding companies. IBNR reserves are estimated by management using various actuarial methods as well as a combination of the Company's own loss experience, historical insurance industry loss experience, underwriters' experience, estimates of pricing adequacy trends and management's professional judgement.

A portion of the Company's business is in classes with high attachment points of coverage, including property catastrophe excess of loss. Reserving for losses in such programmes is inherently complicated in that losses in excess of the attachment level of the Company's policies are characterised by high severity and low frequency and other factors which could vary significantly as losses are settled. This limits the volume of industry loss experience available from which to reliably predict ultimate losses following a loss event.

The estimation of the ultimate loss and loss adjustment expense liability is a complex process which incorporates a significant amount of judgement. It is reasonably possible that uncertainties inherent in the reserving process, delays in insureds or ceding companies reporting losses to the Company, together with the potential for unforeseen adverse developments, could lead to a material change in estimated losses and loss adjustment expenses.

#### LIABILITY ADEQUACY TESTS

At each balance sheet date, the Company performs a liability adequacy test to determine if there is an overall excess of expected claims over unearned premiums for the period of unexpired risk by using current best estimates of future cash outflows generated by its insurance contracts, plus any investment income thereon. If, as a result of these tests, the carrying amount of the Company's insurance liabilities is found to be inadequate, the deficiency is charged to income for the period, initially by writing off deferred acquisition costs and subsequently by establishing a provision.

## ACCOUNTING POLICIES CONTINUED

### FINANCIAL INSTRUMENTS

#### CASH AND CASH EQUIVALENTS

Cash and cash equivalents are carried in the balance sheet at amortised cost and include cash in hand, deposits held on call with banks and other short-term highly liquid investments with a maturity of three months or less at the date of purchase. Carrying amounts approximate fair value due to the short-term nature and high liquidity of the instruments.

Interest income earned on cash and cash equivalents is recognised on the effective interest rate method. The carrying value of accrued interest income approximates estimated fair value due to its short-term nature and high liquidity.

#### INVESTMENTS

The Company's fixed maturity include quoted and unquoted investments that are classified as either AFS or as at FVTPL and are carried at fair value. The classification of the Company's financial assets is determined at the time of initial purchase and depends on the nature of the investment. A financial asset is classified at FVTPL if it is managed and evaluated on a fair value basis or 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. Equity securities classified as AFS are those that are neither classified as held for trading nor designated at FVTPL. Fixed maturity securities classified as AFS are those that are intended to be held for an indefinite period, the composition, duration and allocation of these investments are reviewed by management on a regular basis in order to respond to needs for liquidity, changes in interest rates and other market conditions.

The Company has elected to designate certain fixed maturity securities, index linked securities, exchange traded funds and its private investment funds at FVTPL upon initial recognition. This category includes instruments in which the cash flows are linked to the performance of an underlying pool of securities. Presentation of these securities in the FVTPL category is consistent with how management monitors and evaluates the performance of these securities.

The Company's hedge funds are unquoted investments classified at FVTPL and are carried at fair value. Fair values are determined using a combination of the most recent NAVs provided by each fund's independent administrator and the estimated performance provided by each hedge fund manager.

Regular way purchases and sales of investments are recognised at fair value including, in the case of investments not carried at FVTPL, transaction costs attributable to the acquisition of that investment on the trade date and are subsequently carried at fair value. The fair values of quoted and unquoted investments are determined based on bid prices from recognised exchanges, broker-dealers, recognised indices or pricing vendors. Unrealised gains and losses from changes in the fair value of AFS investments are included in accumulated other comprehensive income in shareholder's equity. Changes in the fair value of investments classified at FVTPL are recognised in the statement of comprehensive (loss) income within net other investment income.

Investments are derecognised when the Company has transferred substantially all of the risks and rewards of ownership. On derecognition of an AFS investment, previously recorded unrealised gains and losses are recycled from accumulated other comprehensive income in shareholder's equity and included in the statement of comprehensive (loss) income as a realised gain or loss within net realised gains (losses) and impairments.

Amortisation and accretion of premiums and discounts on AFS fixed maturity securities are calculated using the effective interest rate method and are recognised in current period net investment income. Interest income is recognised on the effective interest rate method. The carrying value of accrued interest income approximates fair value due to its short-term nature and high liquidity. Dividends on equity securities are recorded as income on the date the dividends become payable to the holders of record.

The Company regularly reviews the carrying value of its AFS investments for evidence of impairment. Such evidence would include a prolonged decline in the fair value below cost or amortised cost, where other factors, such as expected cash flows, do not support a recovery in value. If an impairment is deemed appropriate, the difference between cost or amortised cost and fair value is removed from accumulated other comprehensive income in shareholder's equity and charged to current period profit or loss. Impairment losses on fixed maturity securities may be subsequently reversed through profit or loss while impairment losses on equity securities are not subsequently reversed through profit or loss.

#### DERIVATIVE FINANCIAL INSTRUMENTS

Derivatives are classified as financial assets or liabilities at FVTPL. They are initially recognised at fair value on the date a contract is entered into, the trade date, and are subsequently carried at fair value. Derivative instruments with a positive estimated fair value are recorded as derivative financial assets and those with a negative fair value are recorded as derivative financial liabilities.

Derivative financial instruments include exchange-traded future and option contracts, forward foreign currency contracts, interest rate swaps, credit default swaps and interest rate swaptions. They derive their value from the underlying instrument and are subject to the same risks as that underlying instrument, including liquidity, credit and market risk. Fair values are based on exchange or broker-dealer quotations, where available, or discounted cash flow models, which incorporate the pricing of the underlying instrument, yield curves and other factors. Changes in the fair value of derivative instruments are recognised in the statement of comprehensive (loss) income within net other investment income. The Company does not currently apply hedge accounting to any derivative contracts. For discounted cash flow techniques, estimated future cash flows are based on management's best estimates and the discount rate used is an appropriate market rate.

Derivative financial assets and liabilities are offset and the net amount is reported in the balance sheet only to the extent there is a legally enforceable right of offset and there is an intention to settle on a net basis, or to realise the assets and liabilities simultaneously. Derivative financial assets and liabilities are derecognised when the Company has transferred substantially all of the risks and rewards of ownership or the liability is discharged, cancelled or expired.

## ACCOUNTING POLICIES CONTINUED

### PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is carried at historical cost, less accumulated depreciation and any impairment in value. Depreciation is calculated to write off the cost over the estimated useful economic life on a straight-line basis as follows:

- IT equipment & office furniture and equipment 33% per annum
- Leasehold improvements 20% per annum

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each balance sheet date. An item of property, plant or equipment is derecognised on disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Gains and losses on the disposal of property, plant and equipment are determined by comparing proceeds with the carrying amount of the asset, and are included in the statement of comprehensive (loss) income. Costs for repairs and maintenance are charged to profit or loss as incurred.

### LEASES

The Company assesses whether a contract is or contains a lease, at the inception of a contract, for all contracts that have been entered into or modified on or after 1 January 2019. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Company recognises a right-of-use asset and a lease liability at the lease commencement date. The Company is not a lessor to any lease contracts.

The lease liability is initially measured at the present value of the future lease payments at the lease commencement date. Lease payments are discounted using the rate implicit in the lease, if readily determinable, or the Company's incremental borrowing rate. Lease payments included in the measurement of the lease liability comprise:

- Fixed lease payments;
- Variable lease payments that depend on an index or rate, initially measured using the index or rate at the commencement date; or
- Payments in respect of purchase options, lease termination options or lease extension options that the Company is reasonably certain to exercise.

The lease liability is subsequently measured by increasing the lease carrying amount to reflect the interest due on the lease liability using the effective interest rate method and by reducing the carrying amount to reflect the lease payments made.

The Company re-measures the lease liability and the related right-of-use asset whenever:

- The lease term changes as a result of the Company changing its assessment of whether it will exercise a purchase, extension or termination option, in which case the lease liability is re-measured by discounting the revised lease payments using a revised discount rate;
- The lease payments change due to changes in an index or rate or a change in expected payment under a guaranteed residual value, in which case the lease liability is re-measured by discounting the revised lease payments using the initial discount rate; or
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is re-measured by discounting the revised lease payments using a revised discount rate.

The right-of-use asset is initially measured at cost, which comprises the initial measurement of the corresponding lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of any costs to be incurred at expiration of the lease agreement.

Right-of-use assets are subsequently measured at cost less accumulated depreciation and any impairment losses. Straight-line depreciation is calculated from the commencement date of the lease to the earlier of either the end date of the lease term or the useful life of the underlying asset.

Both the right-of-use assets and lease liabilities are presented as separate financial statement line items on the balance sheet.

## ACCOUNTING POLICIES CONTINUED

### OTHER INCOME

#### QUOTA SHARE AGREEMENTS

The Company entered into a QST agreement with CCL 1998. Under this agreement CCL 1998 ceded 85.0% of its overall net financial results, which includes both insurance and non-insurance related balances, to the Company. The overall net financial result is recorded within other losses in the statement of comprehensive (loss) income. Amounts receivable or payable under this agreement are recorded within other payable or other receivables on the balance sheet. The overall net financial results is settled on a net basis.

In accordance with Lloyd's requirements the Company was required to provide 85% of the required FAL, to support the underwriting activities of Syndicate 2010 and Syndicate 3010. In 2021, the Company agreed to provide 100% of the required FAL. The amount of FAL required is determined by Lloyd's through the Economic Capital Assessment based on the perceived level of risk the Company underwrites through its syndicate participations.

#### SERVICE FEE INCOME (EXPENSE)

The Company conducts business with its parent company and other Group subsidiaries. This includes providing services, including professional and administrative support services, to related entities within the Group. Service agreements are in place to allow corresponding expenses to be re-allocated to the relevant entity with a mark-up to reflect commercial terms. The Company recognises service fee income in line with services provided during the financial period.

### EMPLOYEE BENEFITS

#### EQUITY COMPENSATION PLANS

LHL, LICL's parent, currently operates a RSS under which nil-cost options have been granted. The fair value of the equity instruments granted is estimated on the date of grant. The estimated fair value is recognised as an expense pro-rata over the vesting period of the instrument within the statement of comprehensive (loss) income, adjusted for the impact of any non-market vesting conditions. No adjustment to vesting assumptions is made in respect of market vesting conditions.

#### PENSIONS

The Company operates a defined contribution plan. On payment of contributions to the plan there is no further obligation for the Company. Contributions are recognised as employee benefits in the statement of comprehensive (loss) income in the period when the services are rendered.

## RISK DISCLOSURES

For the year ended 31 December 2021

### RISK DISCLOSURES: INTRODUCTION

The Company is exposed to risks from several sources, classified into six primary risk categories. These include insurance risk, market risk, liquidity risk, credit risk, operational risk and strategic risk. The primary risk to the Company is insurance risk.

The primary objective of the Company's ERM framework is to ensure that the capital resources held are matched to the risk profile of the Company and that the balance between risk and return is considered as part of all key business decisions. The Company has formulated, and keeps under review, a risk appetite which is set by the Board of Directors. The Company's appetite for risk will vary marginally from time to time to reflect the potential risks and returns that present themselves. However, protecting the Company's capital and maximising risk-adjusted return for investors over the long term are constants. The risk appetite of the Company is central to how the business is run and permeates into the risk appetites that the individual operating entity boards of directors have adopted. These risk appetites are expressed through detailed risk tolerances at both a Company and an operating entity level. Risk tolerances represent the maximum amount of capital, generally on a modelled basis, that the Company and its entities are prepared to expose to certain risks.

The Board of Directors is responsible for setting and monitoring the Company's risk appetite and tolerances. All risk tolerances are subject to at least an annual review and consideration by the respective boards of directors. The Board of Directors review actual risk levels versus tolerances, emerging risks and any risk learning events at least quarterly. In addition, on a monthly basis, management assesses the modelled potential catastrophe losses against the risk tolerances and ensures that risk levels are managed in accordance with them.

### CURRENT EVENTS

#### CLIMATE CHANGE

The Company is exposed to both climate-related risk and opportunities. The two major categories of risk being transition and physical risk. Transition risks are those relating to the transition to a lower carbon economy and include risks such as policy and legal risk, technology risk, market risk and reputation risk. Physical risks are those relating to the physical impacts of climate change which can be acute (those from increased frequency and severity of climate related events) or chronic (due to longer-term shifts in climate patterns). As a (re)insurance Company, LICL is more significantly affected by physical risk through its exposure to acute and chronic climate change. However, consideration must be, and is, given to transition and climate-related litigation risks. The potential financial impact from these climate-related risks is assessed through scenario testing and mitigated by the Company's strategic and risk management decisions on managing these risks. A risk radar has been prepared to illustrate the risks identified, the likelihood of the risks and their product impact. The risk assessment also considers the products currently offered by the Company and how these might change over time during the transition to a lower carbon economy.

In our underwriting operations, we manage this risk effectively by supplementing our internal systems, data and procedures with external vendor models. Underwriting guidelines were developed in 2021 to support the underwriting process and provide guidance to assist underwriters in their decision making. Performance against guidelines is monitored via the UMCC and related reporting. We have clear tolerances and preferences in place to actively manage exposures, and the Board regularly monitors our PMLs. The risks to the asset side of the balance sheet from climate change are monitored through the use of a Climate VaR which is monitored versus the MSCI benchmark in part through regular reviews of our third party asset managers, our asset allocation, and the underlying securities within our portfolio.

Climate change, its related risks and opportunities and their financial impact are a key focus of the board at their quarterly meetings. During the year, the Company participated in the BMA's Climate Change Exposure Assessment which involved the Company performing stress tests for three time horizons for climate change physical risk scenarios. The work performed to date has not resulted in any material impact on our business strategy or change to our understanding of the risks' impacts to our business.

#### GLOBAL TAX REFORM

The Company continues to monitor and assess the implications arising from the Organisation for Economic Co-operation and Development's inclusive framework agreement that aims to implement a global minimum tax rate of 15%, along with the potential impacts of other global tax reforms that are relevant to the Company's business operations.

#### COVID-19

On 12 March 2020, the World Health Organisation classified the COVID-19 outbreak as a pandemic. The COVID-19 pandemic has caused significant disruption in global financial markets and to worldwide economies. The COVID-19 pandemic is an ongoing situation making it exceptionally difficult to predict what the ultimate impact for the Company or the insurance industry will be. The Company continues to monitor the impact of the COVID-19 pandemic on our business. During the year ended 31 December 2021, the Company's ultimate loss estimate, net of reinsurance and the impact of inwards and outwards reinstatement premiums, for COVID-19 related losses has remained stable.

### ECONOMIC CAPITAL MODELS

The Company's economic capital models are primarily focused on insurance risks, however it is also used to model other risks including market, credit and operational risks.

The economic capital models produces data in the form of stochastic distributions for all classes, including non-elemental classes. The distributions include the mean outcome and the result at various return periods, including very remote events. Projected financial outcomes for each insurance class are calculated, as well as the overall portfolio including diversification credit. Diversification credit arises as individual risks are generally not strongly correlated and are unlikely to all produce profits or losses at the same time.

The six primary risk categories are discussed in detail below.

#### A. INSURANCE RISK

The Company underwrites worldwide, predominantly short-tail, insurance and reinsurance contracts that transfer insurance risk, including risks exposed to both natural and man-made catastrophes. The Company's exposure in connection with insurance contracts is, in the event of insured losses, whether premiums will be sufficient to cover the loss payments and expenses. Insurance and reinsurance markets are cyclical and premium rates and terms and conditions vary by line of business depending on market conditions and the stage of the cycle. Market conditions are impacted

## RISK DISCLOSURES CONTINUED

by capacity and recent loss events, and broader economic cycle impacts amongst other factors. The Company's underwriters assess likely losses using their experience and knowledge of past loss experience, industry trends and current circumstances. This allows them to estimate the premiums sufficient to meet likely losses and expenses and desired levels of profitability.

The Company considers insurance risk at an individual contract level, at a segment level, a geographic level and at an aggregate portfolio level. This ensures that careful risk selection, limits on concentration and appropriate portfolio diversification are accomplished. The five principal business segments for the Company are property and casualty reinsurance, property and casualty insurance, aviation, energy, and marine. The level of insurance risk tolerance per peril is set by the respective Boards of Directors at both the LHL and entity level.

A number of controls are deployed to manage the amount of insurance exposure assumed:

- the Company has a rolling three-year strategic plan that helps establish the over-riding business goals that the Board of Directors aims to achieve;
- a detailed business plan is produced annually, which includes expected premiums and combined ratios by class and considers risk-adjusted profitability, capital usage and requirements. The plan is approved by the Board of Directors and is monitored, reviewed and updated on an ongoing basis;
- economic capital models are used to measure occurrence risks, aggregate risks and correlations between classes and other non-insurance risks;
- each authorised class has a predetermined normal maximum line structure;
- each underwriter has a clearly defined limit of underwriting authority;
- the Company has predetermined tolerances on probabilistic and deterministic losses of capital for certain single events;
- risk levels versus tolerances are monitored on a regular basis;
- a daily underwriting call is held to peer review insurance proposals, opportunities and emerging risks;
- sophisticated pricing and aggregation models are utilised in certain areas of the underwriting process;
- a number of modelling tools are deployed to model catastrophes and resultant losses to the portfolio and the Company; and
- reinsurance may be purchased to mitigate both frequency and severity of losses on a facultative, excess of loss treaty or proportional treaty basis.

