

TOKIO MILLENNIUM RE AG

Consolidated Financial Statements
(With Independent Auditors' Report Thereon)

Years Ended December 31, 2015 and 2014

TOKIO MILLENNIUM RE AG

Contents

December 31, 2015 and 2014

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Report of the Statutory Auditor to the Board of Directors of

Tokio Millennium Re AG, Zurich

We have audited the accompanying consolidated financial statements of Tokio Millennium Re AG ("the Company"), which comprise the consolidated balance sheet, consolidated statement of comprehensive income, consolidated statement of changes in shareholder's equity, consolidated statement of cash flows, and notes for the year ended December 31, 2015.

Board of Directors' Responsibility

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS). This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider the internal control system relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system.

An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



*Tokio Millennium Re AG, Zurich
Report of the Statutory Auditor
on the Consolidated Financial Statements
to the Board of Directors*

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2015, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG AG

Patrick Scholz
*Licensed Audit Expert
Auditor in Charge*

Bill Schiller
Licensed Audit Expert

Zurich, March 2, 2016

Enclosure:

- Consolidated financial statements (consolidated balance sheet, consolidated statement of comprehensive income, consolidated statement of changes in shareholder's equity, consolidated statement of cash flows, and notes)

TOKIO MILLENNIUM RE AG

Consolidated Balance Sheet

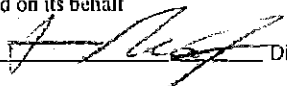
December 31, 2015 and 2014


(Expressed in thousands of United States Dollars)

	Note	<u>12/31/2015</u>	<u>12/31/2014</u>
Assets			
Cash and cash equivalents	5	\$ 279,037	\$ 167,760
Funds withheld	6	78,996	52,801
Investments	7, 8	1,993,777	1,968,316
Accrued interest receivable	11	12,035	7,599
Premiums receivable	11	716,399	474,583
Deposit assets	11, 12	296,177	337,677
Prepaid reinsurance premiums		37,676	34,200
Fair value of derivative assets	8	4,773	1,806
Outstanding losses recoverable from reinsurers	11, 17	52,730	51,473
Deferred acquisition expenses	13	327,938	201,528
Unearned profit commission		6,071	1,790
Deferred tax asset	14	3,021	3,930
Property and equipment	15	11,840	13,769
Intangible assets	16	8,429	7,190
Other assets	11	<u>21,857</u>	<u>26,034</u>
Total assets		<u>\$ 3,850,756</u>	<u>\$ 3,350,456</u>
Liabilities			
Outstanding losses and loss expenses	17, 18	\$ 857,700	\$ 699,305
Liability for collateral held on behalf of counterparties	10, 18	233,617	315,250
Reinsurance balances payable	18	89,107	53,023
Deposit liabilities	12, 18	296,177	337,677
Payable for investments purchased		8,748	-
Unearned premiums	17	1,083,347	688,827
Fair value of derivative liabilities	8, 18	4,307	2,550
Deferred commission income	13	3,511	2,840
Accounts payable and accrued expenses	18	36,565	19,248
Retirement benefit obligation	20	3,284	2,874
Deferred fee income		2,793	3,599
Deferred tax liability	14	706	948
Note payable	18, 19	<u>25,000</u>	<u>25,000</u>
Total liabilities		<u>2,644,862</u>	<u>2,151,141</u>
Shareholder's equity			
Share capital	21	250,000	250,000
Contributed surplus	21	400,000	400,000
Retained earnings		600,349	563,807
Accumulated other comprehensive income		<u>(44,455)</u>	<u>(14,492)</u>
Total shareholder's equity		<u>1,205,894</u>	<u>1,199,315</u>
Total liabilities and shareholder's equity		<u>\$ 3,850,756</u>	<u>\$ 3,350,456</u>

See accompanying notes to consolidated financial statements

The consolidated financial statements were approved by the Board of Directors and authorised for issue on March 2, 2016. They were signed on its behalf

by:  Director

 Director

TOKIO MILLENNIUM RE AG

Consolidated Statement of Comprehensive Income

Years Ended December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

	<u>Note</u>	<u>2015</u>	<u>2014</u>
Revenue			
Reinsurance premiums assumed	4	\$ 1,546,288	\$ 1,172,166
Change in unearned premiums		<u>(411,584)</u>	<u>(218,814)</u>
Reinsurance premiums earned – assumed		<u>1,134,704</u>	<u>953,352</u>
Reinsurance premiums ceded	22	206,970	162,907
Change in prepaid reinsurance		<u>(3,822)</u>	<u>(9,358)</u>
Reinsurance premiums earned – ceded		<u>203,148</u>	<u>153,549</u>
Net premiums earned		931,556	799,803
Catastrophe bond income		561	1,873
Net derivative income	9	8,657	18,703
Other underwriting income		<u>4,514</u>	<u>3,181</u>
Total operating income		945,288	823,560
Net investment income	7	<u>35,310</u>	<u>36,420</u>
Total revenue		<u>980,598</u>	<u>859,980</u>
Expenses			
Loss and loss expenses incurred		509,514	467,670
Losses recoverable from reinsurers		<u>(2,084)</u>	<u>(4,239)</u>
Net loss and loss expenses incurred	17	507,430	463,431
Acquisition expenses	23	251,546	220,927
Profit commission		9,787	4,637
Other underwriting expenses		1,514	1,465
General and administrative expenses	24, 25	106,358	83,345
Foreign exchange (gains) losses	24	<u>(5,087)</u>	<u>11,661</u>
Total expenses		<u>871,548</u>	<u>785,466</u>
Profit before tax		109,050	74,514
Tax expense	14	<u>(1,238)</u>	<u>(3,244)</u>
Profit		<u>\$ 107,812</u>	<u>\$ 71,270</u>

