LANCASHIRE HOLDINGS LIMITED

GROWTH IN FULLY CONVERTED BOOK VALUE PER SHARE, ADJUSTED FOR DIVIDENDS, OF 6.4% IN Q4, 23.3% IN 2010; COMBINED RATIO OF 20.8% FOR Q4, 54.4% FOR 2010 FINAL DIVIDEND OF 10.0 CENTS PER COMMON SHARE FULLY CONVERTED BOOK VALUE PER SHARE OF $7.57 AT 31 DECEMBER 2010

21 February 2011
Hamilton, Bermuda

Lancashire Holdings Limited ("Lancashire" or "the Group") today announces its results for the fourth quarter of 2010 and the year ended 31 December 2010.

Financial highlights

	As at 31 December 2010	**As at 31 December 2009**
Fully converted book value per share	**$7.57**	**$7.41**
Return on equity* – Q4	**6.4%**	**7.0%**
Return on equity* – Year	**23.3%**	**26.5%**
Operating return on equity – Q4	**8.2%**	**7.7%**
Operating return on equity – Year	**20.9%**	**24.9%**
Special dividend per common share**	**$1.40**	**$1.25**

* Return on equity is defined as growth in fully converted book value per share, adjusted for dividends.
** See "Dividends" below for Record Date and Dividend Payment Date.

Financial highlights:

	Three months ended		**Year ended**	
	31 Dec 2010	**31 Dec 2009**	**31 Dec 2010**	**31 Dec 2009**
Highlights ($m)				
Gross premiums written	94.0	103.4	689.1	627.8
Net premiums written	93.7	100.0	649.9	577.1
Net profit after tax	131.8	129.6	330.8	385.4
Net operating profit	123.4	122.4	306.5	364.7
Share repurchases	nil	16.9	136.4	16.9
Per share data				
Fully diluted earnings per share	$0.76	$0.69	$1.86	$2.05
Fully diluted earnings per share – operating	$0.71	$0.65	$1.73	$1.94
Financial ratios				
Total investment return	(0.4%)	0.5%	4.2%	3.9%
Net loss ratio	(6.1%)	(0.8)%	27.0%	16.6%
Combined ratio	20.8%	25.7%	54.4%	44.6%
Accident year loss ratio	7.2%	24.0%	42.9%	27.2%

Richard Brindle, Group Chief Executive Officer, commented:

"In October 2010 Lancashire marked its fifth anniversary and, since our foundation, our approach to underwriting and capital management has been marked by discipline, teamwork and flexibility. These principles have once again been our trademark in the final quarter of 2010 when, as a general rule, premium rates have been flat or declining.

I am therefore pleased to report another excellent set of financial results, and to note that Lancashire's performance has, for the third time in the last four years, enabled us to pay a special dividend to our shareholders. Lancashire increased book value per share by 6.4% in the fourth quarter, delivering a return on equity of 23.3% for the full year. Since our inception in 2005 we have generated a compound annual return on equity of 20.3%. As of 18 February 2011 our original shareholders have received an annualized internal rate of return of 24.3% on their investment.

2010 witnessed an active claims environment. Lancashire had moderate exposure to losses from both the Deepwater Horizon disaster and the Chile Maule earthquake but minimal losses to the New Zealand earthquake in the third quarter, the Australian floods at the turn of the year and the recent unrest in Tunisia and Egypt. Our overall premiums written fell in the fourth quarter. Premiums written increased significantly for energy but declined in other areas. This reflects the relative attractiveness of available opportunities between classes.

Looking ahead, in the core area of underwriting, the bright spots continue to be in the offshore energy lines and the marine retrocessional sector, where premium rates have improved following the Deepwater Horizon disaster in the spring of 2010. We increased our sovereign risk book, contracts in the political risk class relating to sovereign or quasi-sovereign obligors, where we believe pricing remains attractive. Otherwise, premium rates have continued to weaken and we have reduced our underwriting exposure accordingly.

In 2011 we believe that, whilst premium rates will tend to decline overall, our discipline, flexibility and strong and experienced team will keep our business model highly competitive. Companies often lose their discipline at this point in the cycle. Our daily underwriting call helps us stay focused on risk selection whilst protecting our core broker and client relationships. Lancashire is well positioned both for the soft market and to quickly take advantage of the next market moving event, whenever it might occur."

Elaine Whelan, Group Chief Financial Officer, commented:

"Our combined ratio for the fourth quarter was an excellent 20.8%, reflecting very low losses incurred by Lancashire, including in the property catastrophe class. Strong underwriting performance in the fourth quarter was dampened by a substantial drop in bond values, particularly in U.S. Treasuries. Unfortunately, as a result, our investments suffered a loss of 0.4% during the fourth quarter. We do not currently hold any equities and therefore did not benefit from the strong performance of that asset class. However, our investment portfolio structure ensured Q4 losses were minimal and we were still able to produce a respectable total investment return of 1.6% for the second half of 2010 and 4.2% for the year.

With the announcement of our final dividend today we will have returned $1.135 billion, or 82%, of comprehensive income generated over the first five years of trading to our shareholders, and over 130% of comprehensive income generated this year, ending 2010 with just under $100 million less capital than we started with. We continue to actively monitor our capital levels versus the opportunities we see. We will also request shareholder approval for a renewed share repurchase authorisation at our Annual General Meeting in May. This should afford us the flexibility to manage our capital throughout the coming year, however circumstances unfold."

Lancashire Renewal Price Index for major classes

Lancashire's Renewal Price Index ("RPI") is an internal tool that management uses to track trends in premium rates on a portfolio of insurance and reinsurance contracts. The RPI is calculated on a per contract basis and reflects Lancashire's assessment of relative changes in price, terms, conditions and limits and is weighted by premium volume (see "Note Regarding RPI Tool" at the end of this announcement for further guidance). The following RPIs are expressed as an approximate percentage of pricing achieved on similar contracts written in 2009:

Class	Year 2010	Q4 2010	Q3 2010	Q2 2010	Q1 2010
Aviation (AV52)	91%	88%	100%	97%	92%
Gulf of Mexico energy	102%	100%	99%	106%	87%
Energy offshore worldwide	105%	101%	114%	109%	98%
Marine	98%	100%	100%	96%	99%
Direct and facultative	93%	92%	96%	92%	95%
Property reinsurance	96%	90%	96%	94%	97%
Terrorism	92%	90%	92%	93%	92%
Combined	**97%**	**90%**	**99%***	**99%***	**96%***

* Q1 to Q3 combined RPIs are unchanged from previously reported after being updated for subsequent adjustments to bound premium.

Underwriting results

Gross premiums written

	Q4				Year			
	2010 $m	**2009 $m**	**Change $m**	**Change %**	**2010 $m**	**2009 $m**	**Change $m**	**Change %**
Property	36.9	47.2	(10.3)	(21.8)	323.6	317.3	6.3	2.0
Energy	28.0	14.7	13.3	90.5	238.3	175.5	62.8	35.8
Marine	6.5	12.7	(6.2)	(48.8)	76.4	73.7	2.7	3.7
Aviation	22.6	28.8	(6.2)	(21.5)	50.8	61.3	(10.5)	(17.1)
Total	**94.0**	**103.4**	**(9.4)**	**(9.1)**	**689.1**	**627.8**	**61.3**	**9.8**

Gross premiums written decreased by 9.1% in the fourth quarter of 2010 compared to the same period in 2009. In 2010 annual gross premiums written increased by 9.8% compared to 2009. Excluding reinstatement premiums and the impact of multi-year contracts, gross premiums written in 2010 were 1.4% lower than 2009, with the declining pricing environment being offset by an improvement in energy pricing following the Deepwater Horizon loss.

The Group's four principal classes, and the key market factors impacting them, are discussed below.

Property gross premiums written decreased by 21.8% for the fourth quarter of 2010 compared to the same period in 2009 and increased by 2.0% for the year ended 31 December 2010 compared to the year ended 31 December 2009. In the fourth quarter of 2010, the majority of the Group's property book showed premium reductions compared to the same period in the prior year. This largely reflects the declining pricing environment in addition to the timing of renewal of certain multi-year contracts in the terrorism portfolio. The growth area of political risk was attributable to the addition of the sovereign obligors' line within this class in 2010. Reinsurance premiums for the year ended 31 December 2010 were marginally down on the prior year. At the start of 2010, price reductions in property reinsurance classes were minor and a tactical decision was taken to deploy more of the Group's capital at the January 2010 reinsurance renewals than in prior years. A significant amount of new business across this line was therefore written in the first quarter of 2010, including some large multi-year property catastrophe reinsurance contracts, with a corresponding reduction in appetite in these lines during the remainder of the year. The property retrocession line was also impacted by declining pricing throughout the year, but included approximately $12.1 million of reinstatement premiums in the first quarter in connection with the Chile Maule earthquake in February. Within the terrorism line, premiums increased year on year due to opportunities that arose earlier in 2010 from the post recession recommencement of construction projects around the world, plus increased participation in international terror pools.

Energy gross premiums written increased by 90.5% for the fourth quarter of 2010 compared to the same period in 2009 and increased by 35.8% for the year ended 31 December 2010 compared to the year ended 31 December 2009. Although the majority of energy renewals took place during the second quarter, pricing remained positive in the offshore sector during the fourth quarter following the Deepwater Horizon loss in April 2010. The timing of some worldwide offshore contract renewals also had a positive impact on the fourth quarter premiums written compared to the same period in 2009. In the year to date, Gulf of Mexico premium volume was considerably higher compared to the prior year. This was driven by increased demand, including insureds seeking new layers and increased limits following the Deepwater Horizon loss. Premiums written were also buoyed by a number of large Gulf of Mexico catastrophe accounts being written or renewed on a multi-year basis. The Group also wrote some non-elemental Industry Loss Warranty covers in the second quarter following insurance industry losses suffered from Deepwater Horizon. $5.4 million of the premium in respect of these covers is included in the premium numbers for the energy excess of loss class.

Marine gross premiums written decreased by 48.8% for the fourth quarter of 2010, compared to the same period in 2009 and increased by 3.7% for the year ended 31 December 2010 compared to the year ended 31 December 2009. Pricing and renewal rates were broadly stable. The reduction in the fourth quarter of 2010 and the small increase for the year overall were largely driven by the timing of certain multi-year contract renewals and some contract extensions or exposure increases.

Aviation gross premiums written decreased by 21.5% for the fourth quarter of 2010 compared to the same period in 2009 and decreased by 17.1% for the year ended 31 December 2010 compared to the year ended 31 December 2009. The reduction was driven partly by a reduction in the number of flights flown and passengers travelling in the recent recessionary environment plus a competitive fourth quarter renewal environment.

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Ceded premiums decreased by $3.1 million, or 91.2% for the fourth quarter of 2010 and decreased by $11.5 million, or 22.7% for the year ended 31 December 2010 compared to the same periods in 2009. The fourth quarter is not a major renewal period for the Group's reinsurance cover. The reduction in the cost of outwards reinsurance cover for the year was helped by improved pricing compared to 2009 and by a restructuring of the Group's cover from a whole account cover to an individual risk cover, offset by the Group purchasing additional catastrophe cover on its U.S. property direct and facultative portfolio, and reinstating non-elemental cover on its marine and energy book in the second quarter.

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Net premiums earned as a proportion of net premiums written were 159.4% in the fourth quarter of 2010 compared to 155.6% in the same period in 2009 and 94.5% for the year ended 31 December 2010 compared to 103.0% in 2009. The significant increase in premium written volumes in the first quarter of 2010 as compared to 2009 resulted in a comparatively large deferral of earnings from earlier to later in the year and partially into 2011. Premiums on a significant multi-year contract within the property catastrophe reinsurance class and several within the energy Gulf of Mexico class, of $36.7 million and $33.4 million respectively, also drove the material deferrals of earning of premiums written earlier in the year. Year on year fourth quarter earnings are therefore broadly comparable, given relatively consistent levels of premiums written, although there remains a lag for the year to date.

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The Group's net loss ratio for the fourth quarter of 2010 was negative 6.1% compared to negative 0.8% for the same period in 2009 and 27.0% for the year ended 31 December 2010 compared to 16.6% for 2009. Both fourth quarters reflect an unusually low number of reported losses during the period combined with favourable development of prior year loss reserves. The fourth quarter of 2010 also benefited from a reduction in the net loss for the Chile Maule earthquake of $6.8 million to $84.7 million compared to the previous quarter's reported loss of $91.5 million. The Group's expected net loss range is now $77.6 to $92.4 million compared to the initial reported range of $65.0 to $125.0 million at 31 March 2010. The twelve months to 31 December 2010 include the impact of the Chile Maule earthquake plus the total loss of the Deepwater Horizon drilling unit. Lancashire's net claim for the Deepwater Horizon loss remains $25.0 million. Excluding these two events, the net loss ratio for the year would have been 7.2%. While our reserves in relation to the Chile Maule earthquake have become somewhat clearer, there continues to be considerable uncertainty on the eventual ultimate loss. In respect of the New Zealand earthquake and Queensland floods less than $5.0 million has been recorded within reserves for these events combined.

The table below provides further detail of loss development by class, excluding the impact of foreign exchange revaluations.

	Q4		**Year**	
	2010	**2009**	**2010**	**2009**
	$m	**$m**	**$m**	**$m**
Property	(5.1)	7.5	28.8	44.4
Energy	20.0	29.6	47.6	9.3
Marine	6.3	2.2	17.7	6.1
Aviation	0.6	0.2	6.0	3.7
Total	**21.8**	**39.5**	**100.1**	**63.5**

Note: Positive numbers denote favourable development and negative numbers denote adverse development.

Net prior year reserve releases were $21.8 million and $100.1 million for the fourth quarter and for the year ended 31 December 2010 respectively, compared to $39.5 million and $63.5 million for the same periods in 2009. The favourable development in 2010 arose primarily from IBNR releases due to fewer than expected reported losses. In the first quarter of 2009 there was $39.8 million of adverse development on Hurricane Ike, which was subsequently reduced by $22.7 million in the fourth quarter of 2009, based on further loss adjustment reports and some negotiated settlements. The final net adverse development on Ike in 2009 as a whole was $17.1 million.

The accident year loss ratio for the fourth quarter of 2010, including the impact of foreign exchange revaluations, was 7.2% compared to 24.0% for the same period in 2009. The accident year loss ratio for the year ended 31 December 2010 was 42.9% compared to 27.2% for the year ended 31 December 2009. The fourth quarter of 2010 accident year loss ratio reflects the reduction in the Chile Maule net loss and an exceptionally low level of reported losses. Chile Maule and Deepwater Horizon contributed 15.2% and 4.5% respectively to the 2010 accident year loss ratio. Excluding the impact of foreign exchange revaluations, previous accident years' ultimate losses developed as follows during 2010:

- 2006 - favourable development of $0.3 million (2009: $4.4 million development);
- 2007 - favourable development of $8.3 million (2009: $25.2 million);
- 2008 - favourable development of $36.0 million (2009: $33.9 million); and
- 2009 - favourable development of $55.5 million (2009: n/a).

The ratio of IBNR to total reserves was 38.4% at 31 December 2010 compared to 42.4% at 31 December 2009.

Investments

The Group continues to hold a conservative investment portfolio, consistent with its long-held philosophy, with a strong emphasis on preserving capital. At 31 December 2010, the managed portfolio comprised 78.1% fixed income securities and 21.9% cash and cash equivalents compared to 92.9% fixed income securities and 7.1% cash and cash equivalents at 31 December 2009. Key investment portfolio statistics are:

	As at 31 December 2010	**As at 31 December 2009**
Duration	2.2 years	2.3 years
Credit quality	AA	AA+
Book yield	2.4%	2.8%
Market yield	1.9%	2.2%

Net investment income, excluding realised and unrealised gains and losses, was $12.7 million for the fourth quarter of 2010, a decrease of 9.3% from the fourth quarter of 2009. While the decrease was partly due to lower yields compared to the fourth quarter of 2009, the majority was due to the reduction in the Group's fixed income portfolio relative to the same period in 2009. This was driven largely by the funding of the Group's special dividend payment. Net investment income was $53.4 million for the year ended 31 December 2010 compared to $56.0 million for the prior year, a decrease of $2.6 million, or 4.6%, reflecting the lower yield interest rate environment in 2010 compared to 2009.

Total investment return, including net investment income, net realised gains and losses, impairments and net change in unrealised gains and losses, was negative $8.3 million for the fourth quarter of 2010 compared to positive $11.1 million for the fourth quarter of 2009, and was $84.5 million for the year ended 31 December 2010 compared to $82.9 million for the same period in 2009. The negative return in the fourth quarter of 2010 was due to the substantial drop in bond values in November and December 2010. Returns for the year, however, were marginally higher than 2009 due to the increased allocation to both corporate bonds and emerging market debt, which is now 6.8% of managed investments. The emerging market debt portfolio at 31 December 2010 was allocated as follows: 58.1% sovereign debt, 24.8% quasi-sovereign debt, and 17.1% corporate bonds; with an overall average credit quality of BBB-. The corporate bond allocation, excluding Federal Deposit Insurance Corporation guaranteed bonds, represented 31.1% at 31 December 2010 of managed invested assets compared to 23.6% at 31 December 2009. There were no impairments recorded in the year ended 31 December 2010 compared to $0.4 million for the year ended 31 December 2009.

Other operating expenses

Other operating expenses, excluding the cost of equity based compensation, are broadly consistent compared with the same period in 2009, reflecting the Group's stable operating platform. Total employment costs, excluding equity based compensation, were $33.2 million for the year ended 31 December 2010 compared to $35.6 million in the twelve months to 31 December 2009.

Equity based compensation was $6.1 million in the fourth quarter of 2010 compared to $7.1 million in the same period last year. For the years ended 31 December 2010 and 2009 the charge was $21.1 million and $16.4 million, respectively. The reduction in the quarter to date expense was due to the decreasing costs of warrants and options as awards made under these schemes vest, offset to a degree by the maturing restricted share scheme. The increased 2010 expense reflects the maturing restricted share awards program, plus an increase in vesting assumptions given the Group's excellent performance and an increase in the proportion of employees' variable compensation provided as deferred shares compared to prior years. The restricted share program began in 2008.

Capital

At 31 December 2010, total capital was $1.416 billion, comprising shareholders' equity of $1.287 billion and $128.8 million of long-term debt. Leverage was 9.1%. Total capital at 31 December 2009 was $1.510 billion.

Repurchase program

There were no shares repurchased during the fourth quarter of 2010 compared to $16.9 million of shares repurchased in the same period of 2009. In total $136.4 million of shares were repurchased in the year ended 31 December 2010 and $16.9 million in the year ended 31 December 2009. The share repurchase program had 7,841,826 shares of the authorised maximum of 18,250,306 remaining to be purchased at 31 December 2010.

The Board will be proposing, at the Annual General Meeting to be held on 5 May 2011 that the shareholders approve a renewed share repurchase program with such authority to expire on the conclusion of the 2012 Annual General Meeting or, if earlier, 15 months from the date the resolution approving the renewed share repurchase program is passed.

Dividends

The Lancashire Board declared the following dividends during 2010:

- A Final dividend in respect of 2009 of $0.10 per common share;
- An Interim dividend of $0.05 per common share; and
- A Special dividend of $1.40 per common share.