Some of the Company's business provides coverage for natural catastrophes (e.g. hurricanes, earthquakes, wildfires and floods) and is subject to potential seasonal variation. A proportion of the Company's business is exposed to large catastrophe losses in North America, Europe and Japan as a result of windstorms. The level of windstorm activity, and landfall thereof, during the North American, European and Japanese wind seasons may materially impact the Company's loss experience. The North American and Japanese wind seasons are typically June to November and the European wind season November to March. The Company also bears exposure to large losses arising from other non-seasonal natural catastrophes, such as earthquakes, tsunamis, droughts, floods and tornadoes, from risk losses throughout the year and from war, terrorism and political risk and other events.

### CATASTROPHE MANAGEMENT

The Company actively monitors risk levels and manages catastrophe risk accumulations using reinsurance and PML based risk tolerances. The Company's exposures to certain peak zone elemental losses, excluding our QST agreement with CCL 1998, as a percentage of capital are shown below. Net loss estimates are before income tax and net of reinstatement premiums and outwards reinsurance on a first occurrence return period basis.

As at 31 December 2021		100 year return period estimated net loss		250 year return period estimated net loss	
		\$m	% of capital	\$m	% of capital
Zones	Perils				
Gulf of Mexico <sup>1</sup>	Hurricane	225.4	15.8	435.9	30.5
Non-Gulf of Mexico – U.S.	Hurricane	141.5	9.9	481.4	33.6
Pan-European	Windstorm	112.4	7.9	167.5	11.7
California	Earthquake	98.5	6.9	241.8	16.9
Japan	Typhoon	81.6	5.7	91.8	6.4
Japan	Earthquake	62.1	4.3	106.7	7.5
Pacific North West	Earthquake	10.1	0.7	86.2	6.0

(1) Landing hurricane from Florida to Texas.



## RISK DISCLOSURES CONTINUED

As at 31 December 2020		100 year return period estimated net loss		250 year return period estimated net loss	
		\$m	% of capital	\$m	% of capital
<b>Zones</b>	<b>Perils</b>				
Gulf of Mexico <sup>1</sup>	Hurricane	91.0	7.1	215.8	16.8
Non-Gulf of Mexico – U.S.	Hurricane	61.3	4.8	284.2	22.1
Pan-European	Windstorm	48.6	3.8	59.3	4.6
California	Earthquake	55.4	4.3	81.6	6.3
Japan	Typhoon	39.3	3.1	48.8	3.8
Japan	Earthquake	36.6	2.8	65.7	5.1
Pacific North West	Earthquake	5.9	0.5	40.6	3.2

(1) Landing hurricane from Florida to Texas.

There can be no guarantee that the modelled assumptions and techniques deployed in calculating these figures are accurate. There could also be an unmodelled loss which exceeds these figures. In addition, the models contain loss scenarios which could cause a larger loss to capital than the modelled expectation from the above return periods.

Details of annual gross premiums written by geographic area of risks insured are provided below:

	2021		2020	
	\$m	%	\$m	%
U.S. and Canada	263.2	43.4	146.6	43.5
Worldwide – multi territory	233.3	38.5	116.1	34.4
Europe	50.2	8.3	28.9	8.6
Rest of world	59.3	9.8	45.7	13.5
<b>Total</b>	<b>606.0</b>	<b>100.0</b>	<b>337.3</b>	<b>100.0</b>

Details of annual gross premiums written by business segment are provided below:

	2021		2020	
	\$m	%	\$m	%
Property and casualty reinsurance	432.0	71.3	197.6	58.6
Property and casualty insurance	53.1	8.8	28.9	8.5
Aviation	23.3	3.8	24.2	7.2
Energy	77.7	12.8	57.4	17.0
Marine	19.9	3.3	29.2	8.7
<b>Total</b>	<b>606.0</b>	<b>100.0</b>	<b>337.3</b>	<b>100.0</b>

### I. PROPERTY AND CASUALTY REINSURANCE

Property catastrophe excess of loss covers elemental risks and is written on an excess of loss treaty basis. The property catastrophe excess of loss portfolio is written within the U.S. and also internationally. Cover is offered for specific perils and regions or countries.

Property risk excess of loss is written on an excess of loss basis through UNL treaty arrangements, predominantly covering fire and allied perils in addition to natural catastrophe exposure. The portfolio is written on a worldwide basis, with particular focus on the U.S. market.

Property retrocession is written on an excess of loss basis through treaty arrangements and covers elemental risks. Cover may be on a worldwide or regional basis and may cover specific risks or all catastrophe perils. Coverage may be given on a UNL basis, meaning that loss payments are linked directly to the ceding company's own loss, or on a UNL basis warranted on an overall industry loss, as measured by third party index providers, known as ILW coverage.

Accident & Health is written on a direct and reinsurance basis. The vast majority of the reinsurance business is excess of loss, either facultative or treaty. The direct book is a combination of open-market placements, some binding authorities and broker lineslips, with the focus being Group and Commercial Personal Accident and Disability. The distribution is global but with a focus on the US, Canada, UK and EU. There is very little exposure in Asia, Australasia, Africa or South America. Typical coverage offered is death & disablement, medical expenses, evacuation and repatriation, and other limited ancillary expenses.

The casualty book is written predominantly on a quota share basis with a limited amount of excess of loss sold. The book is made up of predominantly U.S. exposure in general casualty and professional lines with some smaller specialty casualty deals and excess casualty.

The specialty reinsurance book is written predominantly on an excess of loss basis and comprises similar exposures to those underwritten out of our insurance operation with a focus on 'Blue Chip' clients.

The Company is exposed to large natural catastrophe losses, such as windstorm and earthquake losses, primarily from assuming property catastrophe excess of loss and property retrocession portfolio risks. Exposure to such events is controlled and measured by setting limits on aggregate exposures in certain classes per geographic zone and through loss modelling. The accuracy of the latter exposure analysis is limited by



## RISK DISCLOSURES CONTINUED

the quality of data and the effectiveness of the modelling. It is possible that a catastrophic event significantly exceeds the expected modelled event loss.

Reinsurance may be purchased to mitigate exposures to large natural catastrophe losses in the U.S., Canada and worldwide with certain exclusions. Reinsurance may also be purchased to reduce the Company's worldwide exposure to large risk losses. Reinsurance is typically purchased on an excess of loss basis, however ILWs or proportional treaty arrangements may be entered into.

### II. PROPERTY AND CASUALTY INSURANCE

Property direct and facultative is a worldwide book of largely commercial property business, written both in the open market and under delegated authorities. The account spans small individual locations to Fortune 500 accounts but with a bias towards small to medium-sized risks. Policies are generally provided both for non-elemental and elemental perils, although not all risks include both elemental and non-elemental coverage. Coverage is generally written on a full value, primary or excess of loss basis, although the very largest accounts are currently seldom written at the primary level.

Terrorism business can be written either ground-up or for primary or excess layers, with cover provided for U.S. and worldwide property risks, but typically excluding nuclear, chemical, biological and cyber coverage in most territories. Cover is generally provided to medium to large commercial and industrial enterprises. Policies are typically written for scheduled locations and exposure is controlled by setting limits on aggregate exposure within a 'blast zone' radius. The term of these contracts is often multi-year reflecting the term of the underlying exposures. Some national pools are also written, which may include nuclear, chemical and biological coverage and may have an element of life coverage.

Property political risk cover is written either ground-up or on an excess of loss basis. Coverage that the Company provides in the political risk book is split between confiscation perils coverage and sovereign/quasi-sovereign obligor coverage. Confiscation perils coverage protects against CEND and may be extended to include other perils. Sovereign/quasi-sovereign obligors coverage protects against the non-payment or non-honouring of an obligation by a sovereign or quasi-sovereign entity. Cover is provided to medium to large commercial and industrial clients as well as bank and commodity trading clients. The term of these contracts is often multi-year reflecting the term of the underlying exposures. The Company does not provide cover against purely private obligor credit risk

Reinsurance may also be purchased to reduce the Company's worldwide exposure to large risk losses. Reinsurance is typically purchased on an excess of loss basis, however ILWs or proportional treaty arrangements may be entered into.

### III. AVIATION

Aviation deductible business is a specialist area with small individual limits normally up to \$1.0 million and covers the deductible the airline would normally have for each and every loss under the terms of their airline policy.

AV52 is written on a risk-attaching excess of loss basis and provides coverage for third-party liability, excluding own passenger liability, resulting from acts of war or hijack of aircraft. Cover excludes countries whose governments provide a backstop coverage, but does, include some U.S. commercial airlines.

Aviation hull and liability line provides cover to the airlines directly and includes cover for the aircraft themselves as well as losses arising from passenger and third-party liability claims against airlines and/or manufacturers.

Aviation war covers loss or damage to aviation assets from war, terrorism and similar causes.

Reinsurance may be purchased to mitigate exposures to an AV52 event loss. Reinsurance is typically purchased on a treaty excess of loss basis. Proportional treaty reinsurance is typically used to reduce the Company's exposure to aviation deductible and the aviation hull and liability business.

### IV. ENERGY

Energy risks are written mostly on a direct basis and may be ground-up or for primary or excess layers on either a first loss or full value basis. Upstream energy policies are typically package policies which may include physical damage, business interruption and third-party liability sections. Coverage can include fire and explosion and elemental risks. Individual assets covered can be high-value and are therefore mostly written on a subscription basis, meaning that coverage is placed with multiple risk carriers.

Downstream energy risks are generally those with an operational hydrocarbon risk - either processing and/or storage and/or transmission - and may also include production of chemicals and intermediates. Policies typically cover property for physical damage (including natural catastrophe) and machinery breakdown perils plus consequential business interruption exposure and may be written on a proportional or excess of loss basis, often with loss limits set at a level commensurate with a modelled estimated maximum loss scenario. The portfolio encompasses a global spread of accounts. Critical natural catastrophe coverage is usually sub-limited, with underwriting assessment employing industry-accepted modelling tools to assess this exposure where possible. The sector provides cover for operational assets, albeit some construction risk is covered where it is not deemed the policy's primary exposure. Third-party liabilities are not covered except where required under legislation for small sub-limited property damage.

The Company writes energy liability business on a stand-alone basis. Unlike the liability contained within the energy packages that the Company writes, stand-alone energy liability is written on an excess of loss basis only. Coverage is worldwide and provides coverage for all kinds of damages and loss to third parties. Coverage is generally restricted to upstream and midstream assets.

Gulf of Mexico offshore energy programmes cover elemental and non-elemental risks. Most policies have sub-limits on coverage for elemental losses. These programmes are exposed to Gulf of Mexico windstorms. Exposure to such events is controlled and measured through loss modelling. The accuracy of this exposure analysis is limited by the quality of data and the effectiveness of the modelling. It is possible that a catastrophic event significantly exceeds the expected modelled event loss.

Construction energy upstream contracts generally cover all risks of platform and drilling units under construction at yards and offshore, during towing and installation. Onshore construction contracts are generally not written.

## RISK DISCLOSURES CONTINUED

Reinsurance protection may be purchased to protect a portion of loss from elemental and non-elemental energy claims, and from the accumulation of smaller, attritional losses. Reinsurance is typically purchased on an excess of loss basis but, from time to time, proportional treaty arrangements may be entered into. Reinsurance may be purchased on a facultative or treaty basis.

### V. MARINE

With the exception of marine liability, where excess layers are written, most policies are written on a ground-up basis. Marine liability is mostly the reinsurance of the International Group of Protection and Indemnity Clubs and covers marine liabilities. Marine hull and total loss is generally written on a direct basis and covers marine risks on a worldwide basis, primarily for physical damage. Marine builders' risk covers the building of ocean-going vessels in specialised yards worldwide and their testing and commissioning. Marine hull war is mostly direct insurance of the loss of vessels from war, piracy or terrorist attack, with a very limited amount of facultative reinsurance. Marine excess of loss is written on a treaty basis and covers ocean and inland marine risks.

The largest expected exposure in the marine class is from physical loss rather than from elemental loss events, although there is exposure to elemental perils and to the costs for removal of wreck.

Reinsurance may be purchased to reduce the Company's exposure to both large risk losses and an accumulation of smaller, attritional losses. Reinsurance is typically purchased on a treaty excess of loss basis.

### REINSURANCE

The Company, in the normal course of business and in accordance with its risk management practices, seeks to reduce certain types of loss that may arise from events that could cause unfavourable underwriting results by entering into reinsurance arrangements. Reinsurance does not relieve the Company of its obligations to policyholders. Under the Company's reinsurance security policy, reinsurers are assessed and approved as appropriate security based on their financial strength ratings, amongst other factors. The RSC considers reinsurers that are not rated or do not fall within the predefined rating categories on a case-by-case basis, and may require collateral to be posted to support such obligations. There are specific guidelines for these collateralised contracts. The RSC monitors its reinsurers on an ongoing basis and formally reviews the Company's reinsurance arrangements at least quarterly. Exposure to the Company's reinsurance counterparties, compared to the board approved tolerance, is reported to the Board of Directors on a quarterly basis.

Reinsurance protection is typically purchased on an excess of loss basis, however it may also include ILW covers or proportional treaty arrangements. The mix of reinsurance cover is dependent on the specific loss mitigation requirements, market conditions and available capacity. Reinsurance may also be purchased to optimise the risk-adjusted return of the underwriting portfolio. The structure varies between types of peril and sub-class. The Company regularly reviews its catastrophe and other exposures and may purchase reinsurance in order to reduce the Company's net exposure to a large natural catastrophe loss and/or to reduce net exposures to other large losses. The Company can purchase both facultative and treaty reinsurance with varying cover and attachment points. The reinsurance coverage is not intended to be available to meet all potential loss circumstances. The Company will retain some losses, as the cover purchased is unlikely to transfer the totality of the Company's exposure. Any loss amount which exceeds the programme would be retained by the Company. Some parts of the reinsurance programme have limited reinstatements, therefore the number of claims which may be recovered from second or subsequent losses in those particular circumstances is limited.

### INSURANCE LIABILITIES

For most insurance and reinsurance companies, the most significant judgement made by management is the estimation of losses and loss adjustment expenses. The estimation of the ultimate liability arising from claims made under insurance and reinsurance contracts is a critical estimate for the Company, particularly given the nature of the business written.

Under GAAP, loss reserves are not permitted until the occurrence of an event which may give rise to a claim. As a result, only loss reserves applicable to losses incurred up to the reporting date are established, with no allowance for the provision of a contingency reserve to account for expected future losses or for the emergence of new types of latent claims. Claims arising from future events can be expected to require the establishment of substantial reserves from time to time. All of the Company's reserves are reported on an undiscounted basis.

Losses and loss adjustment expense reserves are maintained to cover the Company's estimated liability for both reported and unreported claims. Reserving methodologies that calculate an actuarial best estimate for the ultimate losses, along with a reserve margin are utilised. This represents the management's best estimate of ultimate loss and loss adjustment expenses. The Company's internal actuaries review the reserving assumptions and methodologies on a quarterly basis with loss estimates being subject to a semi-annual independent review by external actuaries. The results of the independent review are presented to the Group's Audit Committee. The Group has also established Reserve Committees at the operating entity level, which have responsibility for the review of large claims and IBNR levels, their development and any changes in reserving methodology and assumptions.

The extent to which the reserving process relies on management's judgement is dependent on a number of factors including whether the business is insurance or reinsurance, whether it is short-tail or long-tail and whether the business is written on an excess of loss or pro-rata basis.

### INSURANCE VERSUS REINSURANCE

Loss reserve calculations whether reserving for direct insurance business or for reinsurance classes are not precise in that they deal with the inherent uncertainty of assumptions regarding future reporting and development patterns, frequency and severity trends, claims settlement practices, potential changes in the legal environment and other factors, such as inflation. The estimates and judgements relied on in making loss reserve calculations are based on a number of factors and may be revised as additional experience or other data becomes available.

Loss reserve calculations are also reviewed as new or improved methodologies are developed and as laws or regulations change. Furthermore, as a business operating within a broker market, management must rely on loss information reported to brokers by other insurers and their loss adjusters, who must estimate their own losses at the policy level, often based on incomplete and changing information. The information management receives varies by cedant and may include paid losses, estimated case reserves and an estimated provision for IBNR reserves. Additionally, reserving practices and the quality of data reporting may vary among ceding companies, which adds further uncertainty to management's estimates of the ultimate losses.

## RISK DISCLOSURES CONTINUED

### SHORT-TAIL VERSUS LONG-TAIL

In general, claims relating to short-tail risks, such as the majority of risks underwritten by the Company, are reported more promptly than those relating to long-tail risks, including the majority of casualty risks. The timeliness of reporting can be affected by such factors as the nature of the event causing the loss, the location of the loss and whether the losses are from policies in force with insureds, primary insurers, reinsurers or vendor binding authorities.

