
ILS PROPERTY & CASUALTY RE II LIMITED
FINANCIAL STATEMENTS

For the Period Ended December 31, 2017



April 30, 2018

Report of Independent Auditors

To the Shareholder of ILS Property & Casualty Re II Limited

We have audited the accompanying financial statements of ILS Property & Casualty Re II Limited, which comprise the balance sheet as of December 31, 2017, and the related statements of loss and comprehensive loss, of changes in shareholder's equity and of cash flows for the period from July 20, 2017 (date of incorporation) to December 31, 2017.

Management's responsibility for the financial statements

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

Auditors' responsibility

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

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



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ILS Property & Casualty Re II Limited as of December 31, 2017, and the results of its operations and its cash flows for the period from July 20, 2017 (date of incorporation) to December 31, 2017 in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers Ltd.
Chartered Professional Accountants

ILS PROPERTY & CASUALTY RE II LIMITED

BALANCE SHEET
As of December 31, 2017

	December 31, 2017 (expressed in U.S. dollars, except share data)
ASSETS	
Accounts receivable	\$ 172,819
Premiums receivable	438,496,592
Due from shareholder	154,221,358
Reinsurance balances recoverable	209,889,524
Ceded unearned premium	10,373,578
Deferred charge	33,699,846
TOTAL ASSETS	\$ 848,853,717
LIABILITIES	
Losses and loss adjustment expenses	\$ 475,348,202
Unearned premiums	23,493,606
Insurance and reinsurance balances payable	193,817,732
Accounts payable and accrued liabilities	459,366
TOTAL LIABILITIES	692,918,906
COMMITMENTS AND CONTINGENCIES	
SHAREHOLDER'S EQUITY	
Share capital	
Ordinary shares (issued and outstanding 2017: 120,000)	120,000
Additional paid-in capital	154,101,358
Retained deficit	(286,547)
TOTAL SHAREHOLDER'S EQUITY	153,934,811
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	\$ 848,853,717

See accompanying notes to the financial statements

ILS PROPERTY & CASUALTY RE II LIMITED

STATEMENT OF LOSS AND COMPREHENSIVE LOSS

For the Period from July 20, 2017 (date of incorporation) to December 31, 2017

	<u>2017</u>
	<u>(expressed in U.S. dollars)</u>
EXPENSES	
General and administrative expenses	\$ 286,547
TOTAL EXPENSES	<u>286,547</u>
NET LOSS AND COMPREHENSIVE LOSS	<u>\$ (286,547)</u>

See accompanying notes to the financial statements

ILS PROPERTY & CASUALTY RE II LIMITED

STATEMENT OF CHANGES IN SHAREHOLDER'S EQUITY

For the Period from July 20, 2017 (date of incorporation) to December 31, 2017

	2017 (expressed in U.S. dollars)
Share Capital — Ordinary Shares	
Balance, beginning of period	\$ —
Issue of shares	120,000
Balance, end of period	<u>\$ 120,000</u>
Additional Paid-in Capital	
Balance, beginning of period	\$ —
Contribution from shareholder	154,101,358
Balance, end of year	<u>\$ 154,101,358</u>
Retained Deficit	
Balance, beginning of period	\$ —
Net loss	(286,547)
Balance, end of period	<u>\$ (286,547)</u>