Lancashire announces that its Board has declared a final dividend in respect of 2010 of $0.10 per common share (approximately 6.2 pence per common share at the current exchange rate), which results in an aggregate payment of approximately $9.4 million. The dividend will be paid in Pounds Sterling on 20 April 2011 (the "Dividend Payment Date") to shareholders of record on 18 March 2011 (the "Record Date") using the £ / $ spot market exchange rate at the close of business in London on the Record Date.
In addition to the final dividend payment to shareholders, approximately $2.3 million in aggregate will be paid on the Dividend Payment Date to holders of share purchase warrants issued by the Company pursuant to the terms of the warrants.

The Group will continue to review the appropriate level and composition of capital for the Group with the intention of managing capital to enhance risk-adjusted returns on equity.

Financial information and posting of accounts

The consolidated financial statements set out below are audited. The audited Annual Report and Accounts are expected to be posted to shareholders no later than 14 March 2011 and will also be available on the Company's website by this date.

Further details of our 2010 fourth quarter results can be obtained from our Financial Supplement. This can be accessed via our website www.lancashiregroup.com.

Analyst and Investor Earnings Conference Call

There will be an analyst and investor conference call on the results at 1:00 pm UK time / 8:00 am EST on Monday, 21 February 2011. The call will be hosted by Lancashire management.

The call can be accessed by dialing +44 (0) 20 7138 0844 / +1 212 444 0895 with the passcode 9768470. The call can also be accessed via webcast, please go to our website (www.lancashiregroup.com) to access.

A replay facility will be available for two weeks until Monday, 7 March 2011. The dial in number for the replay facility is +44 (0) 20 7111 1244 / + 1 347 366 9565 with passcode 9768470#. The replay facility can also be accessed at www.lancashiregroup.com

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Investor enquiries and questions can also be directed to info@lancashiregroup.com or by accessing the Group's website www.lancashiregroup.com.

About Lancashire

Lancashire, through its UK and Bermuda-based insurance subsidiaries, is a global provider of specialty insurance products. The Group companies carry the following ratings:

	Financial Strength Rating (1)	**Long Term Issuer Rating (2)**	**Outlook**
A.M. Best	A-	BBB-	Positive
Standard & Poor's	A-	BBB	Stable
Moody's	A3	Baa2	Stable

(1)Financial Strength Rating applies to Lancashire Insurance Company Limited and Lancashire Insurance Company (UK) Limited

(2) Long Term Issuer Rating applies to Lancashire Holdings Limited

Lancashire has capital in excess of $1 billion and its Common Shares trade on the main market of the London Stock Exchange under the ticker symbol LRE. Lancashire is headquartered at Power House, 7 Par-la-Ville Road, Hamilton HM 11, Bermuda. The mailing address is Lancashire Holdings Limited, P.O. Box HM 2358, Hamilton HM HX, Bermuda. For more information on Lancashire, visit the Company's website at www.lancashiregroup.com

NOTE REGARDING RPI TOOL

LANCASHIRE'S RENEWAL PRICE INDEX ("RPI") IS AN INTERNAL TOOL THAT ITS MANAGEMENT USES TO TRACK TRENDS IN PREMIUM RATES OF A PORTFOLIO OF INSURANCE AND REINSURANCE CONTRACTS. THE RPI IS CALCULATED ON A PER CONTRACT BASIS AND REFLECTS LANCASHIRE'S ASSESSMENT OF RELATIVE CHANGES IN PRICE, TERMS, CONDITIONS AND LIMITS AND IS WEIGHTED BY PREMIUM VOLUME. THE CALCULATION INVOLVES A DEGREE OF JUDGEMENT IN RELATION TO COMPARABILITY OF CONTRACTS AND THE ASSESSMENT NOTED ABOVE. TO ENHANCE THE RPI TOOL, MANAGEMENT OF LANCASHIRE MAY REVISE THE METHODOLOGY AND ASSUMPTIONS UNDERLYING THE RPI, SO THE TRENDS IN PREMIUM RATES REFLECTED IN THE RPI MAY NOT BE COMPARABLE OVER TIME. CONSIDERATION IS ONLY GIVEN TO RENEWALS OF A COMPARABLE NATURE SO IT DOES NOT REFLECT EVERY CONTRACT IN LANCASHIRE'S PORTFOLIO. THE FUTURE PROFITABILITY OF

THE PORTFOLIO OF CONTRACTS WITHIN THE RPI IS DEPENDENT UPON MANY FACTORS BESIDES THE TRENDS IN PREMIUM RATES.

NOTE REGARDING FORWARD-LOOKING STATEMENTS:

CERTAIN STATEMENTS AND INDICATIVE PROJECTIONS (WHICH MAY INCLUDE MODELED LOSS SCENARIOS) MADE THAT ARE NOT BASED ON CURRENT OR HISTORICAL FACTS ARE FORWARD-LOOKING IN NATURE INCLUDING WITHOUT LIMITATION, STATEMENTS CONTAINING THE WORDS 'BELIEVES', 'ANTICIPATES', 'PLANS', 'PROJECTS', 'FORECASTS', 'GUIDANCE', 'INTENDS', 'EXPECTS', 'ESTIMATES', 'PREDICTS', 'MAY', 'CAN', 'WILL', 'SEEKS', 'SHOULD', OR, IN EACH CASE, THEIR NEGATIVE OR COMPARABLE TERMINOLOGY. ALL STATEMENTS OTHER THAN STATEMENTS OF HISTORICAL FACTS INCLUDING, WITHOUT LIMITATION, THOSE REGARDING THE GROUP'S FINANCIAL POSITION, RESULTS OF OPERATIONS, LIQUIDITY, PROSPECTS, GROWTH, CAPITAL MANAGEMENT PLANS, BUSINESS STRATEGY, PLANS AND OBJECTIVES OF MANAGEMENT FOR FUTURE OPERATIONS (INCLUDING DEVELOPMENT PLANS AND OBJECTIVES RELATING TO THE GROUP'S INSURANCE BUSINESS) ARE FORWARD-LOOKING STATEMENTS. SUCH FORWARD-LOOKING STATEMENTS INVOLVE KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND OTHER IMPORTANT FACTORS THAT COULD CAUSE THE ACTUAL RESULTS, PERFORMANCE OR ACHIEVEMENTS OF THE GROUP TO BE MATERIALLY DIFFERENT FROM FUTURE RESULTS, PERFORMANCE OR ACHIEVEMENTS EXPRESSED OR IMPLIED BY SUCH FORWARD-LOOKING STATEMENTS.

THESE FACTORS INCLUDE, BUT ARE NOT LIMITED TO: THE NUMBER AND TYPE OF INSURANCE AND REINSURANCE CONTRACTS THAT WE WRITE; THE PREMIUM RATES AVAILABLE AT THE TIME OF SUCH RENEWALS WITHIN OUR TARGETED BUSINESS LINES; THE LOW FREQUENCY OF LARGE EVENTS; UNUSUAL LOSS FREQUENCY; THE IMPACT THAT OUR FUTURE OPERATING RESULTS, CAPITAL POSITION AND RATING AGENCY AND OTHER CONSIDERATIONS HAVE ON THE EXECUTION OF ANY CAPITAL MANAGEMENT INITIATIVES; THE POSSIBILITY OF GREATER FREQUENCY OR SEVERITY OF CLAIMS AND LOSS ACTIVITY THAN OUR UNDERWRITING, RESERVING OR INVESTMENT PRACTICES HAVE ANTICIPATED; THE RELIABILITY OF, AND CHANGES IN ASSUMPTIONS TO, CATASTROPHE PRICING, ACCUMULATION AND ESTIMATED LOSS MODELS; LOSS OF KEY PERSONNEL; A DECLINE IN OUR OPERATING SUBSIDIARIES' RATING WITH RATING AGENCIES; INCREASED COMPETITION ON THE BASIS OF PRICING, CAPACITY, COVERAGE TERMS OR OTHER FACTORS; A CYCLICAL DOWNTURN OF THE INDUSTRY; THE IMPACT OF A DETERIORATING CREDIT ENVIRONMENT CREATED BY THE FINANCIAL MARKETS; A RATING DOWNGRADE OF, OR A MARKET DECLINE IN, SECURITIES IN OUR INVESTMENT PORTFOLIO; CHANGES IN GOVERNMENTAL REGULATIONS OR TAX LAWS IN JURISDICTIONS WHERE LANCASHIRE CONDUCTS BUSINESS; LANCASHIRE OR ITS BERMUDIAN SUBSIDIARY BECOMING SUBJECT TO INCOME TAXES IN THE UNITED STATES OR THE UNITED KINGDOM; AND THE EFFECTIVENESS OF OUR LOSS LIMITATION METHODS. ANY ESTIMATES RELATING TO LOSS EVENTS INVOLVE THE EXERCISE OF CONSIDERABLE JUDGEMENT AND REFLECT A COMBINATION OF GROUND-UP EVALUATIONS, INFORMATION AVAILABLE TO DATE FROM BROKERS AND INSUREDS, MARKET INTELLIGENCE, INITIAL AND/OR TENTATIVE LOSS REPORTS AND OTHER SOURCES. JUDGEMENTS IN RELATION TO LOSS ARISING FROM NATURAL CATASTROPHE AND MAN MADE EVENTS INVOLVE COMPLEX FACTORS POTENTIALLY CONTRIBUTING TO THESE TYPES OF LOSS, AND WE CAUTION AS TO THE PRELIMINARY NATURE OF THE INFORMATION USED TO PREPARE ANY SUCH ESTIMATES.

THESE FORWARD-LOOKING STATEMENTS SPEAK ONLY AS AT THE DATE OF PUBLICATION. LANCASHIRE HOLDINGS LIMITED EXPRESSLY DISCLAIMS ANY OBLIGATION OR UNDERTAKING (SAVE AS REQUIRED TO COMPLY WITH ANY LEGAL OR REGULATORY OBLIGATIONS (INCLUDING THE RULES OF THE LONDON STOCK EXCHANGE)) TO DISSEMINATE ANY UPDATES OR REVISIONS TO ANY FORWARD-LOOKING STATEMENTS TO REFLECT ANY CHANGES IN THE GROUP'S EXPECTATIONS OR CIRCUMSTANCES ON WHICH ANY SUCH STATEMENT IS BASED.

lancashire
HOLDINGS LIMITED

Underwriting comes first

Effectively balance risk and return

Operate nimbly through the cycle

Consolidated financial statements 31 December 2010

Contents

The Directors are responsible for preparing the Group's consolidated financial statements, in accordance with applicable laws and regulations, which give a true and fair view of the state of affairs of the Group and the results of the Group for that period including the assets, liabilities, financial position and profit and loss of the Group. The consolidated financial statements have been prepared in accordance with IFRS. Where IFRS is silent, as it is in respect of the measurement of insurance products, U.S. GAAP is considered. Further detail on the basis of preparation is described in the consolidated financial statements. In preparing the consolidated financial statements, the Directors are required to:

- Select suitable accounting policies and apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether they have been prepared in accordance with IFRS;
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- Prepare the consolidated financial statements on the going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group, and to enable them to ensure that the financial statements comply with applicable laws and regulations. They are also responsible for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors have elected to include the remuneration information contained in this Annual Report, although as a Company incorporated in Bermuda, Lancashire is not bound by UK law or regulation to the same extent that it applies to UK incorporated companies in the area of Directors' remuneration. As an LSE listed company with a premium listing, the Company adopts a comply or explain approach against the requirements of the Combined Code, and to this end the Company reports on both corporate governance and remuneration matters to facilitate its shareholders' better understanding. This Annual Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Legislation in Bermuda governing the preparation and dissemination of the consolidated financial statements may differ from legislation in other jurisdictions. In addition, the rights of shareholders under Bermuda law may differ from those for shareholders of companies incorporated in other jurisdictions.

The Directors responsible for authorising the responsibility statement on behalf of the Board are the Chairman, Martin Thomas, the President, Neil McConachie and the Company Secretary, Greg Lunn and this statement is made to the best of their knowledge and belief.

20 February 2011.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF LANCASHIRE HOLDINGS LIMITED

We have audited the financial statements of Lancashire Holdings Limited and its subsidiaries (collectively "the Group") for the year ended 31 December 2010 which comprise the consolidated balance sheet as at 31 December 2010, consolidated statement of comprehensive income, consolidated statement of changes in shareholders' equity and the statement of consolidated cash flows for the year then ended and the related notes 1 to 28. The financial reporting framework that has been applied in their preparation is International Financial Reporting Standards as adopted by the European Union.

This report is made solely to the Group's shareholders, in accordance with our engagement letter dated 6 July 2010. Our audit work has been undertaken so that we might state to the Group's Directors those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Group and its Directors as a body, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of the Directors and Auditor

As explained more fully in the Statement of Directors' Responsibilities included on page 3, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the Audit of the Consolidated Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on the Consolidated Financial Statements

In our opinion the consolidated financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2010 and of its profit for the year then ended; and
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to the Group’s compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Ernst & Young LLP
1 More London Place
London SE1 2AF
United Kingdom
20 February 2011

The maintenance and integrity of the Group’s website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the consolidated financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of the consolidated financial statements may differ from legislation in other jurisdictions.

Consolidated statement of comprehensive income

For the year ended 31 December 2010

	Notes	2010 $m	2009 $m
Gross premiums written	2	689.1	627.8
Outwards reinsurance premiums	2	(39.2)	(50.7)
Net premiums written		**649.9**	**577.1**
Change in unearned premiums	2	(33.0)	22.0
Change in unearned premiums on premiums ceded	2	(2.7)	(4.4)
Net premiums earned		**614.2**	**594.7**
Net investment income	3	53.4	56.0
Net other investment income	3	0.1	0.3
Net realised gains (losses) and impairments	3	33.2	23.8
Net foreign exchange (losses) gains		(0.1)	3.4
Total net revenue		**700.8**	**678.2**
Insurance losses and loss adjustment expenses	2, 12	194.7	104.4
Insurance losses and loss adjustment expenses recoverable	2, 12	(29.0)	(5.7)
Net insurance losses		**165.7**	**98.7**
Insurance acquisition expenses	2, 4	109.9	112.6
Insurance acquisition expenses ceded	2, 4	(3.6)	(6.6)
Other operating expenses	5, 6, 22	61.8	60.5
Equity based compensation	6	21.1	16.4
Total expenses		**354.9**	**281.6**
Results of operating activities		**345.9**	**396.6**
Financing costs	7	6.7	8.1
Profit before tax		**339.2**	**388.5**
Tax charge	8	8.4	3.1
Profit for the period attributable to equity shareholders		**330.8**	**385.4**
Net change in unrealised gains/losses on investments	3, 10	(2.0)	2.7
Tax (expense) benefit on net change in unrealised gains/losses on investments	10	(0.2)	0.1
Other comprehensive (loss) income	10	**(2.2)**	**2.8**
Total comprehensive income attributable to equity shareholders		**328.6**	**388.2**
Earnings per share			
Basic	23	$2.08	$2.23
Diluted	23	$1.86	$2.05

Consolidated balance sheet
As at 31 December 2010

	Notes	2010 $m	2009 $m
Assets			
Cash and cash equivalents	9, 19	512.5	440.0
Accrued interest receivable		13.4	12.0
Investments			
- Fixed income securities, available for sale	10, 19	1,719.1	1,892.5
- Other investments	10	(0.2)	-
Reinsurance assets			
- Unearned premiums on premiums ceded	11	2.9	5.6
- Reinsurance recoveries	12	35.9	35.8
- Other receivables	11	5.6	4.3
Deferred acquisition costs	14	61.2	52.9
Other receivables		45.7	4.3
Inwards premiums receivable from insureds and cedants	13	217.5	178.2
Deferred tax asset	15	6.4	3.3
Property, plant and equipment	16	7.4	8.2
Total assets		**2,627.4**	**2,637.1**
Liabilities			
Insurance contracts			
- Losses and loss adjustment expenses	12	507.5	488.9
- Unearned premiums	17	350.6	317.6
- Other payables	17, 18	20.6	15.8
Amounts payable to reinsurers	11, 18	4.4	4.2
Deferred acquisition costs ceded	14	0.1	2.7
Other payables	18	321.4	291.6
Corporation tax payable		6.3	2.4
Interest rate swap	19	0.8	3.6
Long-term debt	19	128.8	131.4
Total liabilities		**1,340.5**	**1,258.2**
Shareholders’ equity			
Share capital	20	84.3	91.2
Own shares	20	(106.9)	(76.4)
Share premium		2.4	2.4
Contributed surplus		662.6	757.0
Accumulated other comprehensive income	10	28.2	30.4
Other reserves	21	70.7	65.3
Retained earnings		545.6	509.0
Total shareholders' equity attributable to equity shareholders		**1,286.9**	**1,378.9**
Total liabilities and shareholders' equity		**2,627.4**	**2,637.1**

The consolidated financial statements were approved by the Board of Directors on 20 February 2011 and signed on its behalf by:

MARTIN THOMAS
DIRECTOR/CHAIRMAN

NEIL McCONACHIE
DIRECTOR/PRESIDENT

Consolidated statement of changes in shareholders' equity

For the year ended 31 December 2010

	Notes	Share capital $m	Own shares $m	Share premium $m	Contributed surplus $m	Accumulated other comprehensive income $m	Other reserves $m	Retained earnings $m	Total $m
Balance as at 31 December 2008		**91.1**	**(58.0)**	**2.4**	**758.2**	**27.6**	**54.3**	**397.1**	**1,272.7**
Total comprehensive income for the year	10	-	-	-	-	2.8	-	385.4	388.2
Shares repurchased and held in treasury	20	-	(16.9)	-	-	-	-	-	(16.9)
Shares repurchased and held in trust	20	-	(8.0)	-	-	-	-	-	(8.0)
Shares distributed by trust	20	-	6.5	-	(6.5)	-	-	-	-
Dividends on common shares	18, 20	-	-	-	-	-	-	(225.0)	(225.0)
Dividends on warrants	18, 20	-	-	-	-	-	-	(48.5)	(48.5)
Equity based compensation - exercises	6, 20, 21	0.1	-	-	5.3	-	(5.4)	-	-
Equity based compensation - expense	6	-	-	-	-	-	16.4	-	16.4
Balance as at 31 December 2009		**91.2**	**(76.4)**	**2.4**	**757.0**	**30.4**	**65.3**	**509.0**	**1,378.9**
Total comprehensive income for the year	10	-	-	-	-	(2.2)	-	330.8	328.6
Shares repurchased and held in treasury	20	-	(32.6)	-	-	-	-	-	(32.6)
Shares repurchased and held in trust	20	-	(13.0)	-	-	-	-	-	(13.0)
Shares repurchased and cancelled	20	(6.9)	-	-	(96.7)	-	-	-	(103.6)
Shares distributed by trust	20	-	16.6	-	(16.6)	-	-	-	-
Shares donated to trust	24	-	(1.5)	-	1.5	-	-	-	-
Dividends on common shares	18, 20	-	-	-	-	-	-	(237.2)	(237.2)
Dividends on warrants	18, 20	-	-	-	-	-	-	(57.0)	(57.0)
Equity based compensation - tax	15	-	-	-	-	-	2.0	-	2.0
Equity based compensation - exercises	6, 20, 21	-	-	-	17.7	-	(17.7)	-	-
Equity based compensation - expense	6	-	-	-	(0.3)	-	21.1	-	20.8
Balance as at 31 December 2010		**84.3**	**(106.9)**	**2.4**	**662.6**	**28.2**	**70.7**	**545.6**	**1,286.9**

Statement of consolidated cash flows

For the year ended 31 December 2010

	Notes	2010 $m	2009 $m
Cash flows from operating activities			
Profit before tax		339.2	388.5
Tax paid		(5.8)	(2.7)
Depreciation	5	2.6	0.8
Interest expense on long-term debt	7	5.4	6.4
Interest income		(68.3)	(64.7)
Net amortisation of fixed income securities		11.0	5.3
Equity based compensation	6	21.1	16.4
Foreign exchange (gains) losses		(2.1)	(2.3)
Net other investment income		(0.1)	(0.3)
Net realised (gains) losses and impairments	3	(33.2)	(23.8)
Net unrealised gain on interest rate swaps		(2.8)	(1.3)
Changes in operational assets and liabilities			
- Insurance and reinsurance contracts		9.0	(32.6)
- Other assets and liabilities		(7.2)	(11.3)
Net cash flows from operating activities		**268.8**	**278.4**
Cash flows from (used in) investing activities			
Interest received		66.9	62.8
Net purchase of property, plant and equipment		(2.3)	(7.6)
Purchase of fixed income securities		(2,635.5)	(2,711.6)
Proceeds on maturity and disposal of fixed income securities		2,828.5	2,440.8
Proceeds on disposal of equity securities		-	4.8
Proceeds on disposal of other investments		1.6	0.1
Net cash flows from (used in) investing activities		**259.2**	**(210.7)**
Cash flows used in financing activities			
Interest paid		(5.4)	(6.4)
Dividends paid	20	(293.2)	(10.5)
Shares repurchased	20	(149.5)	(24.9)
Net cash flows used in financing activities		**(448.1)**	**(41.8)**
Net increase in cash and cash equivalents		**79.9**	**25.9**
Cash and cash equivalents at beginning of period		440.0	413.6
Effect of exchange rate fluctuations on cash and cash equivalents		(7.4)	0.5
Cash and cash equivalents at end of period	9	**512.5**	**440.0**

Summary of significant accounting policies

The basis of preparation, consolidation principles and significant accounting policies adopted in the preparation of LHL and the Group's consolidated financial statements are set out below.