### EXCESS OF LOSS VERSUS PROPORTIONAL

For excess of loss contracts, which make up the majority of the Company's business, management is aided by the fact that each policy has a defined limit of liability arising from one event. Once that limit has been reached, there is no further exposure to additional losses from that policy for the same event. For proportional business, an initial estimated loss and loss expense ratio is generally used. This is based upon information provided by the insured or ceding company and/or their broker and management's historical experience of that treaty, if any, and the estimate is adjusted as actual experience becomes known.

### TIME LAGS

There is a time lag inherent in reporting from the original claimant to the primary insurer or binding authority holder to the broker and then to the reinsurer. Also, the combination of low claims frequency and high severity across many of our classes makes the available data more volatile and less useful for predicting ultimate losses. In the case of proportional contracts, reliance is placed on an analysis of a contract's historical experience, industry information, and the professional judgement of underwriters in estimating reserves for these contracts. In addition, if available, reliance is placed partially on ultimate loss ratio forecasts as reported by insureds or cedants, which are normally subject to a quarterly or six-month time lag.

### UNCERTAINTY

As a result of the time lag described above, an estimate must be made of IBNR reserves, which consists of a provision for additional development in excess of the case reserves reported by insureds or ceding companies, as well as a provision for claims which have occurred but which have not yet been reported by insureds or ceding companies. Due to the degree of reliance that is necessarily placed on insureds or ceding companies for claims reporting, the associated time lag, the low frequency/high severity nature of much of the business that the Company underwrites, and the varying reserving practices among ceding companies, reserve estimates are highly dependent on management judgement and are therefore uncertain. During the loss settlement period, which may be years in duration, additional facts regarding individual claims and trends often will become known, and current laws and case law may change as well as regulatory directives, with a consequent impact on reserving.

For certain catastrophic events there are greater uncertainties underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Complexity resulting from problems such as policy coverage issues, multiple events affecting one geographic area and the resulting impact on claims adjusting (including the allocation of claims to the specific event and the effect of demand surge on the cost of building materials and labour) by, and communications from, insureds or ceding companies, can cause delays to the timing with which the Company is notified of changes to loss estimates.

The breakdown of losses and loss adjustment expenses between notified outstanding losses, ACR and IBNR are show in note 11. The majority of the IBNR estimate relates to catastrophe events from 2017-2021, in addition to potential claims on non-elemental risks where timing delays in insured or cedant reporting may mean losses could have occurred of which the Company was not made aware by the balance sheet date.

## B. MARKET RISK

The Company is at risk of loss due to movements in market factors. The main risks include insurance market risk, investment risk and currency risk.

These risks, and the management thereof, are described below.

### I. INSURANCE MARKET RISK

The Company is exposed to insurance market risk from several sources, including the following:

- the advent or continuation of a soft market, which may result in a stabilisation or decline in premium rates and/or terms and conditions for certain lines, or across all lines;
- the actions and reactions of key competitors, which may directly result in volatility in premium volumes and rates, fee levels and other input costs;
- market events, including unusual inflation in rates, may result in a limit in the availability of cover, causing political intervention or national remedies;
- failure to maintain broker, binding authority and client relationships, leading to a limited or substandard choice of risks inconsistent with the Company's risk appetite;
- changes in regulation including capital, governance or licensing requirements; and
- changes in geopolitical environment including the UK's exit from the EU and the implications for ongoing business passporting within the EEA.

The most important method to mitigate insurance market risk is to maintain strict underwriting standards. The Company manages insurance market risk in numerous ways, including the following:

- reviews and amends underwriting plans and outlook as necessary;
- reduces exposure to market sectors where conditions have reached unattractive levels;
- purchases appropriate, cost-effective reinsurance cover to mitigate exposures;
- closely monitors changes in rates and terms and conditions;

## RISK DISCLOSURES CONTINUED

- ensures through continuous capital management that it does not allow surplus capital to drive underwriting appetite;
- holds a daily underwriting call to discuss, inter alia, market conditions and opportunities;
- reviews output from the economic capital models to assess up-to-date profitability of classes and sectors;
- holds a fortnightly Group RRC meeting to discuss risk and reinsurance;
- holds a quarterly Group Underwriting and Underwriting Risk Committee meeting to review underwriting strategy; and
- holds regular documented meetings with regulators.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest bearing.

### II. INVESTMENT RISK

Movements in investments resulting from changes in interest and inflation rates and currency exchange rates, amongst other factors, may lead to an adverse impact on the value of the Company's investment portfolio.

Investment guidelines are established by the Investment Committee of the LHL Board of Directors to manage this risk. The LICL Board of Directors reviews and adopts these guidelines as appropriate. Investment guidelines set parameters within which the Company's external investment managers must operate. 93.6% of the Company's externally managed portfolio are managed by signatories of the UNPRI. Important parameters include guidelines on permissible asset classes, duration ranges, credit quality, currency, maturity, sectors, geographical, sovereign and issuer exposures. Compliance with guidelines is monitored on a monthly basis. Any adjustments to the investment guidelines are approved by the Investment Committee, the LHL Board of Directors and LICL Board of Directors.

The Company's fixed maturity portfolios are managed by five external investment managers. The Company also has a diversified low volatility multi-strategy portfolio of hedge funds, credit funds, principal protected products and private investment funds. The performance of the managers is monitored on an ongoing basis.

Within the Company guidelines are subsets of guidelines for the portion of funds required to meet near-term obligations and cash flow needs following an extreme event. These guidelines add a further degree of requirements, including fewer allowable asset classes, higher credit quality, shorter duration and higher liquidity. The primary objectives for this portion of assets are capital preservation and providing liquidity to meet insurance and other near-term obligations. In addition to cash managed internally, funds held in the investment portfolio to cover this potential liability are designated as the core and core plus portfolios and the portfolio duration is matched to the duration of the insurance liabilities, within an agreed range. The core and core plus portfolios are invested in fixed maturity securities, fixed maturity funds and cash and cash equivalents. The combined core and core plus portfolio may, at times, contain assets significantly in excess of those required to meet insurance liabilities or other defined funding needs.

Assets in excess of those required to be held in the core and core plus portfolios are typically held in the surplus portfolios. The surplus portfolio is invested in fixed maturity securities, principal protected products, derivative instruments, cash and cash equivalents, private investment funds, hedge funds and index linked securities. In general, the duration of the surplus portfolio is slightly longer than the core or core plus portfolio.

The Company reviews the composition, duration and asset allocation of its investment portfolio on a regular basis in order to respond to changes in interest rates and other market conditions. If certain asset classes are anticipated to produce a higher return within management's risk tolerance, an adjustment in asset allocation may be made. Conversely, if the risk profile is expected to move outside of tolerance levels, adjustments may be made to reduce the risks in the portfolio.

The investment portfolio is currently structured to perform similarly in risk-on and risk-off environments. The Company endeavours to limit losses in risk-on, risk-off, and interest rate hike scenarios. The Company models various periods of significant stress in order to better understand the investment portfolio's risks and exposures. The scenarios represent what could, and most likely will occur (albeit not in the exact form of the scenarios, which are based on historic periods of volatility). The Company also monitors the portfolio impact of more severe disaster scenarios consisting of extreme shocks.

The Investment Committee performs a strategic asset allocation study on a biannual basis, which assesses the Company's overall strategy and to determine alternative asset allocations to achieve the best risk-adjusted return within our risk tolerances. The IRRC meets quarterly to ensure that the Company's strategic and tactical investment actions are consistent with investment risk preferences, appetite, risk and return objectives and tolerances. The IRRC also helps further develop the risk tolerances to be incorporated into the ERM framework. During the year the Investment Committee approved the use of a climate-related VaR to monitor the potential climate related financial impact on our portfolio. This VaR will be monitored against an industry benchmark.

## RISK DISCLOSURES CONTINUED

The investment mix of the fixed maturity portfolios is as follows:

As at 31 December 2021	Core		Core plus		Surplus		Total	
	\$m	%	\$m	%	\$m	%	\$m	%
– Short-term investments	6.8	0.5	20.2	1.4	—	—	27.0	1.9
– U.S. treasuries	104.1	7.2	280.6	19.6	51.7	3.6	436.4	30.4
– Other government bonds	—	—	—	—	47.2	3.3	47.2	3.3
– U.S. municipal bonds	—	—	14.6	1.0	5.4	0.4	20.0	1.4
– U.S. government agency debt	—	—	29.8	2.1	21.1	1.5	50.9	3.6
– Asset backed securities	8.0	0.6	19.5	1.4	75.4	5.2	102.9	7.2
– U.S. government agency mortgage backed securities	2.8	0.2	8.6	0.6	66.5	4.6	77.9	5.4
– Non-agency mortgage backed securities	—	—	4.6	0.3	28.6	2.0	33.2	2.3
– Agency commercial mortgage back securities	—	—	—	—	0.1	—	0.1	—
– Non-agency commercial mortgage back securities	—	—	—	—	20.1	1.4	20.1	1.4
– Bank loans	—	—	—	—	110.2	7.7	110.2	7.7
– Corporate bonds	73.5	5.1	319.7	22.3	91.1	6.3	484.3	33.7
<b>Total fixed maturity securities – AFS</b>	<b>195.2</b>	<b>13.6</b>	<b>697.6</b>	<b>48.7</b>	<b>517.4</b>	<b>36.0</b>	<b>1,410.2</b>	<b>98.3</b>
Fixed maturity securities – at FVTPL	—	—	—	—	25.0	1.7	25.0	1.7
<b>Total fixed maturity securities</b>	<b>195.2</b>	<b>13.6</b>	<b>697.6</b>	<b>48.7</b>	<b>542.4</b>	<b>37.7</b>	<b>1,435.2</b>	<b>100.0</b>

As at 31 December 2020	Core		Core plus		Surplus		Total	
	\$m	%	\$m	%	\$m	%	\$m	%
– Short-term investments	20.8	1.6	50.4	3.9	1.0	0.1	72.2	5.6
– U.S. treasuries	62.9	4.8	125.4	9.7	10.3	0.8	198.6	15.3
– Other government bonds	0.3	—	10.3	0.8	36.4	2.8	47.0	3.6
– U.S. municipal bonds	—	—	7.0	0.5	3.5	0.3	10.5	0.8
– U.S. government agency debt	—	—	30.7	2.4	66.4	5.1	97.1	7.5
– Asset backed securities	1.5	0.1	61.2	4.7	60.0	4.6	122.7	9.4
– U.S. government agency mortgage backed securities	3.1	0.2	12.6	1.0	104.6	8.1	120.3	9.3
– Non-agency mortgage backed securities	—	—	6.8	0.5	10.3	0.9	17.1	1.4
– Agency commercial mortgage back securities	—	—	—	—	0.3	—	0.3	—
– Non-agency commercial mortgage back securities	—	—	—	—	5.8	0.4	5.8	0.4
– Bank loans	—	—	—	—	110.5	8.5	110.5	8.5
– Corporate bonds	75.5	5.8	330.9	25.5	59.5	4.6	465.9	35.9
<b>Total fixed maturity securities - AFS</b>	<b>164.1</b>	<b>12.5</b>	<b>635.3</b>	<b>49.0</b>	<b>468.6</b>	<b>36.2</b>	<b>1,268.0</b>	<b>97.7</b>
Fixed maturity securities - at FVTPL	—	—	—	—	29.3	2.3	29.3	2.3
<b>Total fixed maturity securities</b>	<b>164.1</b>	<b>12.5</b>	<b>635.3</b>	<b>49.0</b>	<b>497.9</b>	<b>38.5</b>	<b>1,297.3</b>	<b>100.0</b>

## RISK DISCLOSURES CONTINUED

Bank loans, corporate bonds, fixed maturity securities at FVTPL and other government bonds by country are as follows:

As at 31 December 2021	Financials \$m	Other industries \$m	Total <sup>1</sup> \$m	Other government bonds \$m	Total <sup>2</sup> \$m
United States	155.1	295.0	450.1	—	450.1
United Kingdom	22.1	10.4	32.5	—	32.5
Canada	10.5	9.9	20.4	10.0	30.4
Japan	12.3	3.8	16.1	—	16.1
Netherlands	4.7	5.6	10.3	1.1	11.4
Mexico	3.3	4.2	7.5	1.5	9.0
Sweden	8.2	—	8.2	—	8.2
Qatar	1.7	—	1.7	6.2	7.9
France	4.1	2.6	6.7	—	6.7
Switzerland	5.2	1.3	6.5	—	6.5
Germany	4.9	1.5	6.4	—	6.4
United Arab Emirates	5.3	0.9	6.2	—	6.2
India	—	4.7	4.7	1.5	6.2
Australia	5.2	0.5	5.7	—	5.7
Indonesia	—	0.5	0.5	4.8	5.3
Other	19.9	16.1	36.0	22.1	58.1
<b>Total</b>	<b>262.5</b>	<b>357.0</b>	<b>619.5</b>	<b>47.2</b>	<b>666.7</b>

(1) Includes bank loans, corporate bonds and fixed maturity securities at FVTPL.

(2) Includes bank loans, corporate bonds, fixed maturity securities at FVTPL and other government bonds.

As at 31 December 2020	Financials \$m	Other industries \$m	Total <sup>1</sup> \$m	Other government bonds \$m	Total <sup>2</sup> \$m
United States	147.5	295.2	442.7	—	442.7
United Kingdom	21.2	13.8	35.0	—	35.0
Canada	11.3	2.5	13.8	7.1	20.9
Japan	11.6	5.9	17.5	—	17.5
France	12.3	3.7	16.0	—	16.0
Switzerland	7.7	2.7	10.4	4.0	14.4
Sweden	7.3	—	7.3	3.6	10.9
Netherlands	3.8	4.2	8.0	—	8.0
Spain	7.6	—	7.6	—	7.6
China	1.0	2.5	3.5	3.9	7.4
Australia	6.2	0.2	6.4	—	6.4
Germany	—	6.3	6.3	—	6.3
Italy	3.2	2.9	6.1	—	6.1
United Arab Emirates	2.5	1.5	4.0	1.5	5.5
Qatar	1.6	—	1.6	2.9	4.5
Other	8.8	10.7	19.5	24.0	43.5
<b>Total</b>	<b>253.6</b>	<b>352.1</b>	<b>605.7</b>	<b>47.0</b>	<b>652.7</b>

(1) Includes bank loans, corporate bonds and fixed maturity securities at FVTPL.

(2) Includes bank loans, corporate bonds, fixed maturity securities at FVTPL and other government bonds.

## RISK DISCLOSURES CONTINUED

The sector allocation of bank loans, corporate bonds and fixed maturity securities at FVTPL is as follows:

As at 31 December	2021		2020	
	\$m	%	\$m	%
Industrial	330.6	53.3	323.4	53.4
Financial	262.5	42.4	253.6	41.9
Utility	26.4	4.3	28.7	4.7
<b>Total</b>	<b>619.5</b>	<b>100.0</b>	<b>605.7</b>	<b>100.0</b>

The Company's net asset value is directly impacted by movements in the fair value of investments held. Values can be impacted by movements in interest rates, credit ratings, exchange rates, the current economic environment and outlook.

The Company's investment portfolio is mainly comprised of fixed maturity securities and cash and cash equivalents. The Company also has a hedge fund portfolio as well as principal protected notes and has invested in private investment funds. The estimated fair value of the Company's fixed maturity portfolio is generally inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Company's fixed maturity securities would tend to rise and vice versa.

The sensitivity of the price of fixed maturity securities, and certain derivatives, to movements in interest rates is indicated by their duration. The greater a security's duration, the greater its price volatility to movements in interest rates. The sensitivity of the Company's fixed maturity and derivative investment portfolio to interest rate movements is detailed below, assuming linear movements in interest rates:

As at 31 December	2021		2020	
	\$m	%	\$m	%
<b>Immediate shift in yield (basis points)</b>				
100	(29.9)	(2.1)	(29.4)	(2.0)
75	(22.4)	(1.6)	(22.0)	(1.5)
50	(15.0)	(1.0)	(14.7)	(1.0)
25	(7.5)	(0.5)	(7.3)	(0.5)
(25)	7.5	0.5	7.5	0.5
(50)	15.0	1.1	15.0	1.0
(75)	22.5	1.6	22.5	1.6
(100)	30.0	2.1	30.0	2.1

The Company mitigates interest rate risk on the investment portfolio by establishing and monitoring duration ranges in its investment guidelines. The Company may manage duration through the use of interest rate futures and swaptions from time to time. The duration of the core portfolio is matched to the modelled duration of the insurance reserves, within a permitted range. The permitted duration range for the core plus portfolio is between zero and four years and the surplus portfolio is between one and five years.

The overall duration for fixed maturities, managed cash and cash equivalents and certain derivatives is 1.8 years (31 December 2020 – 2.1 years).