See accompanying notes to the financial statements

ILS PROPERTY & CASUALTY RE II LIMITED

STATEMENT OF CASH FLOWS

For the Period from July 20, 2017 (date of incorporation) to December 31, 2017

	2017
	(expressed in U.S. dollars)
OPERATING ACTIVITIES:	
Net loss	\$ (286,547)
Adjustments to reconcile net earnings to cash flows provided by (used in) operating activities:	
Changes in:	
Reinsurance balances recoverable	(209,889,524)
Other assets	(44,246,243)
Losses and loss adjustment expenses	475,348,202
Premiums receivable	(438,496,592)
Insurance and reinsurance balances payable	193,617,732
Unearned premiums	23,493,606
Accounts payable and accrued liabilities	459,366
Net cash flows provided by (used in) operating activities	<u>286,547</u>
EFFECT OF EXCHANGE RATE CHANGES ON FOREIGN CURRENCY CASH, CASH EQUIVALENTS AND RESTRICTED CASH	<u>—</u>
NET INCREASE (DECREASE) IN CASH, CASH EQUIVALENTS AND RESTRICTED CASH	<u>—</u>
CASH, CASH EQUIVALENTS AND RESTRICTED CASH, BEGINNING OF PERIOD	<u>—</u>
CASH, CASH EQUIVALENTS AND RESTRICTED CASH, END OF PERIOD	<u>\$ —</u>

See accompanying notes to the financial statements

ILS PROPERTY & CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2017

(Tabular information expressed in U.S. dollars)

1. DESCRIPTION OF BUSINESS

ILS Property & Casualty Re II Limited ("PC Re II" or the "Company") is a Bermuda exempted company registered as a Class 3B insurer under the Bermuda Insurance Act 1978. The Company was incorporated on July 20, 2017 and is wholly-owned by ILS Property & Casualty Holding II Company Ltd. ("PC Holding")

The primary purpose of the Company is to acquire discontinued property and casualty business in the non-life sector of the insurance industry from insurers, reinsurers and/or other entities (including, without limitation, self-insured organizations) and the management of the payment of future claims and the assets supporting such liabilities. Unless the context indicates otherwise, the terms the "Company," "PC Re II," "we," "us" or "our" mean ILS Property & Casualty Re II Limited.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The financial statements include our assets, liabilities and results of operations as of December 31, 2017 and for the period from July 20, 2017 (date of incorporation) to December 31, 2017.

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Our actual results could differ materially from our estimates. Accounting policies that we believe are most dependent on assumptions and estimates are considered to be our critical accounting policies and are related to the determination of:

- liability for losses and loss adjustment expenses ("LAE");
- reinsurance balances recoverable; and
- fair value estimates associated with accounting for acquisitions.

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Our actual results could differ materially from our estimates. Accounting policies that we believe are most dependent on assumptions and estimates are considered to be our critical accounting policies and are related to the determination of:

- liability for losses and loss adjustment expenses ("LAE");
- reinsurance balances recoverable; and
- fair value estimates associated with accounting for acquisitions.

Significant Accounting Policies

(a) Premiums

Non-life premiums written are earned on a pro-rata basis over the period the coverage is provided. Reinsurance premiums are recorded at the inception of the policy, are based upon contractual terms and, for certain business, are estimated based on underlying contracts or from information provided by insureds and/or brokers. Changes in reinsurance premium estimates are expected and may result in adjustments in future periods. Any subsequent differences arising on such estimates are recorded as premiums written in the period in which they are determined.

Certain non-life contracts are retrospectively rated and provide for a final adjustment to the premium based on the final settlement of all losses. Premiums on such contracts are adjusted based upon contractual terms, and management judgment is involved with respect to the estimate of the amount of losses that we expect to incur. Additional premiums are recognized at the time loss thresholds specified in the contract are exceeded and are earned over the coverage period, or are earned immediately if the period of risk coverage has passed.

Premiums receivable

Premiums receivable represent amounts currently due and amounts not yet due on insurance and reinsurance policies. Premiums for insurance policies are generally due at inception. Premiums for reinsurance policies generally become due over the period of coverage based on the policy terms. We monitor the credit risk associated with premiums receivable, taking into consideration the impact of our contractual right to offset loss obligations or unearned premiums against premiums receivable. Amounts deemed uncollectible are charged to net earnings in the period they are determined. Changes in the estimates of premiums written will result in an adjustment to premiums receivable in the period they are determined.

Unearned premiums and prepaid reinsurance premiums

Unearned premiums represent the portion of premiums written that relate to the unexpired terms of policies in force. Premiums ceded are similarly pro-rated over the period the coverage is provided with the unearned portion being deferred as prepaid reinsurance premiums.