Basis of preparation

The Group's consolidated financial statements are prepared in accordance with accounting principles generally accepted under IFRS as adopted by the European Union.

Where IFRS is silent, as it is in respect of the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, the Group determines appropriate measurement bases, to provide the most useful information to users of the consolidated financial statements, using their judgement and considering U.S. GAAP.

All amounts, excluding share data or where otherwise stated, are in millions of U.S. dollars.

While a number of new or amended IFRS and IFRIC standards have been issued there are no standards that have had a material impact on the Group.

IFRS 9, Financial Instruments: Classification and Measurement, which has been issued but is not yet effective, has not been early adopted by the Group. The Group continues to apply IAS 39, Financial Instruments: Recognition and Measurement and classifies its fixed income securities as available for sale. The new standard is not expected to have a material impact on the results and disclosures reported in the consolidated financial statements. It would, however, result in a re-classification of fixed income securities from available for sale to estimated fair value through profit or loss and a re-classification of the net change in unrealised gains and losses on investments from accumulated other comprehensive income to income.

IFRS 4, Insurance Contracts, issued in March 2004, specifies the financial reporting for insurance contracts by an insurer. The current standard is Phase I in the IASB's insurance contract project and, as noted above, does not specify the recognition or measurement of insurance contracts. This will be addressed in Phase II of the IASB's project and a standard is scheduled to be released in 2011, with potential implementation in 2013. It will include a number of significant changes regarding the measurement and disclosure of insurance contracts. The Group will continue to monitor the progress of the project in order to assess any potential impacts the new standard will have on its results and the presentation and disclosure thereof.

The consolidated balance sheet of the Group is presented in order of decreasing liquidity.

Use of estimates

The preparation of financial statements in conformity with IFRS requires the Group to make estimates and assumptions that affect the reported and disclosed amounts at the balance sheet date and the reported and disclosed amounts of revenues and expenses during the reporting period. Actual results may differ materially from the estimates made.

The most significant estimate made by management is in relation to losses and loss adjustment expenses. This is discussed on pages 12 and 13 and also in the risk disclosures section from page 24. Estimates in relation to losses and loss adjustment expenses recoverable are discussed on page 12.

Estimates may also be made in determining the estimated fair value of certain financial instruments. These are discussed on pages 13 and 14 and in note 10. Management judgement is applied in determining impairment charges.

Basis of consolidation

The Group's consolidated financial statements include the assets, liabilities, shareholders' equity, revenues, expenses and cash flows of LHL and its subsidiaries. A subsidiary is an entity in which the Group owns, directly or indirectly, more than 50% of the voting power of the entity or otherwise has the power to govern its operating and financial policies. The results of subsidiaries acquired are included in the consolidated financial statements from the date on which control is transferred to the Group. Intercompany balances, profits and transactions are eliminated.

Subsidiaries' accounting policies are consistent with the Group's accounting policies.

Foreign currency translation

The functional currency, which is the currency of the primary economic environment in which operations are conducted, for all Group entities is U.S. dollars. Items included in the financial statements of each of the Group's entities are measured using the functional currency. The consolidated financial statements are also presented in U.S. dollars.

Foreign currency transactions are recorded in the functional currency for each entity 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 translated at period end exchange rates. The resulting exchange differences on translation are recorded in the consolidated statement of comprehensive income. Non-monetary assets and liabilities carried at historical cost denominated in a foreign currency are translated at historic rates. Non-monetary assets and liabilities carried at estimated fair value denominated in a foreign currency are translated at the exchange rate at the date the estimated fair value was determined, with resulting exchange differences recorded in accumulated other comprehensive income in shareholders' equity.

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 date that the contract is bound. The Group writes both excess of loss and pro-rata (proportional) contracts. For the majority of excess of loss contracts, written premium is 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, written premium is recognised based on estimates of ultimate premiums provided by the insureds or ceding companies. Initial estimates of written premium are recognised in the period in which the contract is bound. 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 are earned rateably 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 written premiums when a specific loss event occurs. Reinstatement premiums are not recorded for losses included within the provision for IBNR which 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 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 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 entered into. Outwards reinsurance premiums are accounted for in the period in which the contract is bound. The provision for 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 the underlying losses.

The Group monitors the credit-worthiness 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, including the provision for IBNR and related expenses. Losses and loss adjustment expenses are charged to income as they are incurred.

A significant portion of the Group's business is in classes with high attachment points of coverage, including property catastrophe. Reserving for losses in such programs is inherently complicated in that losses in excess of the attachment level of the Group'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. In addition, the Group has limited past loss experience, which increases the inherent uncertainty in estimating ultimate loss levels.

Losses and loss adjustment expenses represent the estimated ultimate cost of settling all losses and loss adjustment expenses arising from events which have occurred up to the balance sheet date, including a provision for IBNR. The Group does not discount its liabilities for unpaid losses. Outstanding losses are initially set on the basis of reports of losses received from third parties. ACRs are determined where the Group's estimate of the reported loss is greater than that reported. 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 own loss experience, historical insurance industry loss experience, underwriters' experience, estimates of pricing adequacy trends and management's professional judgement.

The estimation of the ultimate liability arising 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 Group, together with the potential for unforeseen adverse developments, could lead to a material change in losses and loss adjustment expenses.

Liability adequacy tests

At each balance sheet date, the Group performs a liability adequacy test 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 Group'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.

Financial instruments

Cash and cash equivalents

Cash and cash equivalents are carried in the consolidated 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 Group's fixed income securities are quoted investments that are classified as available for sale and are carried at estimated fair value. The classification is determined at the time of initial purchase and depends on the category of investment. Investments with an embedded conversion option are designated as at estimated fair value through profit and loss. Movements in estimated fair value relate primarily to the option component.

Regular way purchases and sales of investments are recognised at estimated fair value less transaction costs on the trade date and are subsequently carried at estimated fair value. Estimated fair value of quoted investments is determined based on bid prices from recognised exchanges, broker-dealers, recognised indices or pricing vendors. Investments are derecognised when the Group has transferred substantially all of the risks and rewards of ownership. Realised gains and losses are included in income in the period in which they arise. Unrealised gains and losses from changes in estimated fair value of available for sale investments are included in accumulated other comprehensive income in shareholders' equity.

On derecognition of an investment, previously recorded unrealised gains and losses are removed from accumulated other comprehensive income in shareholders' equity and included in current period income.

Amortisation and accretion of premiums and discounts on available for sale fixed income 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 estimated fair value due to its short-term nature and high liquidity.

The Group reviews the carrying value of its available for sale investments for evidence of impairment. An investment is impaired if its carrying value exceeds the estimated fair value and there is objective evidence of impairment to the asset. Such evidence would include a prolonged decline in estimated 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 estimated fair value is removed from accumulated other comprehensive income in shareholders' equity and charged to current period income. Impairment losses on fixed income securities may be subsequently reversed through income.

Derivative financial instruments
Derivatives are recognised at estimated fair value on the date a contract is entered into, the trade date, and are subsequently carried at estimated fair value. Derivative instruments with a positive estimated fair value are recorded as derivative financial assets and those with a negative estimated 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. Estimated 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 estimated fair value of instruments that do not qualify for hedge accounting are recognised in current period income. The Group does not hold any derivatives classified as hedging instruments. 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 consolidated 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 Group has transferred substantially all of the risks and rewards of ownership or the liability is discharged, cancelled or expired.

Long-term debt
Long-term debt is recognised initially at fair value, net of transaction costs incurred. Thereafter it is held at amortised cost, with the amortisation calculated using the effective interest rate method. Derecognition occurs when the obligation has been extinguished.

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	33% per annum
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 consolidated statement of comprehensive income. Costs for repairs and maintenance are charged to income as incurred.

Leases

Rentals payable under operating leases are charged to income on a straight-line basis over the lease term.

Employee benefits

Equity compensation plans

The Group currently operates an RSS under which nil-cost options have been granted. The Group has also operated a management warrant plan and an LTIP option plan in the past. 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, adjusted for the impact of any non-market vesting conditions. No adjustment to vesting assumptions is made in respect of market vesting conditions.

At each balance sheet date, the Group revises its estimate of the number of RSS nil-cost options, LTIP options and warrants that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of comprehensive income, and a corresponding adjustment is made to other reserves in shareholders' equity over the remaining vesting period.

On exercise, the differences between the expense charged to the consolidated statement of comprehensive income and the actual cost to the Group is transferred to contributed surplus. Where new shares are issued, the proceeds received are credited to share capital and share premium.

Pensions

The Group operates a defined contribution plan. On payment of contributions to the plan there is no further obligation to the Group. Contributions are recognised as employee benefits in the consolidated statement of comprehensive income in the period to which they relate.

Tax

Income tax represents the sum of the tax currently payable and any deferred tax. The tax payable is calculated based on taxable profit for the period. Taxable profit for the period can differ from that reported in the consolidated statement of comprehensive income due to certain items which are not tax deductible or which are deferred to subsequent periods.

Deferred tax is recognised on temporary differences between the assets and liabilities in the consolidated balance sheet and their tax base. Deferred tax assets or liabilities are accounted for using the balance sheet liability method. Deferred tax assets are recognised to the extent that realising the related tax benefit through future taxable profits is likely.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

Where the current estimated fair value of equity based compensation awards exceeds the estimated fair value at the time of grant, adjusted where applicable for dividends, the related corporation tax and deferred tax charge or credit is recognised directly in other reserves.

Own shares

Own shares include shares repurchased under share repurchase authorisations and held in treasury plus shares repurchased and held in trust for the purposes of employee equity based compensation schemes. Own shares are deducted from shareholders' equity. No gain or loss is recognised on the purchase, sale, cancellation or issue of own shares and any consideration paid or received is recognised directly in equity.

Risk disclosures: introduction

The Group is exposed to risks from several sources. These include insurance risk, market risk, liquidity risk, credit risk, operational risk and strategic risk. The primary risk to the Group is insurance risk.

The primary objective of the Group's ERM is to ensure that the amount of capital held is consistent with the risk profile of the Group and therefore that the balance between risk and reward is considered as part of all of key business decisions. The Group has formulated, and keeps under review, a risk appetite which is set by the Board of Directors. The Group's appetite to risk will vary marginally from time to time to reflect the potential risks and rewards that present themselves. However, protecting the Group's capital and providing investors with a superior risk-adjusted return over the long term are constants. The risk appetite of the Group 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 Group and an operating entity level. Risk tolerances are the maximum amount of capital that the Group and its entities are prepared to expose to certain risks.

The Group's Board of Directors is responsible for setting and monitoring Group risk tolerances whereas the Risk Committees of the individual entities are responsible for setting and monitoring entity level risk tolerances. All risk tolerances are subject to at least an annual review and consideration by the respective Boards of Directors or Risk Committees. The Group and individual entity Boards of Directors review actual risk levels versus tolerances, emerging risks and any risk learning events quarterly. In addition, usually on a fortnightly basis, management reviews the output from BLAST in order to assess modeled potential losses against risk tolerances and ensure that risk levels are managed in accordance with them.

The primary role of the CRO is to facilitate the effective operation of ERM throughout the Group at all levels. Responsibility for the management of individual risks has been assigned to, and forms part of the performance objectives of, the risk owners within the business. Each quarter risk owners affirm the status of their risks and the effectiveness of the controls that mitigate them. They also ensure that these risks and controls are consistent with their day to day processes and the entries made in the Group and subsidiary Risk Registers, which are a direct input to BLAST. The CRO provides regular reports to the business outlining the status of the Group's ERM activities and strategy, as well as formal reports to the Boards of Directors of the operating entities and the Group in this regard.

Internal audit

Internal audit plays a key role by providing an independent opinion regarding the accuracy and completeness of risks, in addition to verification of the effectiveness of controls. Internal audit's roles and responsibilities are clearly defined through the Internal Audit Charter. The head of internal audit reports directly to the Group Audit Committee. The CRO receives a copy of each internal audit report and considers the findings and agreed actions in the context of the risk appetites and tolerances, plus the risk policies and risk management strategy of each area. The integration of internal audit and ERM into the business helps facilitate the Group's management in the protection of its assets and reputation.

Economic capital model

The foundation of the Group's risk based capital approach to decision making is its economic capital model, BLAST, which is based on the widely accepted economic capital modeling tool, ReMetrica. Management uses BLAST primarily for monitoring its insurance risks. However, BLAST is also used to monitor the entire spectrum of risks including market, credit and operational risks.

BLAST produces data in the form of a stochastic distribution for all classes, including non-elemental classes. The distribution includes the mean outcome and the result at various return periods, including very remote events. BLAST includes the calculation of present and projected financial outcomes for each insurance class, and also recognises diversification credit. This arises as individual risks are generally not strongly correlated and are unlikely to all produce profits or losses at the same time. Diversification credit is calculated within categories or across a range of risk categories, with the most significant impact resulting from insurance risks. BLAST also measures the Group's aggregate insurance exposures. It therefore helps senior management and the Board of Directors determine the level of capital required to meet the combined risk from a wide range of categories. Assisted by BLAST, the Group seeks to achieve an improved risk-adjusted return over time.

BLAST is used in strategic underwriting decisions as part of the Group's annual planning process and to assist in portfolio optimisation decisions. Management also utilises BLAST in assessing the impact of strategic decisions on individual classes of business that the Group writes, or is considering writing, as well as the overall resulting financial impact to the Group. BLAST output is reviewed, including the anticipated loss curves, combined ratios and risk-adjusted profitability, to determine profitability and risk tolerance headroom by class.

The six primary risk categories listed above are discussed in detail below.

A. Insurance risk

The Group underwrites worldwide short-tail insurance and reinsurance contracts that transfer insurance risk, including risks exposed to both natural and man-made catastrophes. The Group'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 by capacity and recent loss events, amongst other factors. The Group'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.

The Group considers insurance risk at an individual contract level, at a sector level, a geographic level and at an aggregate portfolio level to ensure careful risk selection, limits on concentration and appropriate portfolio diversification are accomplished. The Group's four principal classes, or lines, are property, energy, marine and aviation. These classes are deemed to be the Group's operating segments. The level of insurance risk tolerance per class per occurrence and in aggregate is set by the Risk Committees and ultimately approved by the Board of Directors.

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

- The Group 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 and reviewed on an on-going basis;
- BLAST is used to measure occurrence risks, aggregate risks and correlations between classes;
- Each authorised class has a pre-determined normal maximum line structure;
- The Group has pre-determined tolerances on probabilistic and deterministic losses of capital for certain single events and aggregate losses over a period of time;
- Risk levels versus tolerances are monitored on a regular basis;
- A daily underwriting meeting is held to peer review insurance proposals, opportunities and emerging risks;
- Sophisticated pricing models are utilised in certain areas of the underwriting process, and are updated frequently;
- BLAST and other computer modeling tools are deployed to simulate catastrophes and resultant losses to the portfolio and the Group; and
- Reinsurance may be purchased to mitigate both frequency and severity of losses on a treaty or facultative basis.

The Group also maintains targets for the maximum proportion of capital, including long-term debt, that can be lost in a single extreme event or a combination of events.

Some of the Group's business provides coverage for natural catastrophes (i.e. hurricanes, earthquakes and floods) and is subject to potential seasonal variation. A proportion of the Group'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 Group's loss experience. The North American and Japanese wind seasons are typically June to November and the European wind season November to March. The Group also bears exposure to large losses arising from other non-seasonal natural catastrophes, such as earthquakes, from risk losses throughout the year and from war, terrorism and political risk and other events.

The Group's exposures to certain events, as a percentage of capital, including long-term debt, are shown below. Net loss estimates are before income tax and net of reinstatement premiums and outwards reinsurance.

As at 31 December 2010		**$m**	**% of capital**	**$m**	**% of capital**
Zones	**Perils**	**100 year return period estimated net loss**		**250 year return period estimated net loss**	
Gulf of Mexico [1]	Hurricane	250.7	17.7	352.8	24.9
Japan	Earthquake	130.9	9.2	225.6	15.9
Pan-European	Windstorm	141.1	10.0	214.6	15.2
Pacific North West	Earthquake	56.9	4.0	209.0	14.8
Japan	Typhoon	92.8	6.6	191.5	13.5
California	Earthquake	110.9	7.8	186.3	13.2

[1] Landing hurricane from Florida to Texas.

As at 31 December 2009		$m	% of capital	$m	% of capital
Zones	**Perils**	**100 year return period estimated net loss**		**250 year return period estimated net loss**	
Gulf of Mexico [1]	Hurricane	278.5	18.4	391.2	25.9
Japan	Earthquake	138.2	9.2	236.1	15.6
Pan-European	Windstorm	163.2	10.8	261.7	17.3
Pacific North West	Earthquake	48.5	3.2	215.6	14.3
Japan	Typhoon	86.3	5.7	170.8	11.3
California	Earthquake	190.1	12.6	292.6	19.4

(1) Landing hurricane from Florida to Texas.

There can be no guarantee that the modeled assumptions and techniques deployed in calculating these figures are accurate. There could also be an unmodeled loss which exceeds these figures. In addition, any modeled loss scenario could cause a larger loss to capital than the modeled expectation.