In addition to duration management, the Company monitors VaR to measure potential losses in the estimated fair values of its cash and invested assets and to understand and monitor risk. The VaR calculation is performed using variance/covariance risk modelling to capture the cash flows and embedded optionality of the portfolio. Securities are valued individually using standard market pricing models. These security valuations serve as the input to many risk analytics, including full valuation risk analyses, as well as parametric methods that rely on option-adjusted risk sensitivities to approximate the risk and return profiles of the portfolio.

## RISK DISCLOSURES CONTINUED

The principal VaR measure that is produced is an annual VaR at the 99th percentile confidence level. Under normal conditions, the portfolio is not expected to lose more than the VaR metric listed in the table below, 99% of the time over a one-year time horizon. The appropriateness of this measure is considered by the Investment Committee on behalf of the Board of Directors on an annual basis.

The Company's annual VaR calculations are as follows:

As at 31 December	2021		2020	
	\$m	% of shareholder's equity	\$m	% of shareholder's equity
99th percentile confidence level <sup>1</sup>	47.6	3.3	55.1	4.3

(1) Excluding the impact of internal foreign exchange hedges.

### DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses derivative financial instruments primarily to mitigate exposure to foreign currency risk, interest rate risk and credit risk. The Company's investment guidelines permit the investment managers to utilise exchange-traded futures and options contracts, OTC instruments including interest rate swaps, credit default swaps, interest rate swaptions and forward foreign currency contracts.

The net (losses) gains on the Company's derivative financial instruments recognised in the statement of comprehensive (loss) income are as follows:

As at 31 December	2021			2020		
	Net realised gains \$m	Net realised losses \$m	Net foreign exchange losses \$m	Net realised gains \$m	Net realised losses \$m	Net foreign exchange losses \$m
Interest rate futures	—	(0.5)	—	2.0	—	—
Forward foreign currency contracts	—	—	(0.8)	—	—	(0.6)
Interest rate swaps	0.3	—	—	—	—	—
<b>Total</b>	<b>0.3</b>	<b>(0.5)</b>	<b>(0.8)</b>	<b>2.0</b>	<b>—</b>	<b>(0.6)</b>

The estimated fair values of the Company's derivative instruments are as follows:

As at 31 December	2021			2020		
	Other investments \$m	Other receivables \$m	Other payables \$m	Other investments \$m	Other receivables \$m	Other payables \$m
Forward foreign currency contracts	(0.3)	0.6	(0.6)	(0.7)	1.0	(0.3)
Interest rate swaps	(0.3)	—	—	—	—	—
Credit default swaps	0.5	—	—	—	—	—
<b>Total</b>	<b>(0.1)</b>	<b>0.6</b>	<b>(0.6)</b>	<b>(0.7)</b>	<b>1.0</b>	<b>(0.3)</b>

### A. FUTURES

The Company's investment guidelines permit the use of futures which provide the Company with participation in market movements, determined by the underlying instrument on which the futures contract is based, without holding the instrument itself or the individual securities. This approach allows the Company more efficient and less costly access to the exposure than would be available by the exclusive use of individual fixed maturity and money market securities. Exchange-traded futures contracts may also be used as substitutes for ownership of the physical securities.

All futures contracts are held on a non-leveraged basis. An initial margin is provided, which is a deposit of cash and/or securities in an amount equal to a prescribed percentage of the contract value. The fair value of futures contracts is estimated daily and the margin is adjusted accordingly with unrealised gains and/or losses settled daily in cash and/or securities. A realised gain or loss is recognised when the contract is closed.

Futures contracts expose the Company to market risk to the extent that adverse changes occur in the estimated fair values of the underlying securities. Exchange-traded futures are, however, subject to a number of safeguards to ensure that obligations are met. These include the use of clearing houses (thus reducing counterparty credit risk), the posting of margins and the daily settlement of unrealised gains and losses. The amount of credit risk is therefore considered low. The investment guidelines restrict the maximum notional futures position as a percentage of the investment portfolio's estimated fair value.



## RISK DISCLOSURES CONTINUED

The Company's exposure to interest rate futures are as follows:

As at 31 December	2021			2020		
	Notional long \$m	Notional short \$m	Net notional long (short) \$m	Notional long \$m	Notional short \$m	Net notional long (short) \$m
Interest rate futures	44.1	36.8	7.3	37.6	11.8	25.8

### B. OPTIONS

The Company's investment guidelines permit the use of exchange-traded options on U.S. treasury futures and Eurodollar futures, which are used to manage exposure to interest rate risk and also to hedge duration. Exchange-traded options are held on a similar basis to futures and are subject to similar safeguards. Options are contractual arrangements that give the purchaser the right, but not the obligation, to either buy or sell an instrument at a specific set price at a predetermined future date. The Company may enter into option contracts that are secured by holdings in the underlying securities or by other means which permit immediate satisfaction of the Company's obligations. The notional amount of options is \$nil as at 31 December 2021 and 2020.

The investment guidelines also restrict the maximum notional options exposure as a percentage of the investment portfolio's estimated fair value.

### C. FORWARD FOREIGN CURRENCY CONTRACTS

A forward foreign currency contract is a commitment to purchase or sell a foreign currency at a future date, at a defined rate. The Company may utilise forward foreign currency contracts to gain exposure to a certain currency or market rate or manage the impact of fluctuations in foreign currencies on the value of its foreign currency denominated investments, debt and/or insurance related currency exposures and expenses.

Forward contracts expose the Company to credit, market and liquidity risks. Credit risk arises from the potential inability of counterparties to perform under the terms of the contract. The Company is exposed to market risk to the extent that adverse changes occur in the exchange rate of the underlying foreign currency. Liquidity risk represents the possibility that the Company may not be able to rapidly adjust the size of its forward positions at a reasonable price in times of high volatility and financial stress. These risks are mitigated by requiring a minimum counterparty credit quality, restricting the maximum notional exposure as a percentage of the investment portfolio's estimated fair value and restricting exposures to foreign currencies, individually and in aggregate, as a percentage of the investment portfolio's estimated fair value.

The notional amount of a derivative contract is the underlying quantity upon which payment obligations are calculated. A long position is equivalent to buying the underlying currency whereas a short position is equivalent to having sold the underlying currency.

The Company has the following open forward foreign currency contracts:

As at 31 December	2021			2020		
	Notional long \$m	Notional short \$m	Net notional long (short) \$m	Notional long \$m	Notional short \$m	Net notional long (short) \$m
Canadian Dollar	—	36.2	(36.2)	—	24.6	(24.6)
Euro	19.2	21.0	(1.8)	18.2	27.9	(9.7)
Australian Dollar	—	9.3	(9.3)	—	11.3	(11.3)
Japanese Yen	—	—	—	6.7	—	6.7
Danish Krone	—	3.9	(3.9)	—	—	—
Sterling	45.2	7.6	37.6	30.0	7.6	22.4
<b>Total</b>	<b>64.4</b>	<b>78.0</b>	<b>(13.6)</b>	<b>54.9</b>	<b>71.4</b>	<b>(16.5)</b>

### D. SWAPS

Interest rate swaps, traded primarily OTC, are used to manage interest rate exposure, portfolio duration or capitalise on anticipated changes in interest rate volatility without investing directly in the underlying securities. Interest rate swap agreements entail the exchange of commitments to pay or receive interest, such as an exchange of floating rate payments for fixed rate payments, with respect to a notional amount of principal. These agreements involve elements of credit and market risk. Such risks include the possibility that there may not be a liquid market, that the counterparty may default on its obligation to perform, or that there may be unfavourable movements in interest rates. These risks are mitigated through defining a minimum counterparty credit quality and a maximum notional exposure to interest rate swaps as a percentage of the investment portfolio's estimated fair value. The notional amount of interest rate swaps held in the investment portfolio was \$1.3 million as at 31 December 2021 (31 December 2020 – \$nil). The notional amount of interest rate swaps held for hedging purposes was \$nil as at 31 December 2021 and 2020.

The Company may utilise credit default swaps to add or reduce credit risk to an individual issuer, or a basket of issuers without investing directly in their securities. The Company held credit default swaps of \$13.4 million as at 31 December 2021 (31 December 2020 – \$nil million).

## RISK DISCLOSURES CONTINUED

### III. CURRENCY RISK

The Company underwrites from Bermuda, although risks are assumed on a worldwide basis. Risks assumed are predominantly denominated in U.S. dollars.

The Company is exposed to currency risk to the extent its assets are denominated in different currencies to its liabilities. Exchange gains and losses can impact profit or loss.

The Company hedges monetary non-U.S. dollar liabilities primarily with non-U.S. dollar assets, but may also use derivatives to mitigate foreign currency exposures. The Company's main foreign currency exposure relates to its insurance obligations, cash holdings, investments, premiums receivable and dividends payable. The Company uses forward foreign currency contracts for the purposes of managing currency exposures. The Company uses forward foreign currency contracts for the purpose of managing currency exposures.

The Company's assets and liabilities, categorised by currency at their translated carrying amount, are as follows:

Assets	U.S. \$ \$m	Sterling \$m	Euro \$m	Japanese Yen \$m	Other \$m	Total \$m
Cash and cash equivalents	265.8	1.3	5.6	2.4	15.6	290.7
Accrued interest receivable	5.7	—	0.1	—	0.1	5.9
Investments	1,675.5	(0.4)	(0.6)	—	(0.3)	1,674.2
Inwards premiums receivable from insureds and cedants	134.6	2.8	23.2	6.6	15.6	182.8
Reinsurance assets	208.0	1.5	11.8	1.7	0.9	223.9
Other receivables	88.0	(6.0)	(0.1)	—	1.2	83.1
Property, plant and equipment	0.4	—	—	—	—	0.4
Right-of-use assets	1.8	—	—	—	—	1.8
Deferred acquisition costs	45.2	1.8	11.5	1.3	1.6	61.4
<b>Total assets as at 31 December 2021</b>	<b>2,425.0</b>	<b>1.0</b>	<b>51.5</b>	<b>12.0</b>	<b>34.7</b>	<b>2,524.2</b>

Liabilities	U.S. \$ \$m	Sterling \$m	Euro \$m	Japanese Yen \$m	Other \$m	Total \$m
Losses and loss adjustment expenses	632.6	10.4	43.6	24.8	42.0	753.4
Unearned premiums	197.3	6.1	34.5	13.3	11.0	262.2
Insurance contracts – other payables	1.4	2.2	0.5	—	0.2	4.3
Amounts payable to reinsurers	46.9	(1.3)	8.0	2.2	2.1	57.9
Deferred acquisition costs ceded	2.6	—	0.7	0.1	—	3.4
Other payables	9.3	0.5	—	—	0.1	9.9
Lease liabilities	2.0	—	—	—	—	2.0
<b>Total liabilities as at 31 December 2021</b>	<b>892.1</b>	<b>17.9</b>	<b>87.3</b>	<b>40.4</b>	<b>55.4</b>	<b>1,093.1</b>

## RISK DISCLOSURES CONTINUED

Assets	U.S. \$ \$m	Sterling \$m	Euro \$m	Japanese Yen \$m	Other \$m	Total \$m
Cash and cash equivalents	185.7	0.9	6.2	1.8	8.8	203.4
Accrued interest receivable	6.1	—	0.1	—	—	6.2
Investments	1,434.6	1.0	39.1	—	—	1,474.7
Inwards premiums receivable from insureds and cedants	94.9	(1.5)	16.4	3.3	7.1	120.2
Reinsurance assets	139.8	1.1	6.0	2.3	1.0	150.2
Other reinsurance receivables	4.1	—	—	—	—	4.1
Other receivables	55.3	(4.9)	—	—	0.6	51.0
Property, plant and equipment	0.1	—	—	—	—	0.1
Right-of-use asset	2.8	—	—	—	—	2.8
Deferred acquisition costs	29.5	1.4	8.7	1.1	3.0	43.7
<b>Total assets as at 31 December 2020</b>	<b>1,952.9</b>	<b>(2.0)</b>	<b>76.5</b>	<b>8.5</b>	<b>20.5</b>	<b>2,056.4</b>

Liabilities	U.S. \$ \$m	Sterling \$m	Euro \$m	Japanese Yen \$m	Other \$m	Total \$m
Losses and loss adjustment expenses	400.8	6.6	33.4	21.2	21.4	483.4
Unearned premiums	143.5	3.4	26.5	9.2	13.1	195.7
Insurance contracts – other payables	1.6	0.1	0.3	—	0.2	2.2
Amounts payable to reinsurers	27.4	(0.8)	9.8	2.2	1.9	40.5
Deferred acquisition costs ceded	3.0	—	0.8	0.2	0.2	4.2
Other payables	41.1	0.4	0.1	—	0.1	41.7
Lease liabilities	3.0	—	—	—	—	3.0
<b>Total liabilities as at 31 December 2020</b>	<b>620.4</b>	<b>9.7</b>	<b>70.9</b>	<b>32.8</b>	<b>36.9</b>	<b>770.7</b>

The impact on net income of a proportional foreign exchange movement of 10% up and 10.0% down against the U.S. dollar at the year end spot rates would be an increase or decrease of \$5.8 million (31 December 2020 – \$1.2 million).

## RISK DISCLOSURES CONTINUED

### C. LIQUIDITY RISK

Liquidity risk is the risk that cash may not be available to pay obligations when they are due without incurring an unreasonable cost. The Company's main exposures to liquidity risk are with respect to its insurance and investment activities. The Company is exposed if proceeds from financial assets are not sufficient to fund obligations arising from its insurance contracts. The Company can be exposed to daily calls on its available investment assets, principally to settle insurance claims and to fund trust accounts following a large catastrophe loss.

Exposures in relation to insurance activities are as follows:

- large catastrophic events, or multiple medium-sized events in quick succession, resulting in a requirement to pay a large value of claims within a relatively short time frame or fund trust accounts;
- failure of insureds or cedants to meet their contractual obligations with respect to the payment of premiums in a timely manner; and
- failure of reinsurers to meet their contractual obligations with respect to the payment of claims in a timely manner.

Exposures in relation to investment activities are as follows:

- adverse market movements and/or a duration mismatch to obligations, resulting in investments being disposed of at a significant realised loss; and
- an inability to liquidate investments due to market conditions.

The maturity dates of the Company's fixed maturity portfolio are as follows:

As at 31 December 2021	Core \$m	Core plus \$m	Surplus \$m	Total \$m
Less than one year	34.0	141.8	18.5	194.3
Between one and two years	83.4	249.7	25.4	358.5
Between two and three years	32.7	127.9	38.6	199.2
Between three and four years	20.6	88.7	40.8	150.1
Between four and five years	7.9	32.3	55.1	95.3
Over five years	5.8	24.5	173.3	203.6
Asset backed and mortgage backed securities	10.8	32.7	190.7	234.2
<b>Total fixed maturity securities</b>	<b>195.2</b>	<b>697.6</b>	<b>542.4</b>	<b>1,435.2</b>

As at 31 December 2020	Core \$m	Core plus \$m	Surplus \$m	Total \$m
Less than one year	33.5	151.0	10.6	195.1
Between one and two years	37.6	140.1	11.4	189.1
Between two and three years	49.8	116.5	26.9	193.2
Between three and four years	16.0	67.3	39.9	123.2
Between four and five years	17.1	52.2	92.0	161.3
Over five years	5.5	27.6	136.1	169.2
Asset backed and mortgage backed securities	4.6	80.6	181.0	266.2
<b>Total fixed maturity securities</b>	<b>164.1</b>	<b>635.3</b>	<b>497.9</b>	<b>1,297.3</b>

## RISK DISCLOSURES CONTINUED

The maturity profile of the insurance contracts and financial liabilities of the Company is as follows:

As at 31 December 2021	Years until liability becomes due – undiscounted values				Total \$m
	Less than one \$m	One to three \$m	Three to five \$m	Over five \$m	
Losses and loss adjustment expenses	326.3	272.5	97.1	57.5	753.4
Insurance contracts – other payables	4.0	0.3	—	—	4.3
Amounts payable to reinsurers	57.9	—	—	—	57.9
Other payables	9.9	—	—	—	9.9
Lease liabilities	1.1	1.1	—	—	2.2
<b>Total</b>	<b>399.2</b>	<b>273.9</b>	<b>97.1</b>	<b>57.5</b>	<b>827.7</b>

As at 31 December 2020	Years until liability becomes due – undiscounted values				Total \$m
	Less than one \$m	One to three \$m	Three to five \$m	Over five \$m	
Losses and loss adjustment expenses	211.9	183.5	53.7	34.3	483.4
Insurance contracts – other payables	2.2	—	—	—	2.2
Amounts payable to reinsurers	40.5	—	—	—	40.5
Other payables	41.7	—	—	—	41.7
Lease liabilities	1.1	2.2	—	—	3.3
<b>Total</b>	<b>297.4</b>	<b>185.7</b>	<b>53.7</b>	<b>34.3</b>	<b>571.1</b>

Actual maturities of the above may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. While the estimation of the ultimate liability for losses and loss adjustment expenses is complex and incorporates a significant amount of judgement, the timing of payment of losses and loss adjustment expenses is also uncertain and cannot be predicted as simply as for other financial liabilities. Actuarial and statistical techniques, past experience and management's judgement have been used to determine a likely settlement pattern.