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

(b) Losses and LAE

The liability for losses and LAE includes an amount determined from reported claims ("OSLR") and an amount, based on historical loss experience and industry statistics, for losses incurred but not yet reported ("IBNYR") and losses incurred but not enough reported ("IBNER"). IBNYR plus IBNER are commonly referred to collectively as IBNR. The ultimate claims reserves (OSLR plus IBNR) is established by management based on actuarial analysis of data provided by brokers, ceding companies and insureds and represents the estimated ultimate net outstanding claims liabilities. These estimates are continually reviewed and are necessarily subject to the impact of future changes in factors such as claim severity and frequency, changes in economic conditions including the impact of inflation, legal and judicial developments, and medical cost trends. While we believe that the amount is adequate, the ultimate liability may be in excess of, or less than, the amounts provided. Adjustments will be reflected as part of net increase or reduction in losses and LAE liabilities in the periods in which they become known. Premium and commission adjustments may be triggered by incurred losses, and any amounts are recorded in the same period that the related incurred loss is recognized.

We establish provisions for LAE relating to run-off costs for the estimated duration of the run-off, which are included in losses and LAE. These provisions are assessed at each reporting date, and provisions relating to future periods are adjusted to reflect any changes in estimates of the periodic run-off costs or the duration of the run-off, including the impact of any acceleration of the run-off period that may be caused by commutations.

(c) Reinsurance Recoverable

Amounts billed to, and due from, reinsurers resulting from paid movements in the underlying business are calculated in accordance with the terms of the individual reinsurance contracts. Similarly, reinsurance balances recoverable related to our case reserves are calculated by applying the terms of any applicable reinsurance coverage to movements in the underlying case reserves. Our estimate of reinsurance balances recoverable related to IBNR reserves is recognized on a basis consistent with the underlying IBNR reserves.

Our reinsurance balances recoverable are presented net of a provision for uncollectible amounts, reflecting the amount deemed not collectible due to credit quality, collection problems due to the location of the reinsurer, contractual disputes with reinsurers over individual contentious claims, contract language or coverage issues.

(d) Investments, Cash and Cash Equivalents

Short-term investments and fixed maturity investments

Short-term investments comprise investments with a maturity greater than three months up to one year from the date of purchase. Fixed maturities comprise investments with a maturity of greater than one year from the date of purchase.

Short-term and fixed maturity investments classified as trading are carried at fair value, with realized and unrealized holding gains and losses included in net earnings and reported as net realized and unrealized gains and losses.

Investment purchases and sales are recorded on a trade-date basis. Realized gains and losses on the sale of investments are based upon specific identification of the cost of investments.

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Cash and cash equivalents

Cash equivalents includes all highly liquid debt instruments purchased with an original maturity of three months or less.

(e) Funds Held

Under funds held arrangements, the reinsured company has retained funds that would otherwise have been remitted to our reinsurance subsidiaries. The funds balance is credited with investment income and losses payable are deducted. The investment returns of funds held are recognized in net investment income and net realized and unrealized gains (losses).

(f) Foreign Exchange

Our reporting currency is the U.S. dollar. Other foreign currency assets and liabilities that are considered monetary items are translated at exchange rates in effect at the balance sheet date. Foreign currency revenues and expenses are translated at transaction date exchange rates. These exchange gains and losses are recognized in net earnings.

(g) Retroactive Reinsurance and Deferred Charges

Retroactive reinsurance policies provide indemnification of losses and LAE with respect to past loss events.

We use the balance sheet accounting approach for assumed loss portfolio transfers, whereby at the inception of the contract there are no premiums or losses recorded in earnings. At the inception of a contract, a deferred charge asset is recorded for the excess, if any, of the estimated ultimate losses payable over the premiums received. Deferred charges are amortized over the estimated claim payment period of the related contract with the periodic amortization reflected in earnings as a component of losses and LAE. Deferred charges amortization is adjusted at each reporting period to reflect new estimates of the amount and timing of remaining loss payments. Changes in the estimated amount and the timing of payments of unpaid losses may have an effect on the unamortized deferred charges and the amount of periodic amortization. Deferred charges are assessed at each reporting period for impairment. If the asset is determined to be impaired, it is written down in the period in which the determination is made.