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

	2010		2009	
	$m	**%**	**$m**	**%**
Worldwide offshore	301.4	43.7	227.3	36.2
U.S. and Canada	135.9	19.7	158.3	25.2
Worldwide, including the U.S. and Canada [1]	112.7	16.4	119.2	19.0
Europe	43.5	6.3	36.2	5.8
Worldwide, excluding the U.S. and Canada [2]	40.9	5.9	35.6	5.7
Far East	16.6	2.4	13.2	2.1
Middle East	6.8	1.0	11.9	1.9
Rest of world	31.3	4.6	26.1	4.1
Total	**689.1**	**100.0**	**627.8**	**100.0**

(1) Worldwide, including the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area.
(2) Worldwide, excluding the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area, but that specifically exclude the U.S. and Canada.

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

	2010		2009	
	$m	**%**	**$m**	**%**
Property	323.6	46.9	317.3	50.5
Energy	238.3	34.6	175.5	28.0
Marine	76.4	11.1	73.7	11.7
Aviation	50.8	7.4	61.3	9.8
Total	**689.1**	**100.0**	**627.8**	**100.0**

Further details of the gross premiums written and the risks associated with each of these four principal lines of business are described on the following pages.

i. Property

Gross premiums written, for the year:

	2010 $m	2009 $m
Property catastrophe excess of loss	98.1	76.3
Terrorism	77.8	69.1
Property direct and facultative	64.8	88.6
Property retrocession	52.4	61.2
Property political risk	29.1	15.5
Other property	1.4	6.6
Total	**323.6**	**317.3**

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.

Terrorism business is written on an excess of loss basis and can be written either ground up (i.e. the insured does not retain a deductible) or for primary or high excess layers, with cover provided for U.S. and worldwide property risks, but excluding nuclear, chemical and biological 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. Some national pools are also written, which may include nuclear, chemical and biological coverage.

Property direct and facultative business is typically written on a first loss basis (i.e. for a limit smaller than the total insured values), on an excess of loss basis, where the exposure is excess of a deductible retained by the insured plus lower layers of coverage provided by other (re)insurers. Cover is generally provided to medium to large commercial and industrial enterprises with high value locations for non-elemental perils, including fire and explosion, and elemental (natural catastrophe) perils which can include flood, windstorm, earthquake, brush fire, tsunami and tornado. Not all risks include both elemental and non-elemental coverage. Coverage usually includes indemnification for both property damage and business interruption.

Property retrocession is written on an excess of loss basis through treaty arrangements and covers elemental risks.

Property political risk cover is generally written on a ground up excess of loss basis, on an individual case by case basis, and coverage can vary significantly between policies. Within the political risk class the Group also offers cover for sovereign and quasi-sovereign obligor credit risk. The Group does not currently write private obligor trade credit.

The Group is exposed to large natural catastrophic losses, such as windstorm and earthquake loss, primarily from assuming property catastrophe excess of loss and property retrocession portfolio risks but also from its property direct and facultative portfolio. Exposure to such events is controlled and measured by setting limits on aggregate exposures in certain classes per geographic zone and through loss modeling. The accuracy of the latter exposure analysis is limited by the quality of data and effectiveness of the modeling. It is possible that a catastrophic event significantly exceeds the expected modeled event loss. The Group's appetite and exposure guidelines to large losses are set out on page 19.

Reinsurance may be purchased to mitigate exposures to large natural catastrophe losses in the U.S. and Canada. Reinsurance may also be purchased to reduce the Group's worldwide exposure to large risk losses.

ii. Energy

Gross premiums written, for the year:

	2010 $m	2009 $m
Worldwide offshore energy	123.1	100.5
Gulf of Mexico offshore energy	87.4	53.8
Construction energy	12.2	10.7
Onshore energy	6.9	7.8
Energy excess of loss	5.4	-
Other energy	3.3	2.7
Total	**238.3**	**175.5**

Energy risks are written mostly on a direct excess of loss basis and may be ground up or for primary or excess layers. Worldwide offshore 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 occasionally elemental risks. Individual assets covered can be high value and are therefore mostly written on a subscription basis.

Gulf of Mexico offshore energy programs cover elemental and non-elemental risks. Most policies have sub-limits on coverage for elemental losses. The largest exposure is from hurricanes in the Gulf of Mexico. Exposure to such events is controlled and measured through loss modeling. The accuracy of this exposure analysis is limited by the quality of data and effectiveness of the modeling. It is possible that a catastrophic event significantly exceeds the expected modeled event loss. The Group's appetite and exposure guidelines to large losses are set out on page 19.

Construction energy contracts generally cover all risks of platform and drilling units under construction.

Onshore energy risks can include onshore Gulf of Mexico and worldwide energy installations and are largely subject to the same loss events as described above.

Energy excess of loss currently consists of excess of loss and industry loss warranty covers protecting underlying energy reinsurance portfolios.

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.

iii. Marine

Gross premiums written, for the year:

	2010 $m	2009 $m
Marine hull and total loss	31.7	25.6
Marine hull war	16.9	20.0
Marine builders risk	14.6	16.7
Marine P&I clubs	11.9	10.0
Other marine	1.3	1.4
Total	**76.4**	**73.7**

With the exception of the marine P&I clubs where excess layers are written, most policies are written on a ground up basis. 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 hull war is direct insurance of loss of vessels from war, piracy or terrorist attack. Marine builders risk covers the building of ocean going vessels in specialised yards worldwide. Marine P&I is mostly the reinsurance of the International Group of Protection and Indemnity Clubs and covers marine liabilities. Marine cargo programs are not normally written.

The largest expected exposure in the marine class is from physical loss rather than from elemental loss events.

Reinsurance may be purchased to reduce the Group's exposure to both large risk losses and an accumulation of smaller, attritional losses.

iv. Aviation

Gross premiums written, for the year:

	2010 $m	2009 $m
AV52	42.6	52.9
Other aviation	8.2	8.4
Total	**50.8**	**61.3**

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, excluding U.S. commercial airlines and certain other countries whose governments provide a backstop coverage. Other aviation business includes aviation hull war risks and contingent hull, which the Group writes from time to time. The Group does not presently write general aviation business, including hull and liabilities.

Reinsurance may be purchased to mitigate exposures to an AV52 event loss.

Reinsurance

The Group, 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 Group of its obligations to policyholders. Under the Group's reinsurance security policy, reinsurers are assessed and approved as appropriate security based on their financial strength ratings, amongst other factors. The GRSC has defined limits by reinsurer by rating and with an aggregate exposure to a rating band. The GRSC considers reinsurers that are not rated or do not fall within the pre-defined rating categories on a case by case basis, and would usually require collateral to be posted to support such obligations. The GRSC monitors the credit-worthiness of its reinsurers on an ongoing basis and meets formally at least quarterly.

Reinsurance protection is typically purchased on an excess of loss basis and occasionally includes industry loss warranty covers. The mix of reinsurance cover is dependent on the specific loss mitigation requirements, market conditions and available capacity. The structure varies between types of peril and subclass. The Group regularly reviews its catastrophe exposures and may purchase reinsurance in order to reduce the Group's net exposure to a large natural catastrophe loss and/or to reduce net exposures to other large losses. The Group can purchase both facultative and treaty reinsurance. There is no guarantee that reinsurance coverage will be available to meet all potential loss circumstances, as it is possible that the cover purchased is not sufficient. Any loss amount which exceeds the program would be retained by the Group. Some parts of the reinsurance program 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 loss and loss adjustment expense reserves. The estimation of the ultimate liability arising from claims made under insurance and reinsurance contracts is a critical estimate for the Group.

Under generally accepted accounting principles, 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 reserves are reported on an undiscounted basis.

Loss and loss adjustment expense reserves are maintained to cover the Group's estimated liability for both reported and unreported claims. Reserving methodologies that calculate a point estimate for the ultimate losses are utilised, and then a range is developed around these point estimates. The point estimate represents management's best estimate of ultimate loss and loss adjustment expenses. The Group's internal actuaries review the reserving assumptions and methodologies on a quarterly basis with loss estimates being subject to a quarterly corroborative review by independent actuaries, using U.S. generally accepted actuarial principles. This independent review is presented to the Group's Audit Committee. The Group has also established Large Loss and Reserve Committees at the operating entity level, which have responsibility for the review of large claims, their development and any changes in reserving methodology and assumptions.

The extent of reliance on management's judgement in the reserving process differs as to 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 on a pro-rata basis. Over a typical annual period, the Group expects to write the large majority of programs on a direct excess of loss basis. The Group does not currently write a significant amount of long-tail business.

Insurance versus reinsurance
Loss reserve calculations for direct insurance business are not precise in that they deal with the inherent uncertainty of future contingent events. Estimating loss reserves requires management to make 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. These estimates and judgements are based on numerous factors, and may be revised as additional experience or other data becomes available or reviewed as new or improved methodologies are developed or as current laws change.

Furthermore, as a broker market reinsurer, management must rely on loss information reported to brokers by other insurers 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 the estimation of the ultimate losses.

Short-tail versus long-tail
In general, claims relating to short-tail property risks, such as the majority of risks underwritten by the Group, are reported more promptly by third parties than those relating to long-tail risks, including the majority of casualty risks. However, 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 or with reinsurers.

Excess of loss versus proportional
For excess of loss business, management are 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, generally an initial estimated loss and loss expense ratio is used, 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 to the broker and then to the reinsurer. Also, the combination of low claims frequency and high severity 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 lag.

Uncertainty
As a result of the time lag described above, an estimation must be made of IBNR reserves, which consist 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. Because of 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 Group 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, with a consequent impact on reserving. The claims count on the types of insurance and reinsurance that the Group writes, which are low frequency and high severity in nature, is generally low.

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 Group is notified of changes to loss estimates.

As at 31 December 2010 management's estimates for IBNR represented 40.6% of total net loss reserves (2009 - 43.8%). The majority of the estimate relates to potential claims on non-elemental risks where timing delays in insured or cedant reporting may mean losses could have occurred which the Group were not made aware of by the balance sheet date.

B. Market risk

The Group is at risk of loss due to movements in market factors. The main risks include:

i. Insurance risk;
ii. Investment risk;
iii. Debt risk; and
iv. Currency risk.

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

i. Insurance risk

The Group 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; and
- Market events which may cause a limit in the availability of cover, including unusual inflation in rates, causing political intervention or national remedies.

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

- Reviews and amends underwriting plans and budgets as necessary;
- Reduces exposure to market sectors where conditions have reached unattractive levels;
- Purchases appropriate, cost effective reinsurance cover to mitigate exposure;

- Closely monitors changes in rates and terms and conditions; and
- Regularly reviews output from BLAST to assess up-to-date profitability of classes and sectors.

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, amongst other factors, may lead to an adverse impact on the value of the Group's investment portfolio. Investment guidelines are established by the Investment Committee of the Board of Directors to manage this risk. Investment guidelines set parameters within which the Group's external investment managers must operate. Important parameters include guidelines on permissible assets, duration ranges, credit quality and maturity. Compliance with guidelines is monitored on a monthly basis. Any adjustments to the investment guidelines are approved by the Investment Committee and the Board of Directors.

Within the Group guidelines is a sub-set of guidelines for the portion of funds required to meet near term obligations and cash flow needs following an extreme event. The funds to cover this potential liability are designated as the "core" portfolio and the portfolio duration is matched to the duration of the insurance liabilities, within an agreed range. The core portfolio is invested in fixed income securities and cash and cash equivalents. The core portfolio may, at times, contain assets significantly in excess of those required to meet insurance liabilities or other defined funding needs. The sub-set of guidelines adds a further degree of requirements, including fewer allowable asset classes, higher credit quality, shorter duration and higher liquidity. The primary objectives of this portion of assets are capital preservation and providing liquidity to meet insurance and other near term obligations.

Assets in excess of those required to be held in the core portfolio, are typically held in the "core plus" or "surplus" portfolios. The core plus portfolio is invested in fixed income securities and cash and cash equivalents. The surplus portfolio is invested in fixed income securities, derivative instruments and cash and cash equivalents and can also be invested in equity securities. The assets in the core plus and surplus portfolios are not matched to specific insurance liabilities. In general, the duration of the surplus portfolio may be slightly longer than the core or core plus portfolio, while maintaining a focus on high quality assets.

The Group 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 Group's fixed income portfolios are managed by three external investment managers. The equity portfolio was managed by one investment manager and was fully liquidated in the first half of 2009. The performance of the managers is monitored on an on-going basis.

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

As at 31 December 2010	$m	%	$m	%	$m	%	$m	%
	Core		Core plus		Surplus		Total	
Available for sale - external								
- Short-term investments	10.7	0.6	-	-	1.4	0.1	12.1	0.7
- U.S. treasuries	74.7	4.4	43.2	2.5	182.6	10.6	300.5	17.5
- Other government bonds	14.5	0.8	44.3	2.6	122.6	7.1	181.4	10.5
- U.S. municipal bonds	0.1	-	2.4	0.1	8.4	0.5	10.9	0.6
- U.S. government agency debt	8.6	0.5	10.9	0.6	14.9	0.9	34.4	2.0
- Asset backed securities	4.1	0.2	6.5	0.4	9.1	0.5	19.7	1.1
- U.S. government agency mortgage backed securities	24.0	1.4	149.1	8.7	164.4	9.5	337.5	19.6
- Non-agency mortgage backed securities	2.4	0.1	6.1	0.4	8.0	0.5	16.5	1.0
- Non-agency commercial mortgage backed securities	1.2	0.1	8.6	0.5	16.9	1.0	26.7	1.6
- Corporate bonds	113.3	6.6	293.6	17.0	277.0	16.2	683.9	39.8
- Corporate bonds - FDIC guaranteed	34.8	2.0	48.5	2.9	12.2	0.7	95.5	5.6
Total fixed income securities	**288.4**	**16.7**	**613.2**	**35.7**	**817.5**	**47.6**	**1,719.1**	**100.0**

As at 31 December 2009	$m	%	$m	%	$m	%	$m	%
	Core		Core plus		Surplus		Total	
Available for sale - external								
- Short-term investments	164.3	8.7	3.5	0.2	14.5	0.8	182.3	9.7
- U.S. treasuries	49.8	2.6	8.4	0.4	196.6	10.4	254.8	13.4
- Other government bonds	14.0	0.7	-	-	59.8	3.2	73.8	3.9
- U.S. municipal bonds	-	-	-	-	2.5	0.1	2.5	0.1
- U.S. government agency debt	35.1	1.9	10.7	0.6	69.2	3.7	115.0	6.2
- U.S. government agency mortgage backed securities	64.0	3.4	16.4	0.9	404.0	21.3	484.4	25.6
- Corporate bonds	151.0	8.0	11.8	0.6	317.0	16.8	479.8	25.4
- Corporate bonds - FDIC guaranteed	124.3	6.5	5.0	0.3	64.1	3.4	193.4	10.2
Total available for sale - external	**602.5**	**31.8**	**55.8**	**3.0**	**1,127.7**	**59.7**	**1,786.0**	**94.5**
Available for sale - internal								
- Short-term investments	106.5	5.5	-	-	-	-	106.5	5.5
Total fixed income securities	**709.0**	**37.3**	**55.8**	**3.0**	**1,127.7**	**59.7**	**1,892.5**	**100.0**

The sector allocation of the corporate bonds is as follows:

As at 31 December	2010 $m	2010 %	2009 $m	2009 %
Financial	368.3	47.3	344.1	51.1
Industrial	300.3	38.5	262.9	39.1
Utility	64.6	8.3	52.7	7.8
Foreign agencies	34.3	4.4	-	-
Other	11.9	1.5	13.5	2.0
Total	**779.4**	**100.0**	**673.2**	**100.0**

The financial sector allocation includes $95.5 million (2009 - $193.4 million) of FDIC guaranteed bonds.

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

Following the liquidation of its equity portfolio in the first half of 2009, the Group has no exposure to valuation risk from equity securities. The Group's investment portfolio is comprised mainly of fixed income securities. The estimated fair value of the Group's fixed income portfolio is generally inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Group's fixed income securities would tend to rise and vice versa.

The sensitivity of the price of fixed income 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 Group's fixed income and derivative investment portfolio to interest rate movements is detailed below, assuming linear movements in interest rates:

As at 31 December	2010 $m	2010 %	2009 $m	2009 %
Immediate shift in yield (basis points)				
100	(52.5)	(3.1)	(56.7)	(3.0)
75	(39.4)	(2.3)	(42.5)	(2.2)
50	(26.3)	(1.5)	(28.3)	(1.5)
25	(13.1)	(0.8)	(14.2)	(0.7)
(25)	11.9	0.7	10.0	0.5
(50)	23.8	1.4	20.0	1.1
(75)	35.7	2.1	29.9	1.6
(100)	47.6	2.8	39.9	2.1

The Group mitigates interest rate risk on the investment portfolio by establishing and monitoring duration ranges in its investment guidelines. The duration of the core portfolio is matched to the modeled 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 duration of the externally managed portfolios, expressed in years, is as follows:

As at 31 December	2010	2009
Core portfolio	1.7	1.6
Core plus portfolio	2.1	1.9
Surplus portfolio	3.7	3.2
Overall portfolio	**2.8**	**2.6**

The overall duration for fixed income and managed cash and cash equivalents is 2.2 years (2009 - 2.3 years).

In addition to duration management, the Group uses VaR on a monthly basis 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 modeling to capture the cash flows and embedded optionality of the portfolio. Securities are valued individually using market standard 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.

The principal measure that is produced is a ninety day VaR at the 95th percentile confidence level. Management also monitors the 99th percentile confidence level. The ninety day VaR, at the 95th percentile confidence level, measures the minimum amount the assets should be expected to lose in a ninety day time horizon, under normal conditions, 5% of the time. The current VaR tolerance is 4.0% of shareholders' equity, using the ninety day VaR at the 95th percentile confidence level.

The Group's VaR calculations are as follows:

	2010		2009	
As at 31 December	**$m**	**%**	**$m**	**%**
95th percentile confidence level	34.4	2.7	40.4	2.9
99th percentile confidence level	48.6	3.8	57.0	4.1

Derivative financial instruments

The Group's investment guidelines permit the investment managers to utilise exchange-traded futures and options contracts, interest rate swaps, credit default swaps, interest rate swaptions and forward foreign currency contracts, the latter being non-exchange traded OTC instruments due to their customised nature. Derivatives may be used for yield enhancement, duration management, interest rate and foreign currency exposure management or to obtain an exposure to a particular financial market. These positions are monitored regularly. The Group principally has exposure to derivatives related to the following types of risks: foreign currency risk, interest rate risk and credit risk.

The Group currently invests in the following derivative financial instruments:

a. TBAs;
b. Futures;
c. Options;
d. Forward foreign currency contracts;
e. Swaps; and
f. Swaptions.

These are discussed in detail below.

The net gains or losses on the Group's derivative financial instruments recognised in the consolidated statement of comprehensive income are as follows:

As at 31 December 2010	**$m**	**$m**	**$m**	**$m**
	Net other investment income	**Net realised gains (losses)**	**Net foreign exchange gains (losses)**	**Financing costs**
Eurodollar futures	-	0.8	-	-
Treasury futures	-	0.2	-	-
Forward foreign currency contracts	-	-	0.3	-
Interest rate swaps - investments	(0.1)	-	-	-
Interest rate swaps - debt	-	-	-	(0.3)
Credit default swaps	0.2	-	-	-
Total	**0.1**	**1.0**	**0.3**	**(0.3)**

As at 31 December 2009	**$m**	**$m**	**$m**	**$m**
	Net other investment income	**Net realised gains (losses)**	**Net foreign exchange gains (losses)**	**Financing costs**
Eurodollar futures	-	1.6	-	-
Treasury futures	-	(1.7)	-	-
Options on treasury futures	-	0.2	-	-
Interest rate swaps - debt	-	-	-	(1.3)
Total	**-**	**0.1**	**-**	**(1.3)**

Foreign exchange gains and losses on foreign currency denominated derivatives are included in foreign exchange gains and losses in the consolidated statement of comprehensive income.