The Company manages its liquidity risks via its investment strategy to hold high quality, liquid securities, sufficient to meet its insurance liabilities and other near-term liquidity requirements. The creation of the core and core plus portfolios with their subset of guidelines aims to ensure funds are readily available to meet potential insurance liabilities in an extreme event plus other near-term liquidity requirements. In addition, the Company has established asset allocation and maturity parameters within the investment guidelines such that the majority of the investments are in high quality assets which could be converted into cash promptly and at minimal expense. The Company monitors market changes and outlook and reallocates assets as it deems necessary.

As at 31 December 2021, the Company considers that it has more than adequate liquidity to pay its obligations as they fall due.

## RISK DISCLOSURES CONTINUED

### D. CREDIT RISK

Credit risk is the risk that a counterparty may fail to pay, or repay, a debt or obligation. The Company is exposed to credit risk on its fixed maturity investment portfolio and derivative instruments, its inwards premiums receivable from insureds and cedants, and on any amounts recoverable from reinsurers.

Credit risk on the fixed maturity portfolio is mitigated through the Company's policy to invest in instruments of high credit quality issuers and to limit the amounts of credit exposure with respect to particular ratings categories and any one issuer. Securities rated below an S&P or equivalent rating of BBB-/Baa3 may comprise no more than 15.0% of shareholders' equity. In addition, no one issuer, with the exception of U.S. government and agency securities, other G10 government guaranteed securities (excluding Italy) and Australian sovereign debt, should exceed 5.0% of shareholders' equity. The Company is therefore not exposed to any significant credit concentration risk on its investment portfolio, except for fixed maturity securities issued by the U.S. government and government agencies and other highly-rated governments.

Credit risk on exchange-traded derivative instruments is mitigated by the use of clearing houses to reduce counterparty credit risk, requiring the posting of margins and settling of unrealised gains and losses daily. Credit risk on OTC derivatives is mitigated by monitoring the creditworthiness of the counterparties and by requiring collateral amounts exceeding predetermined thresholds to be posted for positions which have accrued gains.

Credit risk on inwards premiums receivable from insureds and cedants is managed by conducting business with reputable broking organisations, with whom the Company has established relationships, and by rigorous cash collection procedures. The Company also has a broker approval process in place. Binding authorities are subject to standard market controls including credit control. Credit risk from reinsurance recoverables is primarily managed by the review and approval of reinsurer security.

The table below presents an analysis of the Company's major exposures to counterparty credit risk, based on their rating. The table includes amounts due from policyholders and unsettled investment trades. The quality of these receivables is not graded but, based on management's historical experience, there is limited default risk associated with these amounts.

As at 31 December 2021	Cash and fixed maturity securities \$m	Inwards premiums receivable and other receivables \$m	Reinsurance recoveries \$m
AAA	218.1	—	—
AA+, AA, AA-	633.4	—	2.8
A+, A, A-	538.6	—	157.3
BBB+, BBB, BBB-	216.6	—	—
Other <sup>(1)</sup>	119.2	274.3	37.3
<b>Total</b>	<b>1,725.9</b>	<b>274.3</b>	<b>197.4</b>

(1) Reinsurance recoveries classified as "other" are fully collateralised.

As at 31 December 2020	Cash and fixed maturity securities \$m	Inwards premiums receivable and other receivables \$m	Reinsurance recoveries \$m
AAA	323.7	—	—
AA+, AA, AA-	493.2	—	—
A+, A, A-	363.0	4.1	52.9
BBB+, BBB, BBB-	214.2	—	—
Other <sup>(1)</sup>	106.6	171.2	76.1
<b>Total</b>	<b>1,500.7</b>	<b>175.3</b>	<b>129.0</b>

(1) Reinsurance recoveries classified as "other" are fully collateralised.

While interest rates are at all-time lows and expected to remain low, credit spreads will remain volatile in the near-term. As at 31 December 2021, the average credit quality of the fixed maturity portfolio was A+ (31 December 2020 – A+).

## RISK DISCLOSURES CONTINUED

The following table shows inwards premiums receivable that are past due but not impaired:

As at 31 December	2021 \$m	2020 \$m
Less than 90 days past due	11.4	5.0
Between 91 and 180 days past due	3.3	0.5
Over 180 days past due	1.8	1.9
<b>Total</b>	<b>16.5</b>	<b>7.4</b>

Provisions of \$0.7 million (31 December 2020 – \$0.3 million) have been made for impaired or irrecoverable balances and \$0.4 million (2020 – \$0.1 million) was charged to the statement of comprehensive (loss) income in respect of the provision for bad debts.

### E. OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, personnel, systems or external events. The Company has identified and evaluated its key operational risks and these are incorporated in the risk registers and modelled within BLAST. The Company has also established, and monitors compliance with, internal operational risk tolerances. The RRC reviews operational risk on at least an annual basis and operational risk is covered in the CRO's quarterly ORSA report to the Board.

In order to manage operational risks, the Company has implemented a robust governance framework. Policies and procedures are documented and identify the key risks and controls within processes. Key risk indicators have been established and are monitored on a regular basis and a formal loss events and near-miss reporting process has been implemented. The Company's internal audit function provides independent feedback with regard to the accuracy and completeness of key risks and controls, and independently verifies the effective operation of these through substantive testing. All higher risk areas are subject to an annual audit while compliance with tax operating guidelines is reviewed quarterly. Frequency of consideration of audit for all other areas varies from quarterly at the most frequent to a minimum of once every four years, on a rotational basis.

As in 2020, the majority of the Company's employees spent much of 2021 working from home, again with no noticeable adverse impact on the Company's operating effectiveness. As of September 2021, most employees had returned to the office. The operational cyber risk that comes with employees working from home is managed through enhanced monitoring of network activity, targeted staff training, a quarterly risk and control affirmation process, annual testing of business continuity plans and disaster recovery plans and our cyber security incident response plan.

### F. STRATEGIC RISK

The Company has identified several strategic risks. These include:

- the risks that either the poor execution of the business plan or an inappropriate business plan in itself results in a strategy that fails to adequately reflect the trading environment, resulting in an inability to optimise performance, including reputational risk;
- the risks of the failure to maintain adequate capital, accessing capital at an inflated cost or the inability to access capital. This includes unanticipated changes in vendor, regulatory and/or rating agency models that could result in an increase in capital requirements or a change in the type of capital required;
- the risks of succession planning, staff retention and key man risks; and
- the risks of organisational stretch as the Company grows in terms of volume of business written and number of employees as well as from transformation programmes to ensure the Company has appropriate systems and infrastructure and data in place to support the business.

### I. BUSINESS PLAN RISK

The Company addresses the risks associated with the planning and execution of the business plan through a combination of the following:

- an iterative annual forward-looking business planning process with cross departmental involvement;
- evaluation of and approval of the annual business plan by the Board of Directors;
- regular monitoring of actual versus planned results;
- periodic review and re-forecasting as market conditions change;
- responding to current events such as the COVID-19 pandemic and the impact on the business; and
- evaluation of climate change and the potential short, medium and long-term implications/considerations for the business.

The forward-looking business planning process covers a three-year period from 2022 to 2024 and applies a number of sensitivity, stress and scenario tests. These tests include consideration of COVID-19 pandemic and climate change risks. The sensitivity and stress testing identified that even under the more extreme stress scenarios the Company had more than adequate liquidity and solvency headroom.

## RISK DISCLOSURES CONTINUED

### II. CAPITAL MANAGEMENT RISK

The total capital of the Company as at 31 December 2021 is \$1,431.1 million (31 December 2020 – \$1,285.7 million). The Company's capital requirements vary with the insurance cycle.

Risks associated with the effectiveness of the Company's capital management, are mitigated as follows:

- regular monitoring of current and prospective regulatory and rating agency capital requirements;
- oversight of capital requirements by the Board of Directors;
- ability to purchase sufficient, cost-effective reinsurance;
- maintaining contact with vendors, regulators and rating agencies in order to stay abreast of upcoming developments; and
- participation in industry groups such as the International Underwriters Association and the Association of Bermuda Insurers and Reinsurers.

The Company reviews the level and composition of capital on an ongoing basis with a view to:

- maintaining sufficient capital for underwriting opportunities and to meet obligations to policyholders;
- maximising the risk-adjusted return to shareholders within predetermined risk tolerances;
- maintaining adequate financial strength ratings; and
- meeting internal, rating agency and regulatory capital requirements.

Capital is increased or returned as appropriate. The retention of earnings generated leads to an increase in capital. All capital actions require approval by the Board of Directors.

Internal methods have been developed to review the profitability of classes of business and their estimated capital requirements plus the capital requirements of the combination of a wide range of other risk categories. These approaches are used by management in decision making.

The Group's aim is to maximise risk-adjusted returns for LHL's shareholders across the long-term. The return is generated within a broad framework of risk parameters. The return is measured by management in terms of the change in FCBVS. This aim is a long-term goal, acknowledging that management expects both higher and lower results in the shorter term. The cyclicality and volatility of the insurance market is expected to be the largest driver of this pattern. Management monitors these peaks and troughs by adjusting the Company's portfolio to make the most effective use of available capital and seeking to maximise the risk-adjusted return.

The only source of capital used by the Company is equity shareholder's funds. The Company's ability to pay dividends and make capital distributions to LHL is subject to the legal and regulatory restrictions of the jurisdictions in which they operate.

The Company is regulated by the BMA and is required to monitor their enhanced capital requirement under the BMA's regulatory framework, which has been assessed as equivalent to the Solvency II regime. The Company's capital requirements are calculated using the BSCR standard formula model. For the years ended 31 December 2021 and 2020 the Company was more than adequately capitalised under the BMA regulatory regime.

### III. RETENTION RISK

Risks associated with succession planning, staff retention and key man risks are mitigated through a combination of resource planning processes and controls, including:

- the identification of key personnel with appropriate succession plans;
- the identification of key team profit generators and function holders with targeted retention packages;
- documented recruitment procedures, position descriptions and employment contracts;
- resource monitoring and the provision of appropriate compensation, including equity based compensation which vests over a defined time horizon; and
- training schemes.



## NOTES TO THE ACCOUNTS

### 1. GENERAL INFORMATION

The Company is a provider of global specialty insurance and reinsurance products. The Company was incorporated under the laws of Bermuda on 28 October 2005 and is authorised by the BMA as a Class 4 general insurer under The Insurance Act 1978 and related Regulations ('the Act'). The registered office of the Company is Power House, 7 Par-La-Ville Road, Hamilton HM 11, Bermuda. The Company is a wholly owned subsidiary of LHL, a company listed on the LSE, with a secondary listing on the BSX. The Company's financial statements are prepared in accordance with the Bermuda Companies Act 1981.

### 2. SEGMENTAL REPORTING

Management and the Board of Directors review the Company's business primarily by its five principal segments: property and casualty reinsurance, property and casualty insurance, aviation, energy, and marine. These segments are therefore deemed to be the Company's operating segments for the purposes of segmental reporting. Further sub-classes of business are underwritten within each operating segment. The nature of these individual sub-classes is discussed further in the risk disclosures section on pages 15 to 17. Operating segment performance is measured by the net underwriting profit or loss and the combined ratio.

All amounts reported are transactions with external parties and associates. There are no significant inter-segmental transactions and there are no significant insurance or reinsurance contracts that insure or reinsure risks in Bermuda, the Company's country of domicile.

The Company's operating segments for the purpose of segmental reporting have been revised in the current year. The revenue and expenses previously reported in the property segment are now reported within the property and casualty reinsurance and the property and casualty insurance segments. The aviation, energy and marine segments remain unchanged. Comparative figures for the year ended 31 December 2020 have been re-presented in conformity with the current year view.

NOTES TO THE ACCOUNTS CONTINUED

2. SEGMENTAL REPORTING CONTINUED

REVENUE AND EXPENSE BY OPERATING SEGMENT

For the year ended 31 December 2021	Property and casualty reinsurance \$m	Property and casualty insurance \$m	Aviation \$m	Energy \$m	Marine \$m	Total \$m
<b>Gross premiums written by geographic area</b>						
U.S. and Canada	217.4	28.0	1.6	16.1	0.1	263.2
Worldwide – multi territory	143.8	(0.3)	21.7	48.3	19.8	233.3
Europe	29.9	16.2	—	4.1	—	50.2
Rest of world	40.9	9.2	—	9.2	—	59.3
<b>Total gross premiums written</b>	<b>432.0</b>	<b>53.1</b>	<b>23.3</b>	<b>77.7</b>	<b>19.9</b>	<b>606.0</b>
Outwards reinsurance premiums	(141.5)	(6.2)	—	(1.4)	(1.6)	(150.7)
Change in unearned premiums	(68.1)	(0.8)	0.4	(1.5)	3.5	(66.5)
Change in unearned premiums on premiums ceded	(2.4)	(0.6)	(0.1)	—	—	(3.1)
<b>Net premiums earned</b>	<b>220.0</b>	<b>45.5</b>	<b>23.6</b>	<b>74.8</b>	<b>21.8</b>	<b>385.7</b>
Insurance losses and loss adjustment expenses	(335.9)	(50.9)	(4.7)	(24.5)	(10.2)	(426.2)
Insurance losses and loss adjustment expenses recoverable	127.2	0.1	—	—	—	127.3
Insurance acquisition expenses	(50.6)	(18.0)	(11.8)	(32.0)	(12.1)	(124.5)
Insurance acquisition expenses ceded	8.6	0.9	—	—	—	9.5
<b>Net underwriting (loss) profit</b>	<b>(30.7)</b>	<b>(22.4)</b>	<b>7.1</b>	<b>18.3</b>	<b>(0.5)</b>	<b>(28.2)</b>
Net unallocated income and expenses						18.6
<b>Loss for the year</b>						<b>(9.6)</b>
Net loss ratio	94.9%	111.6%	19.9%	32.8%	46.8%	77.5%
Net acquisition cost ratio	19.1%	37.6%	50.0%	42.8%	55.5%	29.8%
Expense ratio	—	—	—	—	—	6.4%
<b>Combined ratio</b>	<b>114.0%</b>	<b>149.2%</b>	<b>69.9%</b>	<b>75.6%</b>	<b>102.3%</b>	<b>113.7%</b>

## NOTES TO THE ACCOUNTS CONTINUED

### 2. SEGMENTAL REPORTING CONTINUED

#### REVENUE AND EXPENSE BY OPERATING SEGMENT

For the year ended 31 December 2020	Property and casualty reinsurance \$m	Property and casualty insurance \$m	Aviation \$m	Energy \$m	Marine \$m	Total \$m
<b>Gross premiums written by geographic area</b>						
U.S. and Canada	128.0	10.0	—	8.6	—	146.6
Worldwide – multi territory	23.4	1.8	24.2	37.5	29.2	116.1
Europe	14.7	10.0	—	4.2	—	28.9
Rest of world	31.5	7.1	—	7.1	—	45.7
<b>Total gross premiums written</b>	<b>197.6</b>	<b>28.9</b>	<b>24.2</b>	<b>57.4</b>	<b>29.2</b>	<b>337.3</b>
Outwards reinsurance premiums	(77.5)	(5.2)	(0.1)	—	(2.9)	(85.7)
Change in unearned premiums	(17.9)	10.4	0.2	(1.6)	(4.3)	(13.2)
Change in unearned premiums on premiums ceded	(0.4)	(0.5)	(0.1)	(0.8)	—	(1.8)
<b>Net premiums earned</b>	<b>101.8</b>	<b>33.6</b>	<b>24.2</b>	<b>55.0</b>	<b>22.0</b>	<b>236.6</b>
Insurance losses and loss adjustment expenses	(40.8)	(7.1)	(10.8)	(39.1)	(24.6)	(122.4)
Insurance losses and loss adjustment expenses recoverable	(11.8)	0.1	0.3	0.2	—	(11.2)
Insurance acquisition expenses	(23.0)	(14.4)	(11.1)	(30.2)	(10.8)	(89.5)
Insurance acquisition expenses ceded	5.5	0.8	0.1	—	0.1	6.5
<b>Net underwriting profit (loss)</b>	<b>31.7</b>	<b>13.0</b>	<b>2.7</b>	<b>(14.1)</b>	<b>(13.3)</b>	<b>20.0</b>
Net unallocated income and expenses						13.0
<b>Profit for the year</b>						<b>33.0</b>
Net loss ratio	51.7%	20.8%	43.4%	70.7%	111.8%	56.5%
Net acquisition cost ratio	17.2%	40.5%	45.5%	54.9%	48.6%	35.1%
Expense ratio	—	—	—	—	—	11.0%
<b>Combined ratio</b>	<b>68.9%</b>	<b>61.3%</b>	<b>88.9%</b>	<b>125.6%</b>	<b>160.4%</b>	<b>102.6%</b>

## NOTES TO THE ACCOUNTS CONTINUED

### 3. INVESTMENT RETURN

The total investment return for the Company is as follows:

	Net investment income and net other investment income <sup>1</sup> \$m	Net realised gains (losses) and impairments \$m	Net change in unrealised gains/losses on AFS <sup>2</sup> \$m	Total investment return excluding foreign exchange \$m	Net foreign exchange (losses)/gains \$m	Total investment return including foreign exchange \$m
<b>For the year ended 31 December 2021</b>						
Fixed maturity securities – AFS	18.0	1.6	(23.4)	(3.8)	(3.2)	(7.0)
Fixed maturity securities – at FVTPL	2.8	(0.1)	—	2.7	—	2.7
Index linked securities – at FVTPL	0.5	—	—	0.5	—	0.5
Hedge funds – at FVTPL	(0.6)	3.7	—	3.1	—	3.1
Private investment funds – at FVTPL	2.3	—	—	2.3	—	2.3
Other investments	(0.1)	(0.2)	—	(0.3)	0.8	0.5
Cash and cash equivalents	—	—	—	—	1.8	1.8
<b>Total investment return</b>	<b>22.9</b>	<b>5.0</b>	<b>(23.4)</b>	<b>4.5</b>	<b>(0.6)</b>	<b>3.9</b>

(1) Net unrealised gains (losses) on our FVTPL investments are included within net investment income and net other investment income.