3. SIGNIFICANT NEW BUSINESS

2018

Knowledge

On March 5, 2018, we entered into a loss portfolio transfer agreement ("LPTA") related to a book of U.K. commercial motor, public and employers' liability lines of business along with property/premises related to U.K. commercial motor. Pursuant to the agreement, we will provide capital of approximately \$27.5 million to fully fund the reinsurance up to the aggregate limit under the terms of the LPTA.

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

2017

River

On December 29, 2017, we entered into an LPTA to reinsure a portfolio of legacy business which primarily includes Commercial Automobile, Non-Standard Personal Automobile, General Liability, Commercial and Personal Property, Mono-line Liquor Liability, Real Estate E&O, Workers' Compensation and other smaller lines of business. We assumed net reinsurance reserves of approximately \$265.5 million. The initial net reinsurance premium receivable by the Company under the LPTA was approximately \$438.5 million relating to the portfolio. In addition, we provided additional collateral to fully fund the reinsurance up to its aggregate limit.

4. REINSURANCE BALANCES RECOVERABLE

The following table provides the total reinsurance balances recoverable as at December 31, 2017:

	2017
Recoverable from reinsurers on unpaid:	
Outstanding losses	\$ 97,230,656
IBNR	112,658,868
Total reinsurance reserves recoverable	209,889,524
Paid losses recoverable	—
	<u>\$ 209,889,524</u>

As of December 31, 2017, we had reinsurance balances recoverable of approximately \$209.9 million.

We remain liable to the extent that retrocessionaires do not meet their obligations under these agreements, and therefore, we evaluate and monitor concentration of credit risk among our reinsurers. Provisions are made for amounts considered potentially uncollectible.

5. LOSSES AND LOSS ADJUSTMENT EXPENSES

The liability for losses and LAE, also referred to as loss reserves, represents our gross estimates before reinsurance for unpaid reported losses and losses that have been incurred but not reported ("IBNR"). We recognize an asset for the portion of the liability that we expect to recover from reinsurers. LAE reserves include allocated loss adjustment expenses ("ALAE"), and unallocated loss adjustment expenses ("ULAE"). ALAE are linked to the settlement of an individual claim or loss, whereas ULAE are based on our estimates of future costs to administer the claims. IBNR represents reserves for loss and LAE that have been incurred but not yet reported to us. This includes amounts for unreported claims, development on known claims and reopened claims.

The following table summarizes the liability for losses and LAE as at December 31, 2017:

	2017
Outstanding losses	\$ 220,203,547
IBNR	230,886,655
ULAE	24,258,000
Total	<u>\$ 475,348,202</u>

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

The table below provides a reconciliation of the beginning and ending liability for losses and LAE for the period ended December 31, 2017:

	2017
Balance as at July 20, 2017 (date of incorporation)	\$ —
Less: reinsurance reserves recoverable	—
Less: deferred charge on retroactive reinsurance	—
Net balance as at July 20, 2017 (date of incorporation)	—
Net incurred losses and LAE:	
Current period	—
Prior periods	—
Total net incurred losses and LAE	—
Net paid losses:	
Current period	—
Prior periods	—
Total net paid losses	—
Effect of exchange rate movement	—
Acquired on purchase of subsidiaries	—
Assumed business	231,758,832
Ceded business	—
Net balance as at December 31	231,758,832
Plus: reinsurance reserves recoverable	209,889,524
Plus: deferred charge on retroactive reinsurance	33,699,846
Balance as at December 31	\$ 475,348,202

The net reserves for losses and loss expenses related to the acquisition of the River LPT completed on December 31, 2017 will be incorporated in PC RE II's reserves for losses and loss expenses on a prospective basis for the year beginning January 1, 2018. The treatment for the acquisition of the River portfolio was adopted primarily as a result of the data necessary to produce the loss development tables were not migrated over on acquisition of the portfolio as it was not requested or received and as a result does not exist within PC Re II's data systems.