The estimated fair value of the Group's derivative instruments is as follows:

As at 31 December	2010 $m Other Investments	2010 $m Interest rate swap	2009 $m Other Investments	2009 $m Interest rate swap
Forward foreign currency contracts	(0.3)	-	-	-
Interest rate swaps - investment	(0.1)	-	-	-
Interest rate swaps - debt	-	(0.8)	-	(3.6)
Credit default swaps	0.2	-	-	-
Total	**(0.2)**	**(0.8)**	**-**	**(3.6)**

a. TBAs
The TBA market is essentially a forward or delayed delivery market for mortgage backed securities issued by U.S. government agencies, where securities of a specific term and interest rate are bought or sold for future settlement on a "to be announced" basis. TBAs are generally physically settled and classified as available for sale fixed income securities. Occasionally TBAs may be traded for net settlement. Such instruments are deemed to be derivative instruments. All TBAs classified as derivatives are held on a non-leveraged basis. The credit exposure is restricted to the differential between the settlement value of the forward purchase and the forward sale. The credit-worthiness of the counter-party is monitored and collateral may be required on open positions.

The estimated fair value of TBA positions as at 31 December 2010 and 2009 is an asset and corresponding liability of $nil.

b. Futures
The Group's investment guidelines only permit the use of futures that are exchange-traded. Such futures provide the Group 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 Group more efficient and less costly access to the exposure than would be available by the exclusive use of individual fixed income 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 Group 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, including: the use of clearing houses (thus reducing counter-party 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.

A Eurodollar futures contract is an exposure to 3 month LIBOR, based on a commitment to a $1.0 million deposit. The estimated fair value is based on expectations of 3 month LIBOR, is determined using exchange-traded prices and was negligible as at 31 December 2010 and 2009. The contracts currently held by the Group will expire throughout 2012.

The sensitivity of the Group's Eurodollar futures position to interest rate movements is detailed below:

As at 31 December	2010 $m	2009 $m
Immediate shift in 3 month LIBOR (basis points)		
100	(0.7)	(1.4)
75	(0.6)	(1.1)
50	(0.4)	(0.7)
25	(0.2)	(0.4)
(25)	0.2	0.4
(50)	0.4	0.7
(75)	0.6	1.1
(100)	0.7	1.4

c. Options

The Group'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 future date, which may or may not be pre-determined. The Group may enter into option contracts that are secured by holdings in the underlying securities or by another means which permits immediate satisfaction of the Group's obligations.

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

d. 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 Group may utilise forward foreign currency contracts to manage the impact of fluctuations in foreign currencies on the value of its foreign currency denominated investments, or to gain exposure to a certain currency or market rate.

Forward contracts expose the Group to credit, market and liquidity risks. Credit risk arises from the potential inability of counter-parties to perform under the terms of the contract. The Group 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 Group 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 counter-party 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.

As at 31 December 2010, the Group had the following open forward foreign currency contracts:

	$m	$m
	Notional receivable	**Notional payable**
Chinese Renminbi	4.0	1.0
Mexican Peso	2.7	3.2
Euro	-	11.2
Other[(1)]	16.2	5.7
Total	**22.9**	**21.1**

(1) Individual currencies included in 'other' have a notional payable or receivable of less than $2.0 million U.S. dollars or equivalent.

There were no open forward foreign currency contracts as at 31 December 2009.

e. Swaps

The Group's investment guidelines permit the use of interest rate swaps and credit default swaps which are traded OTC. These are subject to credit risk on the counter-party's inability to perform. Swaps 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. Swaps are recorded at estimated fair values at the end of each period with unrealised gains and losses recorded in the consolidated statement of comprehensive income.

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 counter-party 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 counter-party credit quality and a maximum notional exposure to interest rate swaps as a percentage of the investment portfolio's estimated fair value.

The Group uses credit default swaps as a way to add or reduce credit risk to an individual issuer, or a basket of issuers, without investing directly in their securities. The Group may also sell credit default protection. As at 31 December 2010, the maximum amount of loss the Group could incur on its open credit default swaps was the notional value of $9.8 million (2009 - $nil).

f. Swaptions

The Group uses swaptions, options on interest rate swaps, to manage interest rate risk exposure and portfolio and yield curve duration. The Group is subject to the credit risk of the counter-party but is only subject to market risk to the extent of the premium paid. As a swaption writer, the Group is not subject to credit risk but is subject to market risk, due to its obligation to make payments under the terms of the contract. These risks are mitigated through maximum allowable notional exposures as a percentage of the investment portfolio's estimated fair value.

iii. Debt risk

The Group has issued long-term debt as described in note 19. The loan notes bear interest at a floating rate that is re-set on a quarterly basis, plus a fixed margin of 3.70%. The Group is subject to interest rate risk on the coupon payments of the long-term debt. The Group has mitigated the interest rate risk by entering into interest rate swap contracts as follows:

	Maturity date	Prepayment date	Interest hedged
Subordinated loan notes $97.0 million	15 December 2035	15 March 2011	50%
Subordinated loan notes €24.0 million	15 June 2035	15 March 2011	50%

The swaps expire on 15 March 2011.

In certain circumstances the subordinated loan notes could have been prepaid from 16 December 2005, with a sliding scale redemption price penalty which reduces to zero by 15 March 2011. Refer to note 19 for further details.

The current Euribor interest rate on 50% of the Euro subordinated loan notes has been set at 1.03% (2009 - 0.71%). The current LIBOR interest rate on 50% of the U.S. dollar subordinated loan notes has been set at 0.30% (2009 - 0.25%). The Group has no interest rate risk on the remaining portion of the notes.

iv. Currency risk

The Group underwrites from two locations, Bermuda and London, although risks are assumed on a worldwide basis. Risks assumed are predominantly denominated in U.S. dollars.

The Group is exposed to currency risk to the extent its assets are denominated in different currencies to its liabilities. The Group is also exposed to non-retranslation risk on non-monetary assets such as unearned premiums and deferred acquisition costs. Exchange gains and losses can impact income.

The Group hedges non-U.S. dollar liabilities primarily with non-U.S. dollar assets. The Group's main foreign currency exposure relates to its insurance obligations, cash holdings, premiums receivable, dividends payable and the €24.0 million subordinated loan notes long-term debt liability. The Group also has exposure to foreign currencies through its EMD investment portfolio. These positions may not be hedged depending on the currency outlook.

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

Assets	$m	$m	$m	$m	$m
	U.S. $	Sterling	Euro	Other	Total
Cash and cash equivalents	141.5	269.8	93.2	8.0	512.5
Accrued interest receivable	13.4	-	-	-	13.4
Fixed income securities, available for sale	1,685.6	-	10.7	22.8	1,719.1
Other investments	0.2	-	(0.2)	(0.2)	(0.2)
Reinsurance assets	44.4	-	-	-	44.4
Deferred acquisition costs	50.1	0.8	6.0	4.3	61.2
Other receivables	41.5	4.2	-	-	45.7
Inwards premiums receivable from insureds and cedants	172.8	3.8	29.2	11.7	217.5
Deferred tax asset	-	6.4	-	-	6.4
Property, plant and equipment	5.7	1.7	-	-	7.4
Total assets as at 31 December 2010	**2,155.2**	**286.7**	**138.9**	**46.6**	**2,627.4**

Liabilities	$m	$m	$m	$m	$m
	U.S. $	Sterling	Euro	Other	Total
Losses and loss adjustment expenses	395.9	9.9	86.6	15.1	507.5
Unearned premiums	296.4	6.5	27.1	20.6	350.6
Insurance contracts - other payables	17.6	0.2	1.6	1.2	20.6
Amounts payable to reinsurers	4.4	-	-	-	4.4
Deferred acquisition costs ceded	0.1	-	-	-	0.1
Other payables	51.9	275.6	0.2	-	327.7
Interest rate swap	0.7	-	0.1	-	0.8
Long-term debt	97.0	-	31.8	-	128.8
Total liabilities as at 31 December 2010	**864.0**	**292.2**	**147.4**	**36.9**	**1,340.5**

Assets	$m	$m	$m	$m	$m
	U.S. $	Sterling	Euro	Other	Total
Cash and cash equivalents	124.9	271.1	37.8	6.2	440.0
Accrued interest receivable	12.0	-	-	-	12.0
Fixed income securities, available for sale	1,892.5	-	-	-	1,892.5
Reinsurance assets	45.7	-	-	-	45.7
Deferred acquisition costs	43.4	1.0	4.6	3.9	52.9
Other receivables	4.0	0.3	-	-	4.3
Inwards premiums receivable from insureds and cedants	143.6	4.8	19.1	10.7	178.2
Deferred tax asset	-	3.3	-	-	3.3
Property, plant and equipment	6.9	1.3	-	-	8.2
Total assets as at 31 December 2009	**2,273.0**	**281.8**	**61.5**	**20.8**	**2,637.1**

Liabilities	$m	$m	$m	$m	$m
	U.S. $	Sterling	Euro	Other	Total
Losses and loss adjustment expenses	445.0	3.6	21.4	18.9	488.9
Unearned premiums	265.8	8.4	22.7	20.7	317.6
Insurance contracts - other payables	12.4	0.2	2.1	1.1	15.8
Amounts payable to reinsurers	4.2	-	-	-	4.2
Deferred acquisition costs ceded	2.7	-	-	-	2.7
Other payables	19.0	274.6	0.4	-	294.0
Interest rate swap	3.0	-	0.6	-	3.6
Long-term debt	97.0	-	34.4	-	131.4
Total liabilities as at 31 December 2009	**849.1**	**286.8**	**81.6**	**40.7**	**1,258.2**

The impact on net income of a proportional foreign exchange movement of 10% up and 10% down against the U.S. dollar at the year end spot rates would be an increase or decrease of $0.2 million (2009 - $0.7 million).

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 Group's main exposures to liquidity risk are with respect to its insurance and investment activities. The Group is exposed if proceeds from financial assets are not sufficient to fund obligations arising from its insurance contracts. The Group can be exposed to daily calls on its available investment assets, principally from insurance claims.

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 amount of claims within a relatively short time-frame;
- 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 Group's fixed income portfolio are as follows:

As at 31 December 2010	**$m**	**$m**	**$m**	**$m**
	Core	**Core plus**	**Surplus**	**Total**
Fixed income securities - external				
Less than one year	48.4	80.1	23.3	151.8
Between one and two years	117.4	142.8	52.9	313.1
Between two and three years	49.7	102.4	76.2	228.3
Between three and four years	25.1	63.4	96.1	184.6
Between four and five years	12.8	42.1	120.3	175.2
Over five years	3.3	12.1	250.3	265.7
Asset backed and mortgage backed securities	31.7	170.3	198.4	400.4
Total	**288.4**	**613.2**	**817.5**	**1,719.1**

As at 31 December 2009	**$m**	**$m**	**$m**	**$m**
	Core	**Core plus**	**Surplus**	**Total**
Fixed income securities - external				
Less than one year	180.4	4.8	29.1	214.3
Between one and two years	120.1	3.5	131.2	254.8
Between two and three years	156.2	15.3	152.0	323.5
Between three and four years	39.8	14.3	70.1	124.2
Between four and five years	38.6	1.5	193.0	233.1
Over five years	3.4	-	148.3	151.7
Mortgage backed securities	64.0	16.4	404.0	484.4
Total fixed income securities - external	**602.5**	**55.8**	**1,127.7**	**1,786.0**
Fixed income securities - internal				
Less than one year	106.5	-	-	106.5
Total	**709.0**	**55.8**	**1,127.7**	**1,892.5**

The maturity profile of the financial liabilities of the Group is as follows:

As at 31 December 2010	$m	$m	$m	$m	$m	$m
		Years until liability becomes due - undiscounted values				
	Balance sheet	Less than one	One to three	Three to five	Over five	Total
Losses and loss adjustment expenses	507.5	191.5	194.3	66.6	55.1	507.5
Insurance contracts - other payables	20.6	17.6	2.8	0.2	-	20.6
Amounts payable to reinsurers	4.4	4.4	-	-	-	4.4
Other payables	321.4	321.4	-	-	-	321.4
Corporation tax payable	6.3	6.3	-	-	-	6.3
Interest rate swap	0.8	0.8	-	-	-	0.8
Long-term debt	128.8	5.0	10.8	10.8	241.1	267.7
Total	**989.8**	**547.0**	**207.9**	**77.6**	**296.2**	**1,128.7**

As at 31 December 2009	$m	$m	$m	$m	$m	$m
		Years until liability becomes due - undiscounted values				
	Balance sheet	Less than one	One to three	Three to five	Over five	Total
Losses and loss adjustment expenses	488.9	183.5	181.7	67.0	56.7	488.9
Insurance contracts - other payables	15.8	12.7	2.4	0.7	-	15.8
Amounts payable to reinsurers	4.2	4.2	-	-	-	4.2
Other payables	291.6	291.6	-	-	-	291.6
Corporation tax payable	2.4	2.4	-	-	-	2.4
Interest rate swap	3.6	2.9	0.7	-	-	3.6
Long-term debt	131.4	5.2	10.7	10.7	243.1	269.7
Total	**937.9**	**502.5**	**195.5**	**78.4**	**299.8**	**1,076.2**

Actual maturities of the above may differ from contractual maturities because certain borrowers have the right to call or pre-pay certain obligations with or without call or prepayment penalties. The prepayment options for the Group's long-term debt are discussed in note 19. 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 Group manages its liquidity risks via its investment strategy to hold high quality, highly liquid securities, sufficient to meet its insurance liabilities and other near term liquidity requirements. The creation of the core portfolio with its subset of guidelines ensures funds are readily available to meet potential insurance liabilities in an extreme event plus other near term liquidity requirements. In addition, the Group 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 Group monitors market changes and outlooks and re-allocates assets as deemed necessary.

D. Credit risk

Credit risk is the risk that a counter-party may fail to pay, or repay, a debt or obligation. The Group is exposed to credit risk on its fixed income 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 income portfolio is mitigated through the Group'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 5% of shareholders' equity, with the exception of U.S. government and agency securities. In addition, no one issuer, with the exception of U.S. government and agency securities, should exceed 5% of shareholders' equity. The Group is therefore not exposed to any significant credit concentration risk on its investment portfolio, except for fixed income securities issued by the U.S. government and government agencies.

Credit risk on exchange-traded derivative instruments is mitigated by the use of exchange-traded instruments which use clearing houses to reduce counter-party credit risk, require the posting of margins and settle unrealised gains and losses daily. Credit risk on OTC derivatives is mitigated by monitoring the credit-worthiness of the counter-parties and by requiring collateral to be posted for positions which are in the money by amounts exceeding predetermined thresholds.

Credit risk on inwards premiums receivable from insureds and cedants is managed by conducting business with reputable broking organisations, with whom the Group has established relationships, and by rigorous cash collection procedures. The Group also has a broker approval process in place. Credit risk from reinsurance recoverables is primarily managed by the review and approval of reinsurer security by the GRSC as discussed on pages 23 and 24.

The table below presents an analysis of the Group's major exposures to counter-party 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 2010	**$m**	**$m**	**$m**	**$m**
	Other investments	**Cash and fixed income securities**	**Inwards premiums receivable and other receivables**	**Reinsurance recoveries**
AAA	-	1,186.0	-	-
AA+, AA, AA-	(0.3)	366.2	-	-
A+, A, A-	0.1	451.3	5.6	35.9
BBB+, BBB, BBB-	-	182.9	-	-
Other	-	45.2	263.2	-
Total	**(0.2)**	**2,231.6**	**268.8**	**35.9**

As at 31 December 2009	$m	$m	$m	$m
	Other investments	Cash and fixed income securities	Inwards premiums receivable and other receivables	Reinsurance recoveries
AAA	-	1,830.6	-	-
AA+, AA, AA-	-	110.8	-	-
A+, A, A-	-	295.9	4.3	35.8
BBB+, BBB, BBB-	-	95.0	-	-
Other	-	0.2	182.5	-
Total	**-**	**2,332.5**	**186.8**	**35.8**

The counter-party to the Group's long-term debt interest rate swap is currently rated AA by S&P.

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

	2010	2009
Less than 90 days past due	8.1	8.6
Between 91 and 180 days past due	0.6	0.4
Over 180 days past due	0.2	0.3
Total	**8.9**	**9.3**

Provisions of $0.6 million (2009 - $1.4 million) have been made for impaired or irrecoverable balances and $0.6 million (2009 - $0.2 million charge) was released to the consolidated statement of comprehensive income in respect of bad debts. No provisions have been made against balances recoverable from reinsurers.

E. Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes or systems. The Group and its subsidiaries have identified and evaluated their key operational risks and these are incorporated in the risk registers and in BLAST. The Group has also established, and monitors compliance with, internal operational risk tolerances.

In order to manage operational risks, the Group has implemented a robust governance framework. Policies and procedures are documented and identify the key risks and controls within processes. The existence and operation of key risks and controls and the adequacy of documented policies and procedures is affirmed by management on a quarterly basis. The Group'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 annual audit, with all other areas audited, on a rotational basis, at least once every three years.

F. Strategic risk

The Group has identified several strategic risks. These include the risks that either the poor execution of the business plan or poor business planning in itself results in a strategy that fails to adequately reflect the trading environment, resulting in an inability to optimise performance. The Group has also identified 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. Lastly, the Group has identified succession planning, staff retention and key man risks as strategic risks.

i. Business plan risks
The Group addresses the risks associated with the planning and execution of the business plan through a combination of the following:

- An iterative annual planning process with cross departmental involvement;
- Approval of the annual business plan by the Board of Directors;
- Regular monitoring of actual versus planned results; and
- Periodic review and re-forecasting as market conditions change.

ii. Capital management risk
The total capital of the Group as at 31 December 2010 is determined as $1,415.7 million (2009 - $1,510.3 million) comprising $1,286.9 million of shareholders' equity (2009 - $1,378.9 million) and $128.8 million of long-term debt (2009 - $131.4 million). The Group's capital requirements vary with the insurance cycle.

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

- Regular monitoring of current regulatory and rating agency capital requirements;
- Oversight of capital requirements by the Board of Directors; and
- Maintaining contact with vendors, regulators and rating agencies in order to stay abreast of upcoming developments.

The Group 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 return to shareholders within pre-determined risk tolerances;
- Maintaining adequate financial strength ratings; and
- Meeting internal and regulatory capital requirements.

Capital is increased or returned as appropriate. The retention of earnings generated leads to an increase in capital. Capital raising can include debt or equity and returns of capital may be made through dividends, share repurchases, a redemption of debt or any combination thereof. Other capital management tools and products available to the Group may also be utilised. 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. Management increasingly uses these approaches in decision making. The operating entities also conduct capital requirement assessments under internal measures and local regulatory requirements. Refer to note 26 for a discussion of the regulatory capital requirements of the Group's operating entities.