(2) In 2023 when we apply IFRS 9 the net change in unrealised gains /losses on AFS will be classified within net investment income and net other investment income.

	Net investment income and net other investment income <sup>1</sup> \$m	Net realised gains (losses) and impairments \$m	Net change in unrealised gains/losses on AFS <sup>2</sup> \$m	Total investment return excluding foreign exchange \$m	Net foreign exchange (losses) gains \$m	Total investment return including foreign exchange \$m
<b>For the year ended 31 December 2020</b>						
Fixed maturity securities – AFS	19.6	1.0	16.0	36.6	6.3	42.9
Fixed maturity securities – at FVTPL	(0.3)	3.2	—	2.9	—	2.9
Hedge funds – at FVTPL	(1.0)	5.7	—	4.7	—	4.7
Private investment funds – at FVTPL	7.3	—	—	7.3	—	7.3
Other investments	0.3	1.9	—	2.2	(0.1)	2.1
Cash and cash equivalents	1.3	—	—	1.3	(2.2)	(0.9)
<b>Total investment return</b>	<b>27.2</b>	<b>11.8</b>	<b>16.0</b>	<b>55.0</b>	<b>4.0</b>	<b>59.0</b>

(1) Net unrealised gains (losses) on our FVTPL investments are included within net investment income and net other investment income.

(2) In 2023 when we apply IFRS 9 the net change in unrealised gains /losses on AFS will be classified within net investment income and net other investment income.

Net investment income includes \$27.2 million (2020 – \$28.0 million) of interest income on our AFS investment portfolio and cash and cash equivalents. Net realised gains (losses) and impairments includes impairment losses of \$nil (2020 – \$0.7 million) recognised on fixed maturity securities held by the Company.

Refer to pages 23 to 24 in the risk disclosures section for the fair values of the Company's derivative instruments. Realised gains and losses on futures and options contracts are included in net realised gains (losses) and impairments.

Included in net investment income and net other investment income is \$4.4 million (2020 – \$3.8 million) of investment management, accounting and custodian fees.

### 4. NET INSURANCE ACQUISITION EXPENSES

	2021 \$m	2020 \$m
<b>For the year ended 31 December</b>		
Insurance acquisition expenses	142.2	84.7
Changes in deferred insurance acquisition expenses	(17.7)	4.8
Insurance acquisition expenses ceded	(8.7)	(6.5)
Changes in deferred insurance acquisition expenses ceded	(0.8)	—
<b>Total net insurance acquisition expenses</b>	<b>115.0</b>	<b>83.0</b>

## NOTES TO THE ACCOUNTS CONTINUED

### 5. RESULTS OF OPERATING ACTIVITIES

Results of operating activities are stated after charging the following amounts:

For the year ended 31 December	2021 \$m	2020 \$m
Depreciation on owned assets	0.2	0.1
Auditors' remuneration	0.6	0.6
<b>Total</b>	<b>0.8</b>	<b>0.7</b>

During the year ended 31 December 2021 and 31 December 2020, no non-audit services were provided by KPMG Audit Limited.

### 6. EMPLOYEE BENEFITS

For the year ended 31 December	2021 \$m	2020 \$m
Wages and salaries	10.5	9.3
Pension costs	1.1	0.9
Bonus and other benefits	3.6	6.5
<b>Total cash compensation</b>	<b>15.2</b>	<b>16.7</b>
RSS – performance	0.6	0.9
RSS – ordinary	1.4	1.2
RSS – bonus deferral	0.4	0.2
<b>Total equity based compensation</b>	<b>2.4</b>	<b>2.3</b>
<b>Total employee benefits</b>	<b>17.6</b>	<b>19.0</b>

### 7. TAX CHARGE

#### BERMUDA

The Company has received an undertaking from the Bermuda government exempting them from all Bermuda local income, withholding and capital gains taxes until 31 March 2035. At the present time no such taxes are levied in Bermuda.

#### UNITED STATES

The Company does not consider itself to be engaged in trade or business in the U.S. and, accordingly, does not expect to be subject to U.S. taxation on its income and capital gains.

### 8. CASH AND CASH EQUIVALENTS

As at 31 December	2021 \$m	2020 \$m
Cash at bank and in hand	159.5	83.0
Cash equivalents	131.2	120.4
<b>Total cash and cash equivalents</b>	<b>290.7</b>	<b>203.4</b>

The carrying amount of these assets approximates their fair value. Refer to note 13 for the cash and cash equivalent balances on deposit as collateral.

NOTES TO THE ACCOUNTS CONTINUED

9. INVESTMENTS

As at 31 December 2021	Cost or amortised cost \$m	Unrealised gains \$m	Unrealised losses \$m	Fair value <sup>1</sup> \$m
<b>Fixed maturity securities – AFS</b>				
– Short-term investments	27.0	—	—	27.0
– U.S. treasuries	438.6	0.5	(2.7)	436.4
– Other government bonds	47.8	0.1	(0.7)	47.2
– U.S. municipal bonds	19.8	0.3	(0.1)	20.0
– U.S. government agency debt	49.9	1.1	(0.1)	50.9
– Asset backed securities	103.6	0.3	(1.0)	102.9
– U.S. government agency mortgage backed securities	78.0	0.9	(1.0)	77.9
– Non-agency mortgage backed securities	33.1	0.3	(0.2)	33.2
– Agency commercial mortgage backed securities	0.1	—	—	0.1
– Non-agency commercial mortgage backed securities	20.2	—	(0.1)	20.1
– Bank loans	110.1	0.7	(0.6)	110.2
– Corporate bonds	480.8	6.2	(2.7)	484.3
<b>Total fixed maturity securities – AFS</b>	<b>1,409.0</b>	<b>10.4</b>	<b>(9.2)</b>	<b>1,410.2</b>
Fixed maturity securities – at FVTPL	19.5	5.5	—	25.0
Private investment funds – at FVTPL	106.0	1.1	(1.4)	105.7
Hedge funds – at FVTPL	93.3	14.8	(5.2)	102.9
Index linked securities – at FVTPL	30.0	0.5	—	30.5
Other investments	0.3	0.1	(0.5)	(0.1)
<b>Total investments</b>	<b>1,658.1</b>	<b>32.4</b>	<b>(16.3)</b>	<b>1,674.2</b>

(1) In 2023 when we apply when IFRS 9, Financial Instruments: Classification and Measurement is implemented, all investments held above will be classified as at FVTPL (mandatory), with no resulting changes in the estimated fair value.

As at 31 December 2020	Cost or amortised cost \$m	Unrealised gains \$m	Unrealised losses \$m	Fair value <sup>1</sup> \$m
<b>Fixed maturity securities – AFS</b>				
– Short-term investments	72.2	—	—	72.2
– U.S. treasuries	196.8	1.9	(0.1)	198.6
– Other government bonds	46.4	0.6	—	47.0
– U.S. municipal bonds	10.0	0.5	—	10.5
– U.S. government agency debt	93.8	3.3	—	97.1
– Asset backed securities	119.3	3.9	(0.5)	122.7
– U.S. government agency mortgage backed securities	117.8	2.6	(0.1)	120.3
– Non-agency mortgage backed securities	16.5	0.6	—	17.1
– Agency commercial mortgage backed securities	0.4	—	(0.1)	0.3
– Non-agency commercial mortgage backed securities	5.6	0.2	—	5.8
– Bank loans	110.6	1.0	(1.1)	110.5
– Corporate bonds	449.3	16.7	(0.1)	465.9
<b>Total fixed maturities - AFS</b>	<b>1,238.7</b>	<b>31.3</b>	<b>(2.0)</b>	<b>1,268.0</b>
Fixed maturity securities – at FVTPL	25.7	3.6	—	29.3
Private investment funds – at FVTPL	91.7	5.6	(1.2)	96.1
Hedge funds – at FVTPL	72.7	13.4	(4.1)	82.0
Other investments	—	—	(0.7)	(0.7)
<b>Total investments</b>	<b>1,428.8</b>	<b>53.9</b>	<b>(8.0)</b>	<b>1,474.7</b>

(1) In 2023 when we apply when IFRS 9, Financial Instruments: Classification and Measurement is implemented, all investments held above will be classified as at FVTPL (mandatory), with no resulting changes in the estimated fair value.

## NOTES TO THE ACCOUNTS CONTINUED

### 9. INVESTMENTS CONTINUED

Accumulated other comprehensive income in relation to AFS fixed maturity securities is as follows:

As at 31 December	2021 \$m	2020 \$m
Unrealised gains	10.4	31.3
Unrealised losses	(9.2)	(2.0)
Net unrealised foreign exchange losses (gains) on fixed maturity securities – AFS	0.9	(3.8)
<b>Accumulated other comprehensive income</b>	<b>2.1</b>	<b>25.5</b>

The Company determines the estimated fair value of each individual security utilising the highest-level inputs available. Prices for the Company's investment portfolio are provided via a third-party investment accounting firm whose pricing processes and the controls thereon are subject to an annual audit on both the operation and the effectiveness of those controls. Various recognised reputable pricing sources are used including pricing vendors and broker-dealers. The pricing sources use bid prices where available, otherwise indicative prices are quoted based on observable market trade data. The prices provided are compared to the investment managers' pricing.

The Company has not made any adjustments to any pricing provided by independent pricing services or its third-party investment managers for either year ending 31 December.

The fair value of securities in the Company's investment portfolio is estimated using the following techniques:

#### LEVEL (I)

Level (i) investments are securities with quoted prices in active markets. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

#### LEVEL (II)

Level (ii) investments are securities with quoted prices in active markets for similar assets or liabilities or securities valued using other valuation techniques for which all significant inputs are based on observable market data. Instruments included in Level (ii) are valued via independent external sources using directly observable inputs to models or other valuation methods. The valuation methods used are typically industry accepted standards and include broker-dealer quotes and pricing models including present values and future cash flows with inputs such as yield curves, interest rates, prepayment speeds and default rates.

#### LEVEL (III)

Level (iii) investments are securities for which valuation techniques are not based on observable market data and require significant management judgement. The Company determines securities classified as Level (iii) to include hedge funds and private investment funds.

The estimated fair value of the Company's private investment funds are determined using statements received from each fund's investment managers on either a monthly or quarterly in arrears basis. In addition these valuations will be compared with benchmarks or other indices to assess the reasonableness of the estimated fair value of each fund. Given the Company's knowledge of the underlying investments and the size of the Company's investment therein, we would not anticipate any material variance between estimated valuations and the final NAV's reported by the investment managers.

The estimated fair values of the Company's hedge funds are determined using a combination of the most recent NAVs provided by each fund's independent administrator and the estimated performance provided by each hedge fund manager. Independent administrators provide monthly reported NAVs with up to a one-month delay in valuation. The most recent NAV available for each hedge fund is adjusted for the estimated performance, as provided by the fund manager, between the NAV date and the reporting date. Historically estimated fair values incorporating these performance estimates have not been significantly different from subsequent NAVs. Given the Company's knowledge of the underlying investments and the size of the Company's investment therein, we would not anticipate any material variance between estimated valuations and the final NAVs reported by the administrators.

The Company determines whether transfers have occurred between levels of the fair value hierarchy by re-assessing the categorisation at the end of each reporting period. Transfers between Level (i) to (ii) securities amounted to \$107.6 million and transfers from Level (ii) to (i) securities amounted to \$35.7 million during the year ended 31 December 2021.

## NOTES TO THE ACCOUNTS CONTINUED

### 9. INVESTMENTS CONTINUED

The fair value hierarchy of the Company's investment holdings is as follows:

As at 31 December 2021	Level (i) \$m	Level (ii) \$m	Level (iii) \$m	Total \$m
<b>Fixed maturity securities – AFS</b>				
– Short-term investments	24.7	2.3	—	27.0
– U.S. treasuries	436.4	—	—	436.4
– Other government bonds	19.9	27.3	—	47.2
– U.S. municipal bonds	—	20.0	—	20.0
– U.S. government agency debt	30.2	20.7	—	50.9
– Asset backed securities	—	102.9	—	102.9
– U.S. government agency mortgage backed securities	—	77.9	—	77.9
– Non-agency mortgage backed securities	—	33.2	—	33.2
– Agency commercial mortgage backed securities	—	0.1	—	0.1
– Non-agency commercial mortgage backed securities	—	20.1	—	20.1
– Bank loans	5.0	105.2	—	110.2
– Corporate bonds	135.4	348.9	—	484.3
<b>Total fixed maturity securities – AFS</b>	<b>651.6</b>	<b>758.6</b>	<b>—</b>	<b>1,410.2</b>
Fixed maturity securities – at FVTPL	—	25.0	—	25.0
Private investment funds – at FVTPL	—	—	105.7	105.7
Hedge funds – at FVTPL	—	—	102.9	102.9
Index linked securities – at FVTPL	—	30.5	—	30.5
Other investments	—	(0.1)	—	(0.1)
<b>Total investments</b>	<b>651.6</b>	<b>814.0</b>	<b>208.6</b>	<b>1,674.2</b>

As at 31 December 2020	Level (i) \$m	Level (ii) \$m	Level (iii) \$m	Total \$m
<b>Fixed maturity securities – AFS</b>				
– Short-term investments	71.2	1.0	—	72.2
– U.S. treasuries	198.6	—	—	198.6
– Other government bonds	13.8	33.2	—	47.0
– U.S. municipal bonds	—	10.5	—	10.5
– U.S. government agency debt	86.5	10.6	—	97.1
– Asset backed securities	—	122.7	—	122.7
– U.S. government agency mortgage backed securities	—	120.3	—	120.3
– Non-agency mortgage backed securities	—	17.1	—	17.1
– Agency commercial mortgage backed securities	—	0.3	—	0.3
– Non-agency commercial mortgage backed securities	—	5.8	—	5.8
– Bank loans	8.3	102.2	—	110.5
– Corporate bonds	186.2	279.7	—	465.9
<b>Total fixed maturities - AFS</b>	<b>564.6</b>	<b>703.4</b>	<b>—</b>	<b>1,268.0</b>
Fixed maturity securities – at FVTPL	—	29.3	—	29.3
Private investment funds – at FVTPL	—	—	96.1	96.1
Hedge funds – at FVTPL	—	—	82.0	82.0
Other investments	—	(0.7)	—	(0.7)
<b>Total investments</b>	<b>564.6</b>	<b>732.0</b>	<b>178.1</b>	<b>1,474.7</b>



## NOTES TO THE ACCOUNTS CONTINUED

### 9. INVESTMENTS CONTINUED

The table below analyses the movements in Level (iii) investments:

	Private investment funds \$m	Hedge funds \$m	Total \$m
<b>As at 31 December 2019</b>	15.5	150.0	165.5
Purchases	82.2	5.8	88.0
Sales	(6.0)	(79.4)	(85.4)
Net realised gains recognised in profit or loss	—	5.7	5.7
Net unrealised gains (losses) in profit or loss	4.4	(0.1)	4.3
<b>As at 31 December 2020</b>	96.1	82.0	178.1
Purchases	17.1	39.9	57.0
Sales	(2.8)	(23.0)	(25.8)
Net realised gains recognised in profit or loss	—	3.7	3.7
Net unrealised (losses) gains in profit or loss	(4.7)	0.3	(4.4)
<b>As at 31 December 2021</b>	105.7	102.9	208.6

### 10. INTERESTS IN UNCONSOLIDATED STRUCTURED ENTITIES

As part of its investment activities, the Company invests in unconsolidated structured entities. As at 31 December 2021, the Company's total interest in unconsolidated structured entities was \$442.8 million (31 December 2020 – \$444.3 million). The Company does not sponsor any of the unconsolidated structured entities.