6. DEFERRED CHARGES

The following tables present a reconciliation of the beginning and ending deferred charges for the period ended December 31, 2017:

2017	Deferred Charges
Balance as at July 20 (date of incorporation)	\$ —
Acquired during the year	33,699,846
Amortization	—
Balance as at December 31, 2017	\$ 33,699,846

Deferred charges relate to retroactive reinsurance policies providing indemnification of losses and LAE with respect to past loss events. At the inception of a contract, a deferred charge asset is recorded for the excess, if any,

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

of the estimated ultimate losses payable over the premiums received. These amounts relate to the transaction with Equator, described in Note 3 - "Significant New Business".

The gross carrying value, accumulated amortization and net carrying value of the deferred charge at December 31, 2017 was as follows:

	2017		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Deferred charges on retroactive reinsurance	\$ 33,699,846	\$ —	\$ 33,699,846

7. PREMIUMS RECEIVABLE

Under the River LPT, the premium owing to the Company of \$438.5 million was contractual due on January 23, 2018. These funds were paid over on that day into the premium trust accounts and will be treated as funds withheld by the Company.

8. SHARE CAPITAL AND ADDITIONAL PAID-IN CAPITAL

As at December 31, 2017, the authorized, issued and fully paid share capital of the Company was 120,000 ordinary shares divided into 120,000 shares of par value of \$1.00 each. The Company recorded \$0.9 million of additional paid-in capital on issuance of its ordinary shares. An affiliate company holds the \$1.0 million paid in for the share capital and paid-in capital of the Company which is included within the amounts due from shareholder.

The Company recorded \$153.2 million in additional paid-in capital in relation to contributions owing from its parent in relation to operational expenses and funding associated with the River transaction.

9. RELATED PARTY TRANSACTIONS

As at December 31, 2017, the Company had an amount of \$154.2 million due from its parent, PC Holding, in relation to \$153.2 million to fund the capital required for the River transaction, as described in Note 3 - "Significant New Business," and \$1.0 million in relation to the initial share capital and paid-in capital as disclosed in Note 7 - "Share Capital and Additional Paid-In Capital."

10. DIVIDEND RESTRICTIONS AND STATUTORY FINANCIAL INFORMATION

The Company is registered under the Insurance Act 1978 of Bermuda and related regulations, as amended (the "Insurance Act"). The Insurance Act imposes certain solvency and liquidity standards and auditing and reporting requirements and grants the BMA powers to supervise, investigate, require information and the production of documents and intervene in the affairs of insurance companies.

ILS PROPERTY AND CASUALTY RE II LIMITED

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

The Company is required to maintain minimum statutory capital and surplus equal to the greater of a minimum solvency margin ("MSM") and the Enhanced Capital Requirement ("ECR") where applicable. The ECR is equal to the higher of the MSM or the Bermuda Solvency Capital Requirement ("BSCR") model. The BSCR for the year ended December 31, 2017 will not be filed with the BMA until May 2018. As a result, the required statutory capital and surplus as at December 31, 2017, based on the MSM, is \$67.7 million.

We would be prohibited from declaring or paying any dividends if we were in breach of our minimum solvency margin (which is a function of outstanding losses) or liquidity ratio (which is a function of relevant assets) or if the declaration or payment of such dividends would cause it to fail to meet such margin or ratio. In addition, we would be prohibited, without the prior approval of the BMA, from reducing by 15% or more our total statutory capital as set out in its previous year's statutory financial statements. We are required to seek regulatory approval for any dividends or distributions.

11. SUBSEQUENT EVENTS

The Company has completed its subsequent events evaluations for the period subsequent to the balance sheet date December 31, 2017 through to April 30, 2018, the date these financial statements would be issued and, except for the item as described in Note 3 - "Significant New Business," concluded that there are no subsequent events requiring recognition or disclosure.