The Group's aim is to provide its shareholders with an RoE of 13% in excess of a risk free rate over the insurance cycle. The return is generated within a broad framework of risk parameters.

The return is measured by management in terms of the IRR of the increase in FCBVS in the period adjusted for dividends accrued. This aim is a long-term goal, acknowledging that management expect 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 - adjusting the Group's portfolio to make the most effective use of available capital and seeking to maximise the risk-adjusted return.

IRR achieved is as follows:

	Annual return	**Compound annual return**	**Inception to date return**
31 December 2005 [(1)]	(3.2%)	n/a	(3.2%)
31 December 2006	17.8%	14.0%	14.0%
31 December 2007	31.4%	22.4%	50.3%
31 December 2008	7.8%	17.9%	63.7%
31 December 2009	26.5%	19.8%	105.8%
31 December 2010	23.3%	20.3%	152.4%

[(1)] The returns shown are for the period from the date of incorporation, 12 October 2005, to 31 December 2005.

IRR achieved in excess of the 3 month treasury yield is as follows:

	Annual return	**Compound annual return**	**Inception to date return**
31 December 2005 [(1)]	(3.4%)	n/a	(3.4%)
31 December 2006	13.0%	9.2%	9.2%
31 December 2007	26.9%	17.8%	40.8%
31 December 2008	6.4%	14.3%	52.7%
31 December 2009	26.4%	17.1%	94.6%
31 December 2010	23.2%	18.2%	141.1%

[(1)] The returns shown are for the period from the date of incorporation, 12 October 2005, to 31 December 2005.

iii. Retention risks

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;
- Documented recruitment procedures, position descriptions and employment contracts; and
- Resource monitoring and the provision of appropriate compensation and training schemes.

1. General information

The Group is a provider of global property insurance and reinsurance products. LHL was incorporated under the laws of Bermuda on 12 October 2005. On 16 March 2009 LHL was listed on the main market of the LSE; previously LHL was listed on AIM, a subsidiary market of the LSE. A secondary listing on the BSX was approved on 21 May 2007. The registered office is Power House, 7 Par-la-Ville Road, Hamilton HM 11, Bermuda.

LHL has five subsidiaries, all wholly owned: LICL, LIHL, LIMSL, LISL and LMEL. LIHL is a holding company for a wholly owned operating subsidiary, LUK.

The subsidiaries were incorporated and licensed as insurance companies or intermediaries as follows:

	Date of incorporation	Licensing body	Nature of business
LICL	28 October 2005	BMA	General insurance business
LIHL	11 April 2006	None	Holding company
LUK	17 March 2006	FSA	General insurance business
LIMSL	7 October 2005	FSA	Insurance mediation activities
LISL	17 March 2006	None	Support services
LMEL	11 March 2007	DFSA	Insurance mediation activities

2. Segmental reporting

Management and the Board of Directors review the Group's business primarily by its four principal classes: property, energy, marine and aviation. These classes are therefore deemed to be the Group’s operating segments for the purposes of segment reporting. Further subclasses 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 21 to 23. Operating segment performance is measured by the net underwriting profit or loss and the combined ratio.

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

Revenue and expense by operating segment - for the year ended 31 December 2010

Gross premiums written	**$m**	**$m**	**$m**	**$m**	**$m**
	Property	**Energy**	**Marine**	**Aviation**	**Total**
(Analysed by geographical region)					
Worldwide offshore	1.2	225.0	75.2	-	301.4
U.S. and Canada	133.3	2.6	-	-	135.9
Worldwide, including the U.S. and Canada (1)	53.9	7.6	0.5	50.7	112.7
Europe	42.9	0.3	0.2	0.1	43.5
Worldwide, excluding the U.S. and Canada (2)	40.6	0.2	0.1	-	40.9
Far East	15.9	0.3	0.4	-	16.6
Middle East	6.1	0.7	-	-	6.8
Rest of world	29.7	1.6	-	-	31.3
Total	**323.6**	**238.3**	**76.4**	**50.8**	**689.1**
Outwards reinsurance premiums	(18.9)	(13.9)	(0.9)	(5.5)	(39.2)
Change in unearned premiums	5.3	(38.8)	(6.9)	7.4	(33.0)
Change in unearned premiums ceded	1.7	(2.3)	(1.8)	(0.3)	(2.7)
Net premiums earned	**311.7**	**183.3**	**66.8**	**52.4**	**614.2**
Insurance losses and loss adjustment expenses	(108.7)	(66.0)	(25.8)	5.8	(194.7)
Insurance losses recoverable	-	29.0	-	-	29.0
Insurance acquisition expenses	(38.8)	(39.7)	(19.3)	(12.1)	(109.9)
Insurance acquisition expenses ceded	0.5	2.8	0.1	0.2	3.6
Net underwriting profit	**164.7**	**109.4**	**21.8**	**46.3**	**342.2**
Net unallocated income and expenses					(3.0)
Profit before tax					**339.2**
Loss ratio	34.9%	20.2%	38.6%	(11.1%)	27.0%
Acquisition cost ratio	12.3%	20.1%	28.7%	22.7%	17.3%
Expense ratio	-	-	-	-	10.1%
Combined ratio	**47.2%**	**40.3%**	**67.3%**	**11.6%**	**54.4%**

(1) Worldwide, including the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area.
(2) Worldwide, excluding the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area, but that specifically exclude the U.S. and Canada.

Revenue and expense by operating segment - for the year ended 31 December 2009

Gross premiums written	**$m**	**$m**	**$m**	**$m**	**$m**
	Property	**Energy**	**Marine**	**Aviation**	**Total**
(Analysed by geographical region)					
Worldwide offshore	1.0	154.9	71.4	-	227.3
U.S. and Canada	156.0	2.2	0.1	-	158.3
Worldwide, including the U.S. and Canada [1]	51.5	7.4	(0.6)	60.9	119.2
Europe	30.3	3.5	2.1	0.3	36.2
Worldwide, excluding the U.S. and Canada [2]	35.1	-	0.4	0.1	35.6
Far East	10.9	2.1	0.2	-	13.2
Middle East	8.6	3.3	-	-	11.9
Rest of world	23.9	2.1	0.1	-	26.1
Total	**317.3**	**175.5**	**73.7**	**61.3**	**627.8**
Outwards reinsurance premiums	(17.2)	(13.5)	(9.3)	(10.7)	(50.7)
Change in unearned premiums	(14.8)	14.9	9.8	12.1	22.0
Change in unearned premiums ceded	(1.8)	(4.3)	1.7	-	(4.4)
Net premiums earned	**283.5**	**172.6**	**75.9**	**62.7**	**594.7**
Insurance losses and loss adjustment expenses	8.9	(82.6)	(29.4)	(1.3)	(104.4)
Insurance losses recoverable	-	5.7	-	-	5.7
Insurance acquisition expenses	(37.8)	(37.8)	(23.1)	(13.9)	(112.6)
Insurance acquisition expenses ceded	2.0	2.9	0.7	1.0	6.6
Net underwriting profit	**256.6**	**60.8**	**24.1**	**48.5**	**390.0**
Net unallocated income and expenses					(1.5)
Profit before tax					**388.5**
Loss ratio	(3.1%)	44.6%	38.7%	2.1%	16.6%
Acquisition cost ratio	12.6%	20.2%	29.5%	20.6%	17.8%
Expense ratio	-	-	-	-	10.2%
Combined ratio	**9.5%**	**64.8%**	**68.2%**	**22.7%**	**44.6%**

(1) Worldwide, including the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area.
(2) Worldwide, excluding the U.S. and Canada, comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area, but that specifically exclude the U.S. and Canada.

3. Investment return

The total investment return for the Group is as follows:

For the year ended 31 December 2010	**$m**	**$m**	**$m**	**$m**
	Investment income and other investment income	**Net realised gains (losses) and impairments**	**Net change in unrealised gains/losses**	**Total investment return**
Fixed income securities	52.5	32.2	(2.0)	82.7
Other investments	0.1	1.0	-	1.1
Cash and cash equivalents	0.9	-	-	0.9
Total investment return	**53.5**	**33.2**	**(2.0)**	**84.7**

For the year ended 31 December 2009	**$m**	**$m**	**$m**	**$m**
	Investment income and other investment income	**Net realised gains (losses) and impairments**	**Net change in unrealised gains/losses**	**Total investment return**
Fixed income securities	53.9	24.7	2.7	81.3
Equity securities	-	(1.0)	-	(1.0)
Other investments	0.3	0.1	-	0.4
Cash and cash equivalents	2.1	-	-	2.1
Total investment return	**56.3**	**23.8**	**2.7**	**82.8**

Net realised gains (losses) and impairments includes an impairment loss of $nil (2009 - $0.4 million) recognised on fixed income securities held by the Group.

Refer to page 32 in the risk disclosures section for the estimated fair value of the Group's derivative instruments. Realised gains and losses on futures and options contracts are included in net realised gains (losses) and impairments. The net impact of TBAs is $nil for all reporting periods.

Included in investment income is $4.0 million (2009 - $3.5 million) of investment management and custodian fees.

4. Net insurance acquisition expenses

	2010 $m	**2009 $m**
Insurance acquisition expenses	118.2	104.6
Changes in deferred insurance acquisition expenses	(8.3)	8.0
Insurance acquisition expenses ceded	(3.2)	(5.2)
Changes in deferred insurance acquisition expenses ceded	(0.4)	(1.4)
Total net insurance acquisition expenses	**106.3**	**106.0**

5. Results of operating activities

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

	2010 $m	2009 $m
Depreciation on owned assets	2.6	0.8
Operating lease charges	3.2	1.6
Auditors' remuneration		
- Group audit fees	1.3	1.2
- Tax advice	-	0.1
- Other services	0.3	0.5
Total	**7.4**	**4.2**

Fees paid to the Group's auditors for tax advice and other services are approved by the Group's Audit Committee.

6. Employee benefits

	2010 $m	2009 $m
Wages and salaries	19.0	15.7
Pension costs	1.5	1.5
Bonus and other benefits	12.7	18.4
Total cash compensation	**33.2**	**35.6**
RSS - ordinary	14.3	6.8
RSS - bonus deferral	1.0	-
RSS - exceptional	0.1	0.5
LTIP	5.3	5.7
Warrants - performance	0.4	3.4
Total equity based compensation	**21.1**	**16.4**
Total employee benefits	**54.3**	**52.0**

Equity based compensation

The Group's primary equity based compensation scheme is its RSS. Previously the Group also administered an LTIP and a warrant plan.

RSS

On 22 December 2010 LHL's shareholders, in a Special General Meeting, voted in favour of the LHL Board's proposal to modify the existing awards program to a nil-cost options program. This extends the exercise period to ten years from the grant date for all outstanding and future RSS grants. Previously, all awards were issued upon the vesting date. As the options are nil-cost, the estimated fair value under the Black-Scholes model of each RSS option granted pursuant to the plan is equal to the estimated fair value used prior to the modification of the plan, the share price of LHL on the date of grant.

RSS - ordinary

The ordinary RSS options vest after a three year period and are dependent on certain performance criteria. A maximum of 50% of the ordinary RSS options will vest only on the achievement of a TSR in excess of the 75^{th} percentile of the TSR of a pre-defined comparator group. A maximum of 50% of the ordinary RSS options will vest only on the achievement of an RoE by LHL in excess of a required amount.

	Number	Weighted average fair value
Outstanding as at 31 December 2008	**1,832,787**	**$5.75**
Granted during the year	2,480,125	$7.79
Forfeited during the year	(20,029)	$5.73
Outstanding as at 31 December 2009	**4,292,883**	**$6.93**
Granted during the year	2,145,681	$7.24
Forfeited during the year	(533,119)	$7.16
Outstanding as at 31 December 2010	**5,905,445**	**$7.02**
Exercisable as at 31 December 2010	**-**	**-**

	2010	2009
Weighted average remaining contractual life	8.3	8.8

The estimated fair value of ordinary restricted share options granted ranges between $5.73 and $8.58. An amount equivalent to the dividends paid between the grant date and the exercise date accrues and is paid at the time of exercise, pro-rata according to the number of RSS options that vest.

RSS - bonus deferral

The bonus deferral restricted shares vest after a two year period and do not have associated performance criteria for vesting.

	Number	Weighted average fair value
Outstanding as at 31 December 2008 and 2009	**-**	**-**
Granted during the year	390,024	$7.06
Forfeited during the year	(18,190)	$7.05
Outstanding as at 31 December 2010	**371,834**	**$7.06**
Exercisable as at 31 December 2010	**-**	**-**

	2010	2009
Weighted average remaining contractual life	9.2	-

The estimated fair value of bonus deferral restricted share options granted ranges between $7.05 and $7.13. An amount equivalent to the dividends paid between the grant date and the exercise date accrues and is paid at the time of exercise, pro-rata according to the number of RSS options that vest.

RSS - exceptional

The exceptional restricted shares vested on 28 March 2010 after a two year period and did not have associated performance criteria for vesting.

	Number	Weighted average fair value
Outstanding as at 31 December 2008 and 2009	**166,904**	**$5.73**
Issued during the year	(166,904)	$5.73
Outstanding as at 31 December 2010	**-**	**-**

An amount of $0.3 million (2009 - $nil) of dividend equity payments was paid at the time of vesting.

LTIP

The LTIP plan was closed on 4 January 2008. All LTIP options will expire ten years from the date of grant. 25% of LTIP options vested on each of the first, second, third and fourth anniversary of the grant date. There were no associated performance criteria. Settlement is at the discretion of the Group and may be in cash or shares.

	Number	Weighted average exercise price[(1)]
Outstanding as at 31 December 2008	**6,893,300**	**$5.34**
Exercised during the year	(2,220,059)	$4.28
Forfeited during the year	(56,489)	$5.57
Outstanding as at 31 December 2009	**4,616,752**	**$4.32**
Exercised during the year	(2,547,678)	$3.76
Forfeited during the year	(285,911)	$4.38
Outstanding as at 31 December 2010	**1,783,163**	**$2.88**
Exercisable as at 31 December 2010	**987,474**	**$2.71**

[(1)] Amounts for prior years have been revalued at the exchange rate as at 31 December 2010.

	2010	2009
Weighted average remaining contractual life	6.3	7.3

As approved by the Remuneration Committee on 18 November 2009, all option exercise prices are automatically adjusted on the dividend Record Date to neutralise the devaluing impact of dividend payments. Prior to this date the Remuneration Committee met and approved each individual exercise price adjustment. The resulting charge to equity based compensation in the consolidated statement of comprehensive income is shown below. In all cases there is a net $nil impact to shareholders' equity.

Date	Adjustment to exercise price $	£	2010 $m	2009 $m
14 February 2008	1.10	0.56	0.3	0.7
4 November 2009	1.30	0.79	2.9	2.0
19 March 2010	0.10	0.07	0.5	-
3 September 2010	0.05	0.03	0.1	-
10 December 2010	1.40	0.89	0.8	-
Total			**4.6**	**2.7**

Management team ordinary warrants

Ordinary warrants were all fully vested by 31 December 2008. All ordinary warrants will expire ten years from the date of issue. The fair value of all ordinary warrants granted was $2.62 per share. Ordinary warrants granted and outstanding are:

	Number	Weighted average exercise price
Outstanding as at 31 December 2008 and 2009	**11,433,465**	**$4.71**
Exercised during the year	(1,398,670)	$4.62
Outstanding as at 31 December 2010	**10,034,795**	**$4.72**
Exercisable as at 31 December 2010	**10,034,795**	**$4.72**

	2010	2009
Weighted average remaining contractual life	5.0	6.0

Management team performance warrants

Performance warrants were all fully vested by 31 December 2009. All performance warrants will expire ten years from the date of issue. Vesting was dependent on achieving certain performance criteria. The fair value of all warrants granted was $2.62 per share. Performance warrants granted and outstanding are:

	Number	Weighted average exercise price
Outstanding as at 31 December 2008	**3,691,687**	**$4.10**
Lapsed during the year	(1,931,377)	$2.60
Outstanding as at 31 December 2009	**1,760,310**	**$3.62**
Exercised during the year	(415,500)	$3.62
Outstanding as at 31 December 2010	**1,344,810**	**$3.62**
Exercisable as at 31 December 2010	**1,344,810**	**$3.62**

	2010	2009
Weighted average remaining contractual life	5.0	6.0

The exercise price of warrants was automatically adjusted for dividends declared prior to their vesting dates, as follows:

Record date	Payment date	U.S.$	Number Ordinary warrants	Number Performance warrants	Number Foundation warrants
10 December 2007	25 January 2008	1.10	2,858,366	5,789,065	162,036
28 August 2009	7 October 2009	0.05	-	2,894,532	-
20 November 2009	6 January 2010	1.25	-	2,894,532	-

Refer to note 21 for further disclosure on non-management warrants outstanding.

7. Financing costs

	2010 $m	2009 $m
Interest expense on long-term debt	5.4	6.4
Net change in unrealised gains/losses on interest rate swap	0.3	1.3
Other financing costs	1.0	0.4
Total	**6.7**	**8.1**

Refer to note 19 for details of long-term debt and financing arrangements

8. Tax charge

Bermuda

LHL, LICL and LUK have received an undertaking from the Bermuda government exempting them from all Bermuda local income, withholding and capital gains taxes until 28 March 2016. At the present time no such taxes are levied in Bermuda.

United States

The Group 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 or capital gains.

United Kingdom

The UK subsidiaries are subject to normal UK corporation tax on all their taxable profits.

Dubai

There are currently no local Dubai or Federal (UAE) taxes payable on the profits or revenue of businesses operating in the UAE. Current law states that DIFC establishments shall be subject to a zero tax rate on income until the year 2054.

Tax charge	2010 $m	2009 $m
Corporation tax charge for the period	8.9	4.8
Adjustments in respect of prior period corporation tax	1.0	0.4
Deferred tax credit for the period	(1.5)	(1.5)
Adjustments in respect of prior period deferred tax	-	(0.6)
Total tax charge	**8.4**	**3.1**

Tax reconciliation	2010 $m	2009 $m
Profit before tax	339.2	388.5
Less profit not subject to tax	(308.8)	(372.9)
Profits subject to tax	**30.4**	**15.6**
UK corporation tax at 28%	8.5	4.4
Adjustments in respect of prior period	1.0	(0.2)
Differences related to equity based compensation	(2.5)	(1.0)
Other expense permanent differences	(0.6)	(0.1)
Tax recognised directly in other reserves	2.0	-
Total tax charge	**8.4**	**3.1**

Due to the different taxpaying jurisdictions throughout the Group the current tax charge as a percentage of the Group's profit before tax is 2.5% (2009 - 0.8%).

As at 31 December 2010, a corporation tax credit of $0.4 million (2009 - $nil) is included in other reserves which relates to tax deductions for equity based compensation award exercises in excess of the cumulative expense at the reporting date. Refer to note 15 for further details of tax credits included in other reserves.

Refer to note 10 for details of the tax expense related to the net change in unrealised gains and losses on investments that is included in accumulated other comprehensive income within shareholders' equity.

9. Cash and cash equivalents

	2010 $m	2009 $m
Cash at bank and in hand	34.5	288.9
Cash equivalents	478.0	151.1
Total cash and cash equivalents	**512.5**	**440.0**

Cash equivalents have an original maturity of three months or less. The carrying amount of these assets approximates their fair value.