A summary of the Company's interest in unconsolidated structured entities is as follows:

As at 31 December	2021 \$m	2020 \$m
<b>Fixed maturity securities</b>		
– Asset backed securities	102.9	122.7
– U.S. government agency mortgage backed securities	77.9	120.3
– Non-agency mortgage backed securities	33.2	17.1
– Agency commercial mortgage backed securities	0.1	0.3
– Non-agency commercial mortgage backed securities	20.1	5.8
<b>Total fixed maturity securities</b>	234.2	266.2
<b>Investment funds</b>		
– Private investment funds	105.7	96.1
– Hedge funds	102.9	82.0
<b>Total investment funds</b>	208.6	178.1
<b>Total interest in unconsolidated structured entities</b>	442.8	444.3

The fixed maturity structured entities are created to meet specific investment needs of borrowers and investors which cannot be met from standardised financial instruments available in the capital markets. As such, they provide liquidity to the borrowers in these markets and provide investors with an opportunity to diversify risk away from standard fixed maturity securities. Whilst individual securities may differ in structure, the principles of the instruments are broadly the same and it is appropriate to aggregate the investments into the categories detailed above.

The risk that the Company faces in respect of the investments in structured entities is similar to the risk it faces in respect of other financial investments held on the balance sheet in that fair value is determined by market supply and demand. This is in turn driven by investor evaluation of the credit risk of the structure and changes in the term structure of interest rates which change investors' expectation of the cash flows associated with the instrument and, therefore, its value in the market. Risk management disclosure for these financial instruments and other investments are provided on pages 19 to 27. The total assets of these structured entities are not considered meaningful for the purpose of understanding the related risks and therefore have not been presented.

The maximum exposure to loss in respect of these structured entities would be the carrying value of the instruments that the Company holds as at 31 December 2021 and 31 December 2020. Generally, default rates would have to increase substantially from their current level before the Company would suffer a loss and this assessment is made prior to investing and regularly through the holding period for the security. The Company has not provided any other financial or other support in addition to that described above as at the reporting date, and there is no intention to provide support in relation to any other unconsolidated structured entities in the foreseeable future.

## NOTES TO THE ACCOUNTS CONTINUED

As at 31 December 2021 the Company has a commitment of \$100.0 million (31 December 2020 – \$100.0 million) in respect of two credit facility funds. The Company, via the funds, provides collateral for revolving credit facilities purchased at a discount from financial institutions and is at risk for its portion of any defaults on those revolving credit facilities. The Company's proportionate share of these revolving credit facilities purchased by the funds as at 31 December 2021 is \$39.7 million (31 December 2020 – \$60.3 million), which currently remains unfunded. The maximum exposure to the two credit facility funds is \$100.0 million and as at 31 December 2021 there have been no defaults under these facilities.

### 11. LOSSES AND LOSS ADJUSTMENT EXPENSES

	Losses and loss adjustment expenses \$m	Reinsurance recoveries \$m	Net losses and loss adjustment expenses \$m
<b>As at 31 December 2019</b>	454.3	(144.7)	309.6
Net incurred losses for:			
Prior years	(59.4)	19.8	(39.6)
Current year	181.8	(8.6)	173.2
Exchange adjustments	6.0	(0.4)	5.6
<b>Incurred losses and loss adjustment expenses</b>	<b>128.4</b>	<b>10.8</b>	<b>139.2</b>
Net paid losses for:			
Prior years	86.2	(4.8)	81.4
Current year	13.1	(0.1)	13.0
<b>Paid losses and loss adjustment expenses</b>	<b>99.3</b>	<b>(4.9)</b>	<b>94.4</b>
<b>As at 31 December 2020</b>	<b>483.4</b>	<b>(129.0)</b>	<b>354.4</b>
Net incurred losses for:			
Prior years	(64.5)	4.7	(59.8)
Current year	490.7	(132.0)	358.7
Exchange adjustments	(10.7)	0.5	(10.2)
<b>Incurred losses and loss adjustment expenses</b>	<b>415.5</b>	<b>(126.8)</b>	<b>288.7</b>
Net paid losses for:			
Prior years	78.3	(54.3)	24.0
Current year	67.2	(4.1)	63.1
<b>Paid losses and loss adjustment expenses</b>	<b>145.5</b>	<b>(58.4)</b>	<b>87.1</b>
<b>As at 31 December 2021</b>	<b>753.4</b>	<b>(197.4)</b>	<b>556.0</b>

Further information on the calculation of loss reserves and the risks associated with them is provided in the risk disclosures section from pages 17 and 18. The risks associated with general insurance contracts are complex and do not readily lend themselves to meaningful sensitivity analysis. The impact of an unreported event could lead to a significant increase in the Company's loss reserves. The Company believes that the loss reserves established are adequate, however a 20% increase in estimated losses would lead to a \$150.7 million (31 December 2020 – \$96.7 million) increase in gross loss reserves. During the year the Company refined its reserving methodology to make our margin more explicit as we transition to IFRS 17.

The breakdown of losses and loss adjustment expenses between notified outstanding losses, ACR and IBNR is shown below:

	Losses and loss adjustment expenses \$m	Reinsurance recoveries \$m	Net losses and loss adjustment expenses \$m
Outstanding losses	237.5	(25.7)	211.8
Additional case reserves	43.2	(2.8)	40.4
Losses incurred but not reported	202.7	(100.5)	102.2
<b>As at 31 December 2020</b>	<b>483.4</b>	<b>(129.0)</b>	<b>354.4</b>
Outstanding losses	173.9	(16.1)	157.8
Additional case reserves	174.5	(5.5)	169.0
Losses incurred but not reported	405.0	(175.8)	229.2
<b>As at 31 December 2021</b>	<b>753.4</b>	<b>(197.4)</b>	<b>556.0</b>

The Company's losses and loss adjustment expenses as at 31 December 2021 and 2020 had an estimated duration of approximately two years.

## NOTES TO THE ACCOUNTS CONTINUED

### 11. LOSSES AND LOSS ADJUSTMENT EXPENSES CONTINUED

#### CLAIMS DEVELOPMENT

The development of insurance liabilities is indicative of the Company's ability to estimate the ultimate value of its insurance liabilities. The Company began writing insurance and reinsurance business in December 2005.

Accident year	2011 & prior \$m	2012 \$m	2013 \$m	2014 \$m	2015 \$m	2016 \$m	2017 \$m	2018 \$m	2019 \$m	2020 \$m	2021 \$m	Total \$m
<b>Gross losses</b>												
Estimate of ultimate liability <sup>1</sup>												
At end of accident year	940.7	191.9	153.3	117.8	143.7	112.7	319.9	197.8	120.6	183.2	485.5	
One year later	928.6	230.4	133.9	84.5	99.8	96.5	267.3	209.5	102.3	159.1		
Two years later	927.9	234.5	111.7	73.9	91.0	73.7	245.4	185.4	94.3			
Three years later	924.3	228.4	116.5	70.0	88.1	61.3	226.1	177.0				
Four years later	930.5	218.2	114.8	67.6	83.3	61.3	210.3					
Five years later	940.5	213.8	112.6	67.6	82.8	54.1						
Six years later	939.3	207.8	112.5	68.2	82.6							
Seven years later	914.0	203.0	112.7	68.4								
Eight years later	912.0	202.8	112.7									
Nine years later	918.8	196.9										
Ten years later	918.1											
<b>Current estimate of cumulative liability</b>	<b>918.1</b>	<b>196.9</b>	<b>112.7</b>	<b>68.4</b>	<b>82.6</b>	<b>54.1</b>	<b>210.3</b>	<b>177.0</b>	<b>94.3</b>	<b>159.1</b>	<b>485.5</b>	<b>2,559.0</b>
<b>Paid</b>	<b>(891.0)</b>	<b>(188.5)</b>	<b>(105.9)</b>	<b>(64.9)</b>	<b>(74.8)</b>	<b>(50.4)</b>	<b>(168.3)</b>	<b>(113.4)</b>	<b>(36.3)</b>	<b>(44.9)</b>	<b>(67.2)</b>	<b>(1,805.6)</b>
<b>Total gross liability</b>	<b>27.1</b>	<b>8.4</b>	<b>6.8</b>	<b>3.5</b>	<b>7.8</b>	<b>3.7</b>	<b>42.0</b>	<b>63.6</b>	<b>58.0</b>	<b>114.2</b>	<b>418.3</b>	<b>753.4</b>

(1) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2021.

Accident year	2011 and prior \$m	2012 \$m	2013 \$m	2014 \$m	2015 \$m	2016 \$m	2017 \$m	2018 \$m	2019 \$m	2020 \$m	2021 \$m	Total \$m
<b>Reinsurance recoveries</b>												
Estimate of ultimate recovery <sup>1</sup>												
At end of accident year	21.6	13.4	—	—	0.1	0.7	86.1	50.5	30.4	8.6	131.8	
One year later	38.6	64.9	—	—	0.2	0.7	70.5	85.7	23.0	12.9		
Two years later	41.3	70.0	—	—	0.2	0.4	63.1	79.5	21.1			
Three years later	33.9	69.9	0.1	—	0.3	0.4	57.5	73.5				
Four years later	34.7	69.9	0.1	—	0.3	0.4	56.1					
Five years later	34.9	69.9	0.1	—	0.3	0.4						
Six years later	35.1	70.1	0.1	—	0.2							
Seven years later	34.9	70.1	—	—								
Eight years later	35.0	70.0	—	—								
Nine years later	35.0	70.0	—	—								
Ten years later	35.0	—	—	—								
<b>Current estimate of cumulative recovery</b>	<b>35.0</b>	<b>70.0</b>	<b>—</b>	<b>—</b>	<b>0.2</b>	<b>0.4</b>	<b>56.1</b>	<b>73.5</b>	<b>21.1</b>	<b>12.9</b>	<b>131.8</b>	<b>401.0</b>
<b>Paid</b>	<b>(33.8)</b>	<b>(69.9)</b>	<b>—</b>	<b>—</b>	<b>(0.2)</b>	<b>(0.3)</b>	<b>(54.2)</b>	<b>(36.6)</b>	<b>(3.1)</b>	<b>(1.4)</b>	<b>(4.1)</b>	<b>(203.6)</b>
<b>Total reinsurance recoveries</b>	<b>1.2</b>	<b>0.1</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>0.1</b>	<b>1.9</b>	<b>36.9</b>	<b>18.0</b>	<b>11.5</b>	<b>127.7</b>	<b>197.4</b>

(1) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2021.

## NOTES TO THE ACCOUNTS CONTINUED

### 11. LOSSES AND LOSS ADJUSTMENT EXPENSES CONTINUED

Accident year	2011 and prior \$m	2012 \$m	2013 \$m	2014 \$m	2015 \$m	2016 \$m	2017 \$m	2018 \$m	2019 \$m	2020 \$m	2021 \$m	Total \$m
<b>Net losses</b>												
Estimate of ultimate liability <sup>1</sup>												
At end of accident year	919.1	178.5	153.3	117.8	143.6	112.0	233.8	147.3	90.2	174.6	353.7	
One year later	890.0	165.5	133.9	84.5	99.6	95.8	196.8	123.8	79.3	146.2		
Two years later	886.6	164.5	111.7	73.9	90.8	73.3	182.3	105.9	73.2			
Three years later	890.4	158.5	116.4	70.0	87.8	60.9	168.6	103.5				
Four years later	895.8	148.3	114.7	67.6	83.0	60.9	154.2					
Five years later	905.6	143.9	112.5	67.6	82.5	53.7						
Six years later	904.2	137.7	112.4	68.2	82.4							
Seven years later	879.1	132.9	112.7	68.4								
Eight years later	877.0	132.8	112.7									
Nine years later	883.8	126.9										
Ten years later	883.1											
<b>Current estimate of cumulative liability</b>	<b>883.1</b>	<b>126.9</b>	<b>112.7</b>	<b>68.4</b>	<b>82.4</b>	<b>53.7</b>	<b>154.2</b>	<b>103.5</b>	<b>73.2</b>	<b>146.2</b>	<b>353.7</b>	<b>2,158.0</b>
<b>Paid</b>	<b>(857.2)</b>	<b>(118.6)</b>	<b>(105.9)</b>	<b>(64.9)</b>	<b>(74.6)</b>	<b>(50.1)</b>	<b>(114.1)</b>	<b>(76.8)</b>	<b>(33.2)</b>	<b>(43.5)</b>	<b>(63.1)</b>	<b>(1,602.0)</b>
<b>Total net liability</b>	<b>25.9</b>	<b>8.3</b>	<b>6.8</b>	<b>3.5</b>	<b>7.8</b>	<b>3.6</b>	<b>40.1</b>	<b>26.7</b>	<b>40.0</b>	<b>102.7</b>	<b>290.6</b>	<b>556.0</b>

(1) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2021.

The inherent uncertainty in reserving gives rise to favourable or adverse development on the established reserves. The total favourable development on net losses and loss adjustment expenses, excluding the impact of foreign exchange revaluations, was as follows:

For the year ended 31 December	2021 \$m	2020 \$m
2016 accident year and prior	12.3	(5.0)
2017 accident year	14.3	14.0
2018 accident year	1.7	18.5
2019 accident year	4.6	12.1
2020 accident year	26.9	—
<b>Total favourable development</b>	<b>59.8</b>	<b>39.6</b>

The favourable development in 2021 was primarily driven by general IBNR releases on the 2020 accident year across most lines of business due to a lack of reported claims. 2021 also included favourable development on the 2017 accident year, mainly from reserve releases on natural catastrophe loss events within the property and casualty reinsurance segment, as well as some beneficial claims settlements from earlier accident years. The Company's COVID-19 related losses remained stable during 2021.

In the prior year, the Company benefited from general IBNR releases across most lines of business due to a lack of reported claims. There was also favourable development on the 2017 catastrophe loss events partially offset by a number of late reported losses from the 2019 accident year, reserve deterioration on a couple of marine claims in the 2017 and 2019 accident years, and adverse development on the 2010 New Zealand earthquake.

In February 2021, Winter Storm Uri was a major winter and ice storm that had widespread impacts across the U.S., Northern Mexico and parts of Canada. In July 2021, the European Floods resulted from a series of storms that occurred in several European countries, resulting in widespread flooding in regions of Germany and other neighbouring countries. These events were followed by Hurricane Ida, which made landfall on 29 August 2021, in the U.S. state of Louisiana and continued its path across the U.S. mainland into the north-eastern region, causing significant property and flooding damage. Our net losses in relation to these combined natural catastrophe events, excluding the impacts of reinstatement premiums, were \$149.7 million. Large risk losses for the year amounted to \$55.8 million, and were principally related to the unrest in South Africa in July 2021.

The estimation of the ultimate loss and loss adjustment expense liability is a complex process which incorporates a significant amount of judgement. It is reasonably possible that uncertainties inherent in the reserving process, delays in insureds or ceding companies reporting losses to the Company, together with the potential for unforeseen adverse developments, could lead to a material change in estimated losses and loss adjustment expenses.

There were no other individually significant net loss events for the year ended 31 December 2021 and 2020.

### 12. INSURANCE, REINSURANCE AND OTHER RECEIVABLES

All receivables are considered current other than \$27.0 million (31 December 2020 – \$20.3 million) of inwards premiums receivable related to multi-year contracts. The carrying value approximates fair value due to the short-term nature of the receivables. There are no significant concentrations of credit risk within the Company's receivables.

## NOTES TO THE ACCOUNTS CONTINUED

### 13. FINANCING ARRANGEMENTS

#### LETTERS OF CREDIT

As the Company is a non-admitted insurer or reinsurer throughout the U.S., the terms of certain contracts require them to provide LOCs to policyholders as collateral. The following LOCs have been issued:

As at 31 December	2021 \$m	2020 \$m
Issued to third parties	27.1	27.6

These LOCs are required to be fully collateralised.

The Company has a \$250.0 million syndicated collateralised credit facility with a \$50.0 million loan sub-limit that has been in place since 20 March 2020 and will expire on 20 March 2025. There was no outstanding debt under this facility as at 31 December 2021 and 2020.

The facility is available for the issue of LOCs to ceding companies. The facility is also available for the Company to issue LOCs to LUK to collateralise certain insurance balances.

The terms of the \$250.0 million syndicated collateralised facility include standard default and cross-default provisions that are broadly consistent, which require certain covenants to be adhered to. These include the following:

- an A.M. Best financial strength rating of at least B++;
- a maximum debt to capital ratio of 30.0%, where the LHL junior subordinated loan notes are excluded as debt from this calculation;
- a maximum subordinated unsecured indebtedness of \$350.0 million; and
- a maximum aggregated indebtedness (i) under any syndicate arrangement entered into by Lancashire Syndicates in connection with the underwriting business carried on by all such members of the syndicates and (ii) incurred by CCL 1998, LHL or LICL in the ordinary course of business in connection with coming into line requirements, of \$200.0 million.

On 3 March 2021, LHL and LICL obtained a waiver from its lenders in relation to the limits on debt incurrence under the \$250.0 million syndicated collateralised credit facility, which allowed LHL to issue its \$450.0 million 5.625% fixed rate reset junior subordinated notes due in 2041.

An uncollateralised facility has been in place since 30 July 2019, for an original amount of \$31.0 million. The facility was most recently increased to \$115.5 million on 29 October 2021 (from \$95.0 million effective 2 November 2020). It is available for utilisation by the Company and guaranteed by LHL for FAL purposes. As at 31 December 2021 \$115.5 million (31 December 2020 – \$90.5 million) of the LOC was issued under this facility and will expire on 31 December 2025.

The terms of the \$115.5 million uncollateralised facility included standard default and cross-default provisions and require certain covenants to be adhered to. These include the following:

- an A.M. Best financial strength rating of at least B++;
- a maximum debt to capital ratio of 30.0%, where the LHL junior subordinated loan notes are excluded as debt from this calculation; and
- maintenance of a minimum net worth requirement.

As at all reporting dates the Company was in compliance with all covenants under these facilities.

#### TRUSTS AND RESTRICTED BALANCES

The Company has several trust arrangements in place in favour of policyholders and ceding companies in order to comply with the security requirements of certain reinsurance contracts and/or the regulatory requirements of certain jurisdictions.

In 2012, the Company entered into an MBRT to collateralise its reinsurance liabilities associated with U.S. domiciled clients. As at and for the years ended 31 December 2021 and 2020, the Company had been granted authorised or trustee reinsurer status in all U.S. States. The MBRT is subject to the rules and regulations of the aforementioned states and the respective deed of trust. These rules and regulations include minimum capital funding requirements, investment guidelines, capital distribution restrictions and regulatory reporting requirements.

In 2013 the Company entered into a QST agreement with CCL 1998. See note 17 for further details. Under the original agreement the Company was required to provide 85.0% of the required FAL to support the underwriting capacity of Syndicate 2010 and Syndicate 3010. In 2021, the QST agreement was amended and the Company is now required to provide 100% of the required FAL. FAL are restricted in their use and are only drawn down to pay cash calls to Syndicate 2010 and Syndicate 3010. FAL requirements are formally assessed twice a year and any funds surplus to requirements may be released at this time.

As at and for the years ended 31 December 2021 and 2020, the Company was in compliance with all covenants under its trust facilities.

## NOTES TO THE ACCOUNTS CONTINUED

### 13. FINANCING ARRANGEMENTS CONTINUED

The following cash and cash equivalent and investment balances were held in trust, other collateral accounts in favour of third parties, or are otherwise restricted:

As at 31 December	2021			2020		
	Cash and cash equivalents \$m	Fixed maturity securities \$m	Total \$m	Cash and cash equivalents \$m	Fixed maturity securities \$m	Total \$m
FAL	108.1	227.3	335.4	16.7	251.5	268.2
MBRT	0.3	259.9	260.2	0.8	179.3	180.1
In trust in favour of affiliates	0.4	210.4	210.8	7.2	204.5	211.7
In favour of LOCs	2.1	32.3	34.4	4.9	29.8	34.7
In trust accounts for policyholders	15.9	5.6	21.5	14.5	5.9	20.4
In favour of derivative contracts	1.4	1.9	3.3	1.8	—	1.8
<b>Total</b>	<b>128.2</b>	<b>737.4</b>	<b>865.6</b>	<b>45.9</b>	<b>671.0</b>	<b>716.9</b>

### 14. SHARE CAPITAL

Authorised ordinary shares of \$1.00 each	Number	\$m
<b>As at 31 December 2021 and 2020</b>	<b>1,000,000</b>	<b>1.0</b>
Allocated, called up and fully paid	Number	\$m
<b>As at 31 December 2021 and 2020</b>	<b>1,000,000</b>	<b>1.0</b>

#### DIVIDENDS

During the year ended 31 December 2021 and 31 December 2020, there were no dividends declared.

### 15. LEASES

The Company leases two properties and has the following right-of-use assets and lease liabilities in relation to these leases. The Company does not face a significant liquidity risk with regards to its lease liabilities.

#### RIGHT-OF-USE ASSETS

	Property \$m	Total \$m
<b>As at 31 December 2019</b>	3.6	3.6
Additions	0.2	0.2
Depreciation	(1.0)	(1.0)
<b>As at 31 December 2020</b>	2.8	2.8
Depreciation	(1.0)	(1.0)
<b>As at 31 December 2021</b>	<b>1.8</b>	<b>1.8</b>

#### LEASE LIABILITIES

As at 31 December	2021 \$m	2020 \$m
Due in less than one year	1.1	1.1
Due between one and five years	1.1	2.2
<b>Total undiscounted lease liabilities</b>	<b>2.2</b>	<b>3.3</b>
<b>Total discounted lease liabilities</b>	<b>2.0</b>	<b>3.0</b>
Current	1.0	1.0
Non-current	1.0	2.0

## NOTES TO THE ACCOUNTS CONTINUED

### 15. LEASES CONTINUED

#### AMOUNTS RECOGNISED IN PROFIT OR LOSS

For the year ended 31 December	2021 \$m	2020 \$m
Depreciation of right-of-use assets	1.0	1.0
Interest expense on lease liabilities	0.2	0.2
Expenses relating to short-term leases and variable leases	0.1	0.2
<b>Total</b>	<b>1.3</b>	<b>1.4</b>

Total lease payments included in the cash flow statement are \$1.2 million for the year ended 31 December 2020 (2020 – \$1.1 million).

### 16. COMMITMENTS AND CONTINGENCIES

#### A. CREDIT FACILITY FUND

As at 31 December 2021 the Company has a commitment of \$100.0 million (31 December 2020 – \$100.0 million) relating to two credit facility funds (refer to note 10).

#### B. PRIVATE INVESTMENT FUNDS

On 28 July 2021, the Company entered into an agreement to invest in a private investment fund, with an initial commitment of \$34.0 million. As at 31 December 2021, there was a remaining undrawn commitment in the amount of \$27.9 million.

On 9 December 2020, the Company entered into an agreement to invest in a private investment fund, with an initial commitment of \$25.0 million. As at 31 December 2021, there was a remaining undrawn commitment in the amount of \$8.1 million.

On 5 November 2019, the Company entered into an agreement to invest in a private investment fund, with an initial commitment of \$25.0 million. As at 31 December 2021, there was a remaining undrawn commitment in the amount of \$1.0 million.

#### C. LEGAL PROCEEDINGS AND REGULATIONS

The Company operates in the insurance industry and is subject to legal proceedings in the normal course of business. While it is not practicable to estimate or determine the final results of all pending or threatened legal proceedings, management does not believe that such proceedings (including litigation) will have a material effect on its results and financial position.

### 17. RELATED PARTY DISCLOSURES

#### KEY MANAGEMENT COMPENSATION

Remuneration for key management was as follows:

For the year ended 31 December	2021 \$m	2020 \$m
Short-term compensation	3.3	5.6
Equity based compensation	1.1	1.5
<b>Total</b>	<b>4.4</b>	<b>7.1</b>

#### TRANSACTIONS WITH AFFILIATES

The Company entered into various services agreements with its parent company and other Group subsidiaries. Net other income in the statement of comprehensive(loss)income includes an expense of \$2.2 million (2020 – \$1.3 million income) relating to such transactions with LHL and its subsidiaries.

The table below provides a break down of the net service fees included within net other income:

For the year ended 31 December	2021 \$m	2020 \$m
Service fee income	3.6	5.1
Service fee expenses	(5.8)	(3.8)
<b>Net service fees</b>	<b>(2.2)</b>	<b>1.3</b>

During the year ended 31 December 2021 LHL contributed cash and fixed maturity securities of \$178.4 million (31 December 2020 – \$285.0 million) to the Company. These transaction are reflected in contributed surplus.

## NOTES TO THE ACCOUNTS CONTINUED

### 17. RELATED PARTY DISCLOSURES CONTINUED

LHL's equity based compensation scheme is its RSS. LHL has issued RSS options to certain LICL employees. LHL charges the Company for equity based compensation granted. Charges are based on the underlying estimated fair values and vesting conditions, adjusted by actions taken by LHL's Remuneration Committee as required. Refer to note 6 for the equity based compensation expense included in the statement of comprehensive (loss) income.

The Company has entered into a QST agreement with LUK. Under this agreement LUK cedes a share of all its business written or assumed. The following balances and transactions with LUK under the QST are included in the Company's financial statements:

Balance sheet	2021 \$m	2020 \$m
<b>Assets</b>		
Deferred acquisition costs	25.3	28.0
Inwards premium receivable from insureds and cedants	17.7	19.1
Other receivables	—	4.1
<b>Liabilities</b>		
Losses and loss adjustment expenses	208.3	185.3
Unearned premiums	89.5	84.5
<b>Statement of comprehensive (loss) income</b>	<b>2021 \$m</b>	<b>2020 \$m</b>
Gross premiums written	154.0	118.0
Change in unearned premiums	(5.0)	0.9
Insurance losses and loss adjustment expenses	82.3	75.3
Insurance acquisition expenses	70.9	62.1

The Company holds \$211.8 million (31 December 2020 – \$212.6 million) of cash and cash equivalents, fixed maturity securities and accrued interest in trust for the benefit of LUK in relation to the QST agreement.

The Company has entered into a QST agreement with CCL 1998. Under this agreement CCL 1998 cedes 85.0% of its financial result, which includes both insurance and non-insurance balances, to the Company. Net other income in the statement of comprehensive (loss) income includes \$20.1 million (2020 – \$2.4 million) relating to the QST agreement. As at 31 December 2021, other receivables includes \$6.9 million (31 December 2020 – \$26.7 million was included in other payables) relating to the QST agreement.

Excerpts from the CCL 1998 statement of comprehensive (loss) income are shown below. LICL's share of the CCL 1998's net financial result is shown in the statement of comprehensive (loss) income within net other losses.

For the year ended 31 December	2021 \$m	2020 \$m
Gross premiums written	376.2	356.5
Outwards reinsurance premiums	(115.4)	(115.2)
Net premium written	260.8	241.3
Net premium earned	224.6	214.8
Net insurance losses and loss adjustment expenses	121.5	131.5
Other expenses	79.4	80.5
<b>Net result</b>	<b>23.7</b>	<b>2.8</b>
<b>LICL 85.0% share of the net result of CCL 1998</b>	<b>20.1</b>	<b>2.4</b>

The Company holds \$335.4 million (31 December 2020 – \$268.2 million) of cash and cash equivalents and fixed maturity securities in FAL in relation to the QST agreement. On 15 October 2021 the Company agreed to provide 100% of FAL and increase from the previous 85%. During the year the Company increased the uncollateralised facility for FAL purposes to \$115.5 million (31 December 2020 – \$95.0 million). As at 31 December 2021 \$115.5 million (31 December 2020 – \$95.0 million) of the LOC was issued under this facility. See note 13 for further details.



## NOTES TO THE ACCOUNTS CONTINUED

### 17. RELATED PARTY DISCLOSURES CONTINUED

#### TRANSACTIONS WITH SUBSIDIARY OF AFFILIATE

During 2021 and 2020, the Company entered into an reinsurance agreement with KRL. The following balances were included in the Company's financial statements for the year ended 31 December 2021 and 2020.

	2021	2020
	\$m	\$m
<b>Balance sheet</b>		
Unearned premiums on premiums ceded	3.1	3.5
Reinsurance recoveries	25.0	—
Amounts payable to reinsurers	2.8	3.1
Deferred acquisition cost ceded	0.4	0.4
	2021	2020
	\$m	\$m
<b>Statement of comprehensive (loss) income</b>		
Outwards reinsurance premiums	(13.9)	(7.0)
Change in unearned premiums on premiums ceded	(0.3)	(0.3)
Insurance losses and loss adjustment expenses recoverable	(25.0)	—
Insurance acquisition expenses ceded	0.9	0.9

## GLOSSARY

### Additional case reserves (ACR)

Additional reserves deemed necessary by management

### AFS

Available-for-sale

### Aggregate

Accumulations of insurance loss exposures which result from underwriting multiple risks that are exposed to common causes of loss

### A.M. Best Company (A.M. Best)

A.M. Best is a full-service credit rating organisation dedicated to serving the financial services industries, focusing on the insurance sector

### Board of Directors

Unless otherwise stated, refers to the Company's Board of Directors

### Best Lancashire Assessment of Solvency over Time (BLAST)

The Company's economic internal capital model

### BMA

Bermuda Monetary Authority

### BSCR

Bermuda Solvency and Capital Return

### BSX

Bermuda Stock Exchange

### CCL 1998

Cathedral Capital (1998) Limited, the Lloyd's corporate member of the Group

### CEND

Confiscation, expropriation, nationalisation and deprivation

### Change in FCBVS

The IRR of the change in FCBVS in the period plus accrued dividends

### The Company (LICL)

Lancashire Insurance Company Limited

### Ceded

To transfer insurance risk from a direct insurer to a reinsurer and/or from a reinsurer to a retrocessionaire

### Combined ratio

Ratio, in per cent, of the sum of net insurance losses, net acquisition expenses and other operating expenses to net premiums earned

### CRO

Chief Risk Officer

### Deferred acquisition costs

Costs incurred for the acquisition or the renewal of insurance policies (e.g. brokerage and premium taxes) which are deferred and amortised over the term of the insurance contracts to which they relate

### Duration

Duration is the weighted average maturity of a security's cash flows, where the present values of the cash flows serve as the weights. The effect of the convexity, or sensitivity, of the portfolio's response to changes in interest rates is also factored in to the calculation

### EEA

European Economic Area

### ERM

Enterprise Risk Management

### Excess of loss

Reinsurance or insurance that indemnifies the reinsured or insured against all or a specified portion of losses on an underlying insurance policy in excess of a specified amount

### Expense ratio

Ratio, in per cent, of other operating expenses to net premiums earned

### Facultative reinsurance

A reinsurance risk that is placed by means of a separately negotiated contract as opposed to one that is ceded under a reinsurance treaty

### FAL

Funds at Lloyd's

### Fully converted book value per share (FCBVS)

Calculated by dividing the value of the total shareholders' equity plus the proceeds that would be received from the exercise of all dilutive equity compensation awards by the sum of all shares, including equity compensation awards, assuming all are exercised

### FVTPL

Fair value through profit or loss

## GLOSSARY CONTINUED

### G10

Belgium, Canada, Germany, France, Italy, Japan, the Netherlands, Sweden, the United Kingdom, and the United States

### Gross premiums written

Amounts payable by the insured, excluding any taxes or duties levied on the premium, including any brokerage and commission deducted by intermediaries

### The Group

LHL and its subsidiaries

### IFRIC

International Financial Reporting Interpretations Committee

### IFRS

International Financial Reporting Standard(s)

### Industry loss warranty (ILW)

A type of reinsurance or derivative contract through which one party will purchase protection based on the total loss arising from an event to the entire insurance industry rather than their own losses.

### Incurred but not reported (IBNR)

These are anticipated or likely losses that may result from insured events which have taken place, but for which no losses have yet been reported. IBNR also includes a reserve for possible adverse development of previously reported losses

### International Accounting Standard(s) (IAS)

Standards, created by the IASB, for the preparation and presentation of financial statements

### International Accounting Standards Board (IASB)

An international panel of accounting experts responsible for developing IAS and IFRS

### IRR

Internal rate of return

### IRRC

Investment Risk and Return Committee

### KRL

Kinesis Reinsurance I Limited, the Group holds an interest in KRL's parent company

### LHL

Lancashire Holdings Limited

### LIBOR

London Interbank Offered Rate

### LICL

Lancashire Insurance Company Limited

### LOC

Letter of credit

### Losses

Demand by an insured for indemnity under an insurance contract

### LUK

Lancashire Insurance Company (UK) Limited, an entity under common control

### Managed cash

Managed cash includes both cash managed by external investment managers and non-operating cash managed internally

### MBRT

Multi-beneficiary reinsurance trust

### NAV

Net asset value

### Net acquisition cost ratio

Ratio, in per cent, of net acquisition expenses to net premiums earned

### Net loss ratio

Ratio, in per cent, of net insurance losses to net premiums earned

### Net premiums written

Net premiums written is equal to gross premiums written less outwards reinsurance premiums written

## GLOSSARY CONTINUED

### ORSA

Own Risk and Solvency Assessment

### OTC

Over the counter

### Pro-rata/proportional

Reinsurance or insurance where the reinsured or insured shares a proportional part of the original premiums and losses of the reinsured or insured

### QST

Quota Share Treaty

### Retrocession

The reinsurance of the reinsurance account

### Return on Equity (RoE)

The IRR of the change in FCBVS in the period plus accrued dividends

### RDS

Realistic Disaster Scenarios

### RRC

Risk and Return Committee

### RSC

Reinsurance Security Committee

### RSS

Restricted share scheme

### Syndicate 2010

Lloyd's Syndicate 2010 managed by CUL, a subsidiary of CCL

### Syndicate 3010

Lloyd's Syndicate 3010 managed by CUL, a subsidiary of CCL

### TBAs

Mortgage backed "to be announced" securities

### Treaty reinsurance

A reinsurance contract under which the reinsurer agrees to offer and to accept all risks of a certain size within a defined class

### Unearned premiums

The portion of premium income that is attributable to periods after the balance sheet date is deferred and amortised to future accounting periods

### UMCC

Underwriting and Marketing Conference Call

### UNL

Ultimate net loss

### Value at Risk (VaR)

A measure of the risk of loss of a specific portfolio of financial asset