Included in cash at bank and in hand at 31 December 2009 is $232.5 million of cash held on deposit by LHL's share registrar to fund the special dividend payment disclosed in note 20.

Refer to note 19 for the cash and cash equivalent balances on deposit as collateral.

10. Investments

As at 31 December 2010	**$m**	**$m**	**$m**	**$m**
	Cost or amortised cost	**Gross unrealised gain**	**Gross unrealised loss**	**Estimated fair value**
Fixed income securities				
- Short-term investments	12.1	-	-	12.1
- U.S. treasuries	295.8	5.5	(0.8)	300.5
- Other government bonds	179.0	3.9	(1.5)	181.4
- U.S. municipal bonds	10.9	0.1	(0.1)	10.9
- U.S. government agency debt	34.2	0.6	(0.4)	34.4
- Asset backed securities	19.4	0.3	-	19.7
- U.S. government agency mortgage backed securities	331.2	8.4	(2.1)	337.5
- Non-agency mortgage backed securities	16.4	0.1	-	16.5
- Non-agency commercial mortgage backed securities	26.3	0.6	(0.2)	26.7
- Corporate bonds	670.2	16.8	(3.1)	683.9
- Corporate bonds - FDIC guaranteed	93.7	1.8	-	95.5
Total fixed income securities - available for sale	**1,689.2**	**38.1**	**(8.2)**	**1,719.1**
Other investments	**-**	**0.6**	**(0.8)**	**(0.2)**
Total investments	**1,689.2**	**38.7**	**(9.0)**	**1,718.9**

As at 31 December 2009	**$m**	**$m**	**$m**	**$m**
	Cost or amortised cost	**Gross unrealised gain**	**Gross unrealised loss**	**Estimated fair value**
Fixed income securities				
- Short-term investments	288.8	-	-	288.8
- U.S. treasuries	251.9	4.1	(1.2)	254.8
- Other government bonds	72.5	1.5	(0.2)	73.8
- U.S. municipal bonds	2.5	-	-	2.5
- U.S. government agency debt	114.1	1.0	(0.1)	115.0
- U.S. government agency mortgage backed securities	473.7	11.6	(0.9)	484.4
- Corporate bonds	467.1	13.3	(0.6)	479.8
- Corporate bonds - FDIC guaranteed	191.0	2.6	(0.2)	193.4
Total investments - available for sale	**1,861.6**	**34.1**	**(3.2)**	**1,892.5**

Accumulated other comprehensive income is in relation to the Group's fixed income securities classified as available for sale and is as follows:

	2010 $m	2009 $m
Gross unrealised gains	38.1	34.1
Gross unrealised losses	(8.2)	(3.2)
Net foreign exchange gains	(1.0)	-
Tax provision	(0.7)	(0.5)
Accumulated other comprehensive income	**28.2**	**30.4**

Fixed income maturities are presented in the risk disclosures section on page 38. Refer to note 19 for the investment balances in trusts in favour of ceding companies and on deposit as collateral.

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

Category (i)
Category (i) includes 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. The Group determines securities classified as category (i) to include highly liquid U.S. treasuries and certain highly liquid short-term investments.

Category (ii)
Category (ii) investments include securities with quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data. Instruments included in category (ii) are valued via independent external sources using modeled or other valuation methods. Such methods are typically industry accepted standard and include:

- Broker-dealer quotes;
- Pricing models or matrix pricing;
- Present values;
- Future cash flows;
- Yield curves;
- Interest rates;
- Prepayment speeds; and
- Default rates.

Other similar quoted instruments or market transactions may be used.

The Group determines securities classified as category (ii) to include short-term and fixed maturity investments such as:

- Non-U.S. government bonds;
- U.S. municipal bonds;
- U.S. government agency debt;
- Asset backed securities;
- U.S. government agency mortgage backed securities;
- Non-agency mortgage backed securities
- Corporate bonds; and
- OTC derivatives, including futures, options, forward foreign exchange contracts, interest rate swaps, credit default swaps and swaptions.

Category (iii)
Category (iii) includes securities for which valuation techniques are not based on observable market data. During the years ended 31 December 2010 and 2009, the Group did not hold any category (iii) investments.

The Group determines the estimated fair value of each individual security utilising the highest level inputs available. Prices for the Group's investment portfolio are provided by 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 - a "SAS 70" audit. SAS 70 audit reports are available to clients of the firm and the report is reviewed annually by management. In accordance with their pricing policy, various recognised reputable pricing sources are used including index providers, broker-dealers, and pricing vendors. 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' and custodian's pricing.

The Group 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 hierarchy of the Group's investment holdings is as follows:

As at 31 December 2010	**$m**	**$m**	**$m**
	(i)	**(ii)**	**Total**
Fixed income securities			
- Short-term investments	11.1	1.0	12.1
- U.S. treasuries	300.5	-	300.5
- Other government bonds	-	181.4	181.4
- U.S. municipal bonds	-	10.9	10.9
- U.S. government agency debt	-	34.4	34.4
- Asset backed securities	-	19.7	19.7
- U.S. government agency mortgage backed securities	-	337.5	337.5
- Non-agency mortgage backed securities	-	16.5	16.5
- Non-agency commercial mortgage backed securities	-	26.7	26.7
- Corporate bonds	-	683.9	683.9
- Corporate bonds - FDIC guaranteed	-	95.5	95.5
Total fixed income securities - available for sale	**311.6**	**1,407.5**	**1,719.1**
Other investments	**-**	**(0.2)**	**(0.2)**
Total investments	**311.6**	**1,407.3**	**1,718.9**

As at 31 December 2009	$m (i)	$m (ii)	$m Total
Fixed income securities			
- Short-term investments	175.1	113.7	288.8
- U.S. treasuries	254.8	-	254.8
- Other government bonds	-	73.8	73.8
- U.S. municipal bonds	-	2.5	2.5
- U.S. government agency debt	-	115.0	115.0
- U.S. government agency mortgage backed securities	-	484.4	484.4
- Corporate bonds	-	479.8	479.8
- Corporate bonds - FDIC guaranteed	-	193.4	193.4
Total fixed income securities - available for sale	**429.9**	**1,462.6**	**1,892.5**

There have been no transfers between categories (i) and (ii) or movements within category (iii), therefore no reconciliations have been presented.

11. Reinsurance assets and liabilities

	$m Unearned premiums ceded	$m Amounts payable to reinsurers	$m Other receivables	$m Total
As at 31 December 2008	**10.0**	**(2.0)**	**3.2**	**11.2**
Net deferral for:				
Prior years	(9.7)	-	-	(9.7)
Current year	5.3	-	-	5.3
Other	-	(2.2)	1.1	(1.1)
As at 31 December 2009	**5.6**	**(4.2)**	**4.3**	**5.7**
Net deferral for:				
Prior years	(5.6)	-	-	(5.6)
Current year	2.9	-	-	2.9
Other	-	(0.2)	1.3	1.1
As at 31 December 2010	**2.9**	**(4.4)**	**5.6**	**4.1**

12. Losses and loss adjustment expenses

	$m Losses and loss adjustment expenses	$m Reinsurance recoveries	$m Net losses and loss adjustment expenses
As at 31 December 2008	**528.8**	**(42.1)**	**486.7**
Net incurred losses for:			
Prior years	(59.5)	(4.0)	(63.5)
Current year	163.9	(1.7)	162.2
Exchange adjustments	(0.4)	(0.1)	(0.5)
Incurred losses and loss adjustment expenses	**104.0**	**(5.8)**	**98.2**
Net paid losses for:			
Prior years	137.8	(12.1)	125.7
Current year	6.1	-	6.1
Paid losses and loss adjustment expenses	**143.9**	**(12.1)**	**131.8**
As at 31 December 2009	**488.9**	**(35.8)**	**453.1**
Net incurred losses for:			
Prior years	(104.9)	4.8	(100.1)
Current year	299.6	(33.8)	265.8
Exchange adjustments	(1.8)	-	(1.8)
Incurred losses and loss adjustment expenses	**192.9**	**(29.0)**	**163.9**
Net paid losses for:			
Prior years	123.0	(11.8)	111.2
Current year	51.3	(17.1)	34.2
Paid losses and loss adjustment expenses	**174.3**	**(28.9)**	**145.4**
As at 31 December 2010	**507.5**	**(35.9)**	**471.6**

Further information on the calculation of loss reserves and the risks associated with them is provided in the risk disclosures section from page 24. 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 our loss reserves. The Group believes that the loss reserves established are adequate, however a 20% increase in estimated losses would lead to a $101.5 million (2009 - $97.8 million) increase in loss reserves. There was no change to the Group's reserving methodology during the year. The split of losses and loss adjustment expenses between notified outstanding losses, ACRs assessed by management and IBNR is shown below:

	2010		**2009**	
As at 31 December	**$m**	**%**	**$m**	**%**
Outstanding losses	251.8	49.6	258.6	52.9
ACR	61.1	12.0	22.9	4.7
IBNR	194.6	38.4	207.4	42.4
Total	**507.5**	**100.0**	**488.9**	**100.0**

The Group's reserve for unpaid losses and loss adjustment expenses as at 31 December 2010 and 2009 had an estimated duration of approximately two years.

Claims development

The development of insurance liabilities is indicative of the Group's ability to estimate the ultimate value of its insurance liabilities. The Group began writing insurance and reinsurance business in December 2005. Due to the minimal number of underlying risks and lack of known loss events occurring during the period to 31 December 2005, the Group does not expect to incur any losses from coverage provided in 2005. Accordingly, the loss development tables do not include that year.

Accident year	2006 $m	2007 $m	2008 $m	2009 $m	2010 $m	Total $m
Gross losses						
Estimate of ultimate liability [1]						
At end of accident year	39.1	154.8	444.6	163.3	297.4	
One year later	34.7	131.2	417.4	107.8		
Two years later	32.0	103.5	377.5			
Three years later	27.6	94.8				
Four years later	27.2					
Current estimate of cumulative liability	**27.2**	**94.8**	**377.5**	**107.8**	**297.4**	**904.7**
Payments made	**(21.0)**	**(65.6)**	**(233.4)**	**(25.9)**	**(51.3)**	**(397.2)**
Total gross liability	**6.2**	**29.2**	**144.1**	**81.9**	**246.1**	**507.5**

Accident year	2006 $m	2007 $m	2008 $m	2009 $m	2010 $m	Total $m
Reinsurance						
Estimate of ultimate recovery [1]						
At end of accident year	-	3.6	40.7	1.6	33.8	
One year later	-	6.2	47.1	1.3		
Two years later	-	4.0	43.1			
Three years later	-	3.5				
Four years later	-					
Current estimate of cumulative recovery	**-**	**3.5**	**43.1**	**1.3**	**33.8**	**81.7**
Payments received	**-**	**(3.0)**	**(25.7)**	**-**	**(17.1)**	**(45.8)**
Total gross recovery	**-**	**0.5**	**17.4**	**1.3**	**16.7**	**35.9**

Accident year	2006 $m	2007 $m	2008 $m	2009 $m	2010 $m	Total $m
Net losses						
Estimate of ultimate liability [1]						
At end of accident year	39.1	151.2	403.9	161.7	263.6	
One year later	34.7	125.0	370.3	106.5		
Two years later	32.0	99.5	334.4			
Three years later	27.6	91.3				
Four years later	27.2					
Current estimate of cumulative liability	**27.2**	**91.3**	**334.4**	**106.5**	**263.6**	**823.0**
Payments made	**(21.0)**	**(62.6)**	**(207.7)**	**(25.9)**	**(34.2)**	**(351.4)**
Total net liability	**6.2**	**28.7**	**126.7**	**80.6**	**229.4**	**471.6**

[1] Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2010.

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:

	2010 $m	2009 $m
2006 accident year	0.3	4.4
2007 accident year	8.3	25.2
2008 accident year	36.0	33.9
2009 accident year	55.5	-
Total favourable development	**100.1**	**63.5**

During 2010 the Group was impacted by significant losses in relation to the Chilean earthquake and subsequent aftershocks as follows:

	$m
Insurance losses and loss adjustment expenses	96.8
Reinstatement premium	(12.1)
Net ultimate loss as at 31 December 2010	**84.7**

The Group has exposure to risks in Chile in the following classes: property retrocession, property direct and facultative, property catastrophe excess of loss and marine. Loss information after a severe earthquake can take longer to obtain than for other events, particularly in the property retrocession portfolio which accounts for the majority of the Group's exposure. As additional information emerges the actual ultimate net loss from the earthquake could be materially different from this estimate. The 90th percentile of the loss distribution for this estimate is $100.9 million with the 95th percentile being $106.4 million.

During 2009 there were no major loss events that impacted the Group.

In September 2008, Hurricane Ike passed through the Gulf of Mexico oil fields, making landfall in the U.S. Hurricane Ike was a very destructive storm, causing damage to and destruction of a significant number of oil platforms. The net ultimate financial impact of Hurricane Ike is as follows:

	$m
Net ultimate financial impact as at 31 December 2008	**150.8**
Change in insurance losses and loss adjustment expenses	21.0
Change in insurance losses and loss adjustment expenses recoverable	(4.6)
Change in reinstatement premium	0.7
Change in other deductions	(1.3)
Net ultimate financial impact as at 31 December 2009	**166.6**
Change in insurance losses and loss adjustment expenses	1.6
Change in insurance losses and loss adjustment expenses recoverable	1.4
Change in reinstatement premium	(2.0)
Change in other deductions	(0.5)
Net ultimate financial impact as at 31 December 2010	**167.1**

Estimation of the ultimate liability of offshore losses is complex. Loss assessments require skilled loss adjusters. The availability of loss adjusters with the necessary expertise is scarce and large events put a further strain on this resource. A substantial degree of judgement is involved in assessing the ultimate cost of Hurricane Ike, and the final amount could be materially different from that currently reported. Management's current best estimate of the ultimate liability for Hurricane Ike is $179.7 million. The 90th percentile of the loss distribution for this estimate is $194.0 million with the 95th percentile being $198.8 million.

13. Insurance, reinsurance and other receivables

All receivables are considered current other than $30.7 million (2009 - $21.1 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 Group's receivables.

14. Deferred acquisition costs and deferred acquisition costs ceded

The reconciliation between opening and closing deferred acquisition costs incurred and ceded is shown below:

	Incurred $m	Ceded $m	Net $m
As at 31 December 2008	**60.9**	**(1.9)**	**59.0**
Net deferral during the year	104.6	(7.4)	97.2
Income (expense) for the year	(112.6)	6.6	(106.0)
As at 31 December 2009	**52.9**	**(2.7)**	**50.2**
Net deferral during the year	118.2	(1.0)	117.2
Income (expense) for the year	(109.9)	3.6	(106.3)
As at 31 December 2010	**61.2**	**(0.1)**	**61.1**

15. Deferred tax asset

	2010 $m	2009 $m
Deferred tax assets (related to equity based compensation)	7.8	3.9
Deferred tax liabilities (related to claims equalisation reserves)	(1.4)	(0.6)
Net deferred tax asset	**6.4**	**3.3**

During 2010, the UK government enacted a change in the corporation tax rate from 28.0% to 27.0% that will become effective from 1 April 2011. A deferred tax expense of $0.1 million was recognised during the period with respect to this change. Deferred tax on temporary differences that are expected to unwind in 2011 have a tax rate of 27.3% applied to them and a rate of 27.0% is applied to those that are expected to unwind in subsequent years.

As at 31 December 2010, a deferred tax credit of $1.6 million (2009 - $nil) was recognised in other reserves which relates to deferred tax credits for unexercised equity based compensation awards where the estimated market value is in excess of the cumulative expense at the reporting date.

Deferred tax assets are recognised to the extent that realising the related tax benefit through future taxable profits is likely. It is anticipated that the Lancashire UK group of companies will be profitable in 2011, thus the entire deferred tax asset is recognised. All deferred tax assets and liabilities are classified as non-current.

16. Property, plant and equipment

	2010 $m	2009 $m
Cost	11.9	10.2
Accumulated depreciation	(4.5)	(2.0)
Net book value	**7.4**	**8.2**

17. Insurance liabilities

	$m Unearned premiums	$m Other payables	$m Total
As at 31 December 2008	**339.6**	**17.6**	**357.2**
Net deferral for:			
Prior years	(274.8)	-	(274.8)
Current year	252.8	-	252.8
Other	-	(1.8)	(1.8)
As at 31 December 2009	**317.6**	**15.8**	**333.4**
Net deferral for:			
Prior years	(259.1)	-	(259.1)
Current year	292.1	-	292.1
Other	-	4.8	4.8
As at 31 December 2010	**350.6**	**20.6**	**371.2**

18. Insurance, reinsurance and other payables

	2010 $m	2009 $m
Dividends payable	258.4	263.0
Other payables	62.7	28.4
Accrued interest payable	0.3	0.2
Total other payables	**321.4**	**291.6**
Insurance contracts - other payables	20.6	15.8
Amounts payable to reinsurers	4.4	4.2
Total payables	**346.4**	**311.6**

Further information on dividends declared is shown in note 20. Other payables include unsettled investment trades, unsettled share repurchases, accrued interest and other accruals. Insurance payables relate to amounts due to policyholders for profit commission, return premiums and claims payable. All payables are considered current. The carrying value approximates fair value due to the short-term nature of the payables.

19. Long-term debt and financing arrangements

Long-term debt

On 15 December 2005 the Group issued, via a trust company, $97.0 million and €24.0 million in aggregate principal amount of subordinated loan notes at an issue price of $1,000 and €1,000 of their principal amounts respectively. The carrying values are shown below:

As at 31 December	2010 $m	2009 $m
Long-term debt $97.0 million	97.0	97.0
Long-term debt €24.0 million	31.8	34.4
Carrying value	**128.8**	**131.4**

The U.S. dollar subordinated loan notes are repayable on 15 December 2035 with a prepayment option available from 15 March 2011. Prior to 15 March 2011, upon the occurrence and during the continuation of a Special Event, LHL may, at its option, redeem the securities, in whole but not in part, at a sliding scale redemption price. Interest on the principal is based on a set margin (3.70%) above the variable LIBOR rate and is payable quarterly.

The Euro subordinated loan notes are repayable on 15 June 2035 with a prepayment option available from 15 March 2011. Prior to this date prepayment would only be available in the event of a Special Event. Interest on the principal is based on a set margin (3.70%) above the variable Euribor rate and is payable quarterly.

The Group is exposed to cash flow interest rate risk and currency risk on its long-term debt. Further information is provided in the risk disclosures section from page 35.

The fair value of the long-term debt is estimated as $118.7 million (2009 - $121.4 million). The fair value is estimated by reference to similar financial instruments quoted in active markets.

The interest accrued on the long-term debt was $0.3 million (2009 - $0.2 million) at the balance sheet date and is included in other payables.

Refer to note 7 for details of the interest expense for the year included in financing costs.

Interest rate swaps

The Group hedges a portion of its floating rate borrowings using interest rate swaps to transfer floating to fixed rate. These instruments are held at estimated fair value. Refer to the risk disclosures section from page 35 for further details. The Group has the right to net settle these instruments. The final cash settlement on these instruments is $0.8 million (2009 - $0.8 million) and is due on 15 March 2011 when these instruments expire. The counter-party requires collateralisation of positions in excess of $2.0 million.

The interest rate swaps are held at estimated fair value, priced using observable market inputs, and are therefore classified as category (ii) securities in the fair value hierarchy.

Refer to note 7 for the net impact from cash settlement and changes in estimated fair value included in financing costs.

Letters of credit

As both LICL and LUK are non-admitted insurers or reinsurers throughout the U.S., the terms of certain contracts require them to provide LOCs to policyholders as collateral. LHL and LICL have a syndicated collateralised credit facility in the amount of $200.0 million which expires on 16 July 2012. The facility contains a $75.0 million loan sub-limit available for general corporate purposes. There was no outstanding debt under this facility at any reporting date.

On 23 April 2010, LHL and LICL entered into a bi-lateral collateralised two year credit facility in the amount of $200.0 million with Lloyds TSB Bank PLC.

The facilities are available for the issue of LOCs to ceding companies. The facilities are also available for LICL to issue LOCs to LUK to collateralise certain insurance balances.

The total of LOC facilities available to LHL and LICL is $400.0 million.

The terms of both facilities also include standard default and cross default provisions which require certain covenants to be adhered to. These include the following:

(i) an S&P or equivalent financial strength rating of at least B++; and
(ii) a maximum debt to capital ratio of 30%, where the current long-term debt issuance is excluded from this calculation.

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

The following LOCs have been issued:

	2010 $m	**2009 $m**
Issued to affiliates	-	-
Issued to third parties	18.9	25.7

Letters of credit are required to be fully collateralised.

Trusts

The Group 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.

As at and for the years ended 31 December 2010 and 2009 the Group was in compliance with all covenants under its trust facilities.

The following cash and cash equivalents and investment balances were held in trust and other collateral accounts in favour of third parties:

As at 31 December	2010 $m Cash and cash equivalents	2010 $m Fixed income securities	2009 $m Cash and cash equivalents	2009 $m Fixed income securities
In various trust accounts for policyholders	7.7	223.8	14.1	100.9
In favour of letters of credit	12.3	22.8	1.9	37.0
In favour of interest rate swap	-	-	2.8	-
In favour of derivative contracts	0.5	0.1	0.6	-
Total	**20.5**	**246.7**	**19.4**	**137.9**

20. Share capital

Allocated, called up and fully paid	Number	$m
As at 31 December 2008	**182,283,095**	**91.1**
Shares issued due to warrant exercise	219,968	0.1
As at 31 December 2009	**182,503,063**	**91.2**
Shares repurchased and cancelled	(13,900,636)	(6.9)
As at 31 December 2010	**168,602,427**	**84.3**

Own shares	Number held in treasury	$m	Number held in trust	$m	Total number of own shares	$m
As at 31 December 2008	**9,433,168**	**58.0**	**-**	**-**	**9,433,168**	**58.0**
Shares repurchased	2,406,674	16.9	1,078,403	8.0	3,485,077	24.9
Shares distributed	-	-	(885,575)	(6.5)	(885,575)	(6.5)
As at 31 December 2009	**11,839,842**	**74.9**	**192,828**	**1.5**	**12,032,670**	**76.4**
Shares repurchased and held	4,608,603	32.6	1,819,926	13.0	6,428,529	45.6
Shares distributed	-	-	(2,276,729)	(16.6)	(2,276,729)	(16.6)
Shares donated to trust	(1,000,000)	(7.3)	1,000,000	8.8	-	1.5
As at 31 December 2010	**15,448,445**	**100.2**	**736,025**	**6.7**	**16,184,470**	**106.9**

The number of common shares in issue with voting rights (allocated share capital less shares held in treasury) as at 31 December 2010 was 153,153,982 (31 December 2009 - 170,663,221).

Share repurchases

At the AGM held on 4 May 2010 the Group's shareholders approved a renewal of the Repurchase Program authorising the repurchase of a maximum of 18,250,306 shares, with such authority to expire on the conclusion of the 2011 Annual General Meeting or, if earlier, 15 months from the date the resolution approving the Repurchase Program was passed.

The Group continues to repurchase its own shares by way of on and off market purchases utilising the current Repurchase Program, which had 7,841,826 shares remaining to be purchased at 31 December 2010 (approximately $67.1 million at the 31 December 2010 share price).

Previously share repurchase authorisations were approved for a dollar value. As at 31 December 2009 $175.1 million of approved repurchase remained in place under the authorisations that were current at that date.

To date, shares have been repurchased by the Group under share repurchase authorisations as follows:

	Number of shares cancelled	Number of shares transferred to treasury shares	Weighted average share price	$m
As at 31 December 2008	**13,640,916**	**9,433,168**	**£3.38**	**158.2**
Repurchases	-	2,406,674	£4.28	16.9
As at 31 December 2009	**13,640,916**	**11,839,842**	**£3.46**	**175.1**
Repurchases	13,900,636	4,608,603	£4.89	136.4
Stamp duty refund	-	-	-	(0.2)
Shares donated to trust	-	(1,000,000)	£4.84	(7.3)
As at 31 December 2010	**27,541,552**	**15,448,445**	**£4.05**	**304.0**

At the balance sheet date $nil (2009 - $0.1 million) remained to be settled.

In 2010 the trustees of the Lancashire Holdings Employee Benefit Trust (the “EBT”) acquired 1,819,926 (2009 - 1,078,403) shares in accordance with the terms of the trust and distributed 2,276,729 (2009 - 885,575). There were no unsettled balances in relation to EBT purchases at either balance sheet date.

Dividends

The Board of Directors have authorised the following dividends:

Dividends	Record date	Payment date	$m
Interim dividend of $0.05 (£0.03082)	28 August 2009	7 October 2009	10.5
Special dividend of $1.25 (£0.75625)	20 November 2009	6 January 2010	263.0
Final dividend of $0.10 (£0.06658)	19 March 2010	14 April 2010	20.8
Interim dividend of $0.05 (£0.03237)	3 September 2010	13 October 2010	9.4
Special dividend of $1.40 (£0.88563)	10 December 2010	19 January 2011	264.0

21. Other reserves

Other reserves represent the Group's restricted shares, options and warrants. Changes in the number of restricted shares and options outstanding are disclosed in note 6. The change in the number of non-management warrants outstanding is as follows:

Warrants	Number Founders' warrants	Number Foundation warrants	Number Management performance warrants unallocated
As at 31 December 2008	**25,303,917**	**648,143**	**198,395**
Cancelled	-	-	(198,395)
Exercised	(833,200)	-	-
As at 31 December 2009 and 2010	**24,470,717**	**648,143**	**-**
Exercisable as at 31 December 2010	**24,470,717**	**648,143**	**-**
Weighted average exercise price as at 31 December 2010	**$5.00**	**$4.73**	**-**

	2010	**2009**
Weighted average remaining contractual life	5.0	6.0

The exercise price of the Lancashire Foundation warrants was automatically adjusted for dividends declared prior to the vesting date. Refer to note 6 for further details. This did not apply to the Founders' warrants as they were fully vested at the date of grant and exercisable upon issuance.

22. Lease commitments

The Group has payment obligations in respect of operating leases for certain items of office equipment and office space. Operating lease expenses for the year were $3.2 million (2009 - $1.6 million). Future minimum lease payments under non-cancellable operating leases are as follows:

	2010 $m	**2009 $m**
Due in less than one year	2.5	2.1
Due between one and five years	7.6	9.0
Due in more than five years	5.2	6.5
Total	**15.3**	**17.6**

23. Earnings per share

The following reflects the profit and share data used in the basic and diluted earnings per share computations:

	2010 $m	2009 $m
Profit for the period attributable to equity shareholders	330.8	385.4

	Number of shares	Number of shares
Basic weighted average number of shares	158,806,410	172,740,238
Dilutive effect of RSS	3,990,315	1,903,964
Dilutive effect of LTIP	500,310	494,544
Dilutive effect of warrants	14,214,198	12,649,142
Diluted weighted average number of shares	**177,511,233**	**187,787,888**

Earnings per share	**2010**	**2009**
Basic	$2.08	$2.23
Diluted	$1.86	$2.05

Share-based payments are only treated as dilutive when their conversion to common shares would decrease earnings per share or increase loss per share from continuing operations. Unvested restricted shares without performance criteria are therefore included in the number of potentially dilutive shares. Incremental shares from ordinary restricted share options where relevant performance criteria have not been met are not included in the calculation of dilutive shares. In addition, where options are antidilutive, they are not included in the number of potentially dilutive shares.

24. Related party disclosures

The consolidated financial statements include LHL and the entities listed below:

Name	Domicile
Subsidiaries	
LICL	Bermuda
LIHL	United Kingdom
LUK	United Kingdom
LIMSL	United Kingdom
LISL	United Kingdom
LMEL	United Arab Emirates
Other controlled entities	
LHFT	United States
EBT	Jersey

All subsidiaries are wholly owned, either directly or indirectly.

The Group has issued subordinated loan notes via a trust vehicle - LHFT (refer to note 19). The Group effectively has 100% of the voting rights in LHFT. These rights are subject to the property trustee's obligations to seek the approval of the holders of LHFT's preferred securities in case of default and other limited circumstances where the property trustee would enforce its rights. While the ability of the Group to influence the actions of LHFT is limited by the Trust Agreement, LHFT was set up by the Group with the sole purpose of issuing the subordinated loan notes, is in essence controlled by the Group, and is therefore consolidated.

The EBT was established to assist in the administration of the Group's employee equity based compensation schemes. While the group does not have legal ownership of the EBT and the ability of the Group to influence the actions of the EBT is limited by the Trust Deed, the EBT was set up by the Group with the sole purpose of assisting in the administration of these schemes, is in essence controlled by the Group, and is therefore consolidated.

During the year the Group made cash donations of $nil (2009 - $1.2 million) to the EBT for funding. The Group also entered into a Loan Facility Agreement (the "Facility") with RBC Cees Trustee Limited, the Trustees of the EBT. The Facility is an interest free revolving credit facility under which the Trustee can request advances on demand, within the terms of the facility, up to a maximum aggregate of $20.0 million. The Facility may only be used by the Trustees for the purpose of achieving the objectives of the EBT. During the year ended 31 December 2010, the Group had made advances of $10.0 million (2009 - $7.0 million) to the EBT under the terms of the Facility.

The Group donated 1,000,000 (2009 - nil) treasury shares to the EBT at the prevailing market rate on 13 December 2010. The total value of the treasury share donation was $8.8 million (2009 - $nil).

LICL holds $306.4 million (2009 - $271.3 million) of cash and cash equivalents and fixed income securities in trust for the benefit of LUK relating to intra-group reinsurance agreements.

Key management compensation

Remuneration for key management (the Group's executive and non-executive directors) for the years ending 31 December was as follows:

	2010 $m	2009 $m
Short-term compensation	5.1	5.6
Equity based compensation	5.1	6.1
Directors' fees and expenses	1.9	1.7
Monitoring fees	-	0.1
Total	**12.1**	**13.5**

The directors' fees and expenses includes $0.7 million (2009 - $0.7 million) paid to significant founding shareholders. The monitoring fees were previously paid to significant founding shareholders. These fee agreements ended in 2009. Non-executive directors do not receive any benefits in addition to their agreed fees and expenses and do not participate in any of the Group's incentive, performance or pension plans.

Transactions with a founding shareholder

Under the share repurchase authorisations discussed in note 20, the Group repurchased common shares for cancellation from a significant founding shareholder with representation on the Group's Board of Directors. The details are as follows:

Date	Number of shares	Price per share	$m
1 April 2010	4,120,879	$7.28	30.0
11 June 2010	1,000,000	$7.03	7.0
1 July 2010	500,000	$7.42	3.7
Total	**5,620,879**	**$7.24**	**40.7**

The sellers were Crestview Partners, L.P., Crestview Offshore Holdings (Cayman), L.P., Crestview Holdings (TE), L.P., Crestview Partners ERISA, L.P. and Crestview Partners (PF), L.P (collectively, "Crestview"). All of the shares were repurchased in off-market transactions at a discount to the then prevailing market price. As of 2 July 2010 Crestview no longer owned any common shares of the Group but continues to hold 1.2 million Founders' warrants. The founding shareholder resigned from the LHL Board of Directors as of 7 July 2010.

Transactions with Lancashire Foundation

Cash donations to the Lancashire Foundation have been approved by the Board of Directors as follows:

Date	$m
14 May 2009	1.1
25 February 2010	1.1
5 November 2010	1.3

25. Non-cash transactions

TBAs classified as derivatives were settled net during the year with purchases and sales of $246.2 million (2009 - $229.3 million) and $246.6 million (2009 - $229.5 million) respectively.

There was no unsettled element of share repurchases as at 31 December 2010. The 2009 unsettled amount of $0.1 million discussed in note 20 was not reflected in that year's cash flows. It was recorded in the subsequent year when it was actually settled. The 2010 special dividend declared of $264.0 million (2009 - $263.0 million) is not reflected in the current year cash flows. The settlement date was 19 January 2011 (2009 - 6 January 2010) and the cash flow on this transaction has been recorded in the year it was actually settled.

26. Statutory requirements and dividend restrictions

The primary source of capital used by the Group is equity shareholders' funds and borrowings. As a holding company, LHL relies on dividends from its operating entities to provide the cash flow required for debt service and dividends to shareholders. The operating entities' ability to pay dividends and make capital distributions is subject to the legal and regulatory restrictions of the jurisdictions in which they operate. For the primary operating entities these are based principally on the amount of premiums written and reserves for losses and loss adjustment expenses, subject to overall minimum solvency requirements. Operating entity statutory capital and surplus is different from shareholder's equity due to certain items that are capitalised under

IFRS but expensed or have a different valuation basis for regulatory reporting, or are not admitted under insurance regulations.

Annual statutory capital and surplus reported to regulatory authorities by the primary operating entities is as follows:

As at 31 December 2010	**$m**	**£m**
	LICL	**LUK**
Statutory capital and surplus	1,324.7	131.7
Minimum required statutory capital and surplus	289.1	25.4

As at 31 December 2009	**$m**	**£m**
	LICL	**LUK**
Statutory capital and surplus	1,213.6	120.0
Minimum required statutory capital and surplus	257.1	22.6

For LUK, various capital calculations are performed and an ICA is presented to the FSA. The FSA then considers the capital calculations and issues an ICG, reflecting the FSA's own view as to the level of capital required. The FSA considers that a decrease in an insurance company's capital below the level of its ICG represents a regulatory intervention point.

LICL is required to maintain a minimum liquidity ratio, whereby relevant assets, as defined in the regulations, must exceed 75% of relevant liabilities. As at 31 December 2010 and 2009 the liquidity ratio was met. LICL is also required to perform various capital calculations under the BMA's regulatory framework. An assessment is made of LICL's capital needs and a target capital amount is determined. The BMA may require a further capital loading on the target capital amount in certain circumstances. The BMA considers that a decrease in capital below the target level represents a regulatory intervention point.

As at 31 December 2010 and 2009 the capital requirements of both regulatory jurisdictions were met.

27. Contingencies

Litigation

LICL has been engaged in litigation in connection with the assignment of a leasehold interest. The judgement at first instance is subject to an appeal which is likely to be heard in 2011. Efforts are continuing to sub-let or assign the remaining leasehold interest.

28. Subsequent events

Establishment of a marketing office in Brazil

In November 2010, LICL made an application for admitted reinsurer status to SUSEP, the Brazilian regulatory agency which is responsible for the supervision and control of the insurance, reinsurance, open private pension and capitalisation markets in Brazil. It is intended that LICL will be authorised in Brazil as an admitted reinsurer and that a subsidiary of the Group will be incorporated to act as LICL's representative office. This subsidiary will be subject to the disclosure requirements, internal controls and restrictions of activities as prescribed by SUSEP regulations. The representative office will also be required to maintain a permanent representative in Brazil.

Dividend

On 20 February 2011 the Board of Directors declared the payment of a final ordinary dividend of 10.0 cents per common share to shareholders of record on 18 March 2011, with a settlement date of 20 April 2011. The total dividend payable will be approximately $18.9 million. An amount equivalent to the dividend accrues on all RSS options and is paid at the time of exercise, pro-rata according to the number of RSS options that vest.

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

Additional case reserves (ACR)
Additional reserves deemed necessary by management

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

AGM
Annual General Meeting

Best Lancashire Assessment of Solvency over Time (BLAST)
The Group's economic capital model

BMA
Bermuda Monetary Authority

BSX
Bermuda Stock Exchange

Catastrophe reinsurance
A form of excess of loss reinsurance which, subject to a specified limit, indemnifies the reinsured company for the amount of loss in excess of a specified retention with respect to an accumulation of losses resulting from a catastrophic event or series of events

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 earned premiums

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

DFSA
Dubai Financial Services Authority

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.

Earnings per share (EPS)
Basic EPS - Calculated by dividing net profit for the year attributable to shareholders by the weighted average number of common shares outstanding during the year, excluding treasury shares and shares held by the EBT
Diluted EPS - Calculated by dividing the net profit for the year attributable to shareholders by the weighted average number of common shares outstanding during the year plus the weighted average number of common shares that would be issued on the conversion of all potentially dilutive common shares into common shares under the treasury stock method

EBT
Lancashire Holdings Employee Benefit Trust

EMD
Emerging Market Debt

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 earned premiums

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

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 outstanding options, dilutive warrants, and diluted RSS awards by the sum of all shares, including dilutive options, dilutive warrants, and dilutive RSS awards, assuming all are exercised

FDIC Guaranteed Corporate Bonds
Corporate bonds protected by the Federal Deposit Insurance Corporation, an agency of the U.S. government

FSA
Financial Services Authority, United Kingdom

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

GRSC
Group Reinsurance Security Committee

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

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.

ICA
Individual capital assessment

ICG
Individual capital guidance

IFRS
International Financial Reporting Standard(s)

IFRIC
International Financial Reporting Interpretations Committee

IRR
Internal rate of return

Lancashire Foundation
The Lancashire Foundation is a Bermuda registered charitable trust

LHL
Lancashire Holdings Limited

LHFT
Lancashire Holdings Financing Trust I

LICL
Lancashire Insurance Company Limited

LIHL
Lancashire Insurance Holdings (UK) Limited

LIMSL
Lancashire Insurance Marketing Services Limited

LISL
Lancashire Insurance Services Limited

LMEL
Lancashire Insurance Marketing Services (Middle East) Limited

LOC
Letter of credit

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

Losses
Demand by an insured for indemnity under an insurance contract

LSE
London Stock Exchange

LTIP
Long-term incentive plan

LUK
Lancashire Insurance Company (UK) Limited

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

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

Retention limits
Limits imposed upon underwriters for retention of exposures by the Group after the application of reinsurance programmes

Return on Equity (RoE)
The IRR of the change in FCBVS in the period plus accrued dividends

Retrocessional reinsurance
The reinsurance of the reinsurance account

RPI
Renewal Price Index

RSS
Restricted share scheme

Special Event
A Special Event is a change in the tax and/or investment status of the issuing trust

Standards & Poors (S&P)
Standards & Poors is a worldwide insurance rating and information agency whose ratings are recognised as an ideal benchmark for assessing the financial strength of insurance related organisations

SUSEP
The Superintendence of Private Insurance, Brazil

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

Total Shareholder Return (TSR)
The IRR of the increase in share price, in the period, measured in U.S. dollars, adjusted for dividends

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

U.S. GAAP
Accounting principles generally accepted in the United States

Value at Risk (VaR)
A measure of the risk of loss of a specific portfolio of financial assets