TOKIO MILLENNIUM RE AG

Consolidated Statement of Comprehensive Income (continued)

Years Ended December 31, 2015 and 2014
(Expressed in thousands of United States Dollars)

	<u>2015</u>	<u>2014</u>
Other comprehensive income (loss)		
<i>Items that are or may be reclassified to profit or loss</i>		
Net change in unrealised (losses) gains on investments	\$ (23,562)	\$ 4,311
Net change in tax reserve for unrealised gains on investments	717	(948)
Change in foreign currency translation adjustment	<u>(6,986)</u>	<u>(6,302)</u>
	(29,831)	(2,939)
<i>Item that will not be reclassified to profit or loss</i>		
Change in retirement benefit obligation	<u>(132)</u>	<u>(2,075)</u>
Other comprehensive loss, net of tax	(29,963)	(5,014)
	<u> </u>	<u> </u>
Total comprehensive income	<u>\$ 77,849</u>	<u>\$ 66,256</u>

See accompanying notes to consolidated financial statements

TOKIO MILLENNIUM RE AG

Consolidated Statement of Changes in Shareholder's Equity

Years Ended December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

	Share capital	Contributed surplus	Retained earnings	Unrealised gain (loss) on investments	Tax reserve on unrealised investment gains	Foreign currency translation reserve	Retirement benefit obligation	Accumulated other comprehensive income	Total
Balance January 1, 2014	\$ 250,000	\$ 400,000	\$ 632,537	\$ 3,516	\$ –	\$ (12,582)	\$ (412)	\$ (9,478)	\$ 1,273,059
Profit	–	–	71,270	–	–	–	–	–	71,270
Other comprehensive income (loss)	–	–	–	4,311	(948)	(6,302)	(2,075)	(5,014)	(5,014)
Dividends	–	–	(140,000)	–	–	–	–	–	(140,000)
Balance December 31, 2014	\$ 250,000	\$ 400,000	\$ 563,807	\$ 7,827	\$ (948)	\$ (18,884)	\$ (2,487)	\$ (14,492)	\$ 1,199,315
Profit	–	–	107,812	–	–	–	–	–	107,812
Other comprehensive income (loss)	–	–	–	(23,562)	717	(6,986)	(132)	(29,963)	(29,963)
Dividends	–	–	(71,270)	–	–	–	–	–	(71,270)
Balance December 31, 2015	\$ 250,000	\$ 400,000	\$ 600,349	\$ (15,735)	\$ (231)	\$ (25,870)	\$ (2,619)	\$ (44,455)	\$ 1,205,894

See accompanying notes to consolidated financial statements

TOKIO MILLENNIUM RE AG

Consolidated Statement of Cash Flows

Years Ended December 31, 2015 and 2014
(Expressed in thousands of United States Dollars)

	<u>Note</u>	<u>2015</u>	<u>2014</u>
Cash flows from operating activities			
Profit before tax		\$ 109,050	\$ 74,514
Adjustments for:			
Depreciation of property and equipment	15	3,997	3,504
Amortisation of intangible assets	16	4,059	3,735
Amortisation of investments		7,814	8,184
Interest income		(42,498)	(42,346)
Net gain on sale of investments	7	(2,864)	(3,309)
Foreign exchange gains on cash and cash equivalents		(4,303)	(2,622)
Foreign exchange losses on investments		11,340	2,147
Net impairment and other investment losses (gains)		2,582	(194)
Retirement benefit cost		278	(15)
Change in:			
Funds withheld		(26,195)	(3,292)
Premiums receivable		(241,816)	(119,149)
Deposit assets	12	41,500	(337,677)
Prepaid reinsurance premiums		(3,476)	(9,262)
Fair value of derivative assets		(2,967)	12,233
Outstanding losses recoverable from reinsurers		(1,257)	(20,804)
Deferred acquisition expenses		(126,410)	(65,612)
Unearned profit commission		(4,281)	2,967
Other assets		4,177	(20,623)
Outstanding losses and loss expenses		158,395	115,614
Liability for collateral held on behalf of counterparties		(81,633)	292,372
Reinsurance balances payable		36,084	34,801
Deposit liabilities	12	(41,500)	337,677
Unearned premiums		394,520	205,532
Fair value of derivative liabilities		1,757	(8,115)
Deferred commission income		671	1,002
Accounts payable and accrued expenses		17,317	881
Deferred fee income		<u>(806)</u>	<u>2,620</u>
Cash provided by operating activities		213,535	464,763
Income taxes paid		<u>(1,073)</u>	<u>(4,114)</u>
Net cash provided by operating activities		<u>\$ 212,462</u>	<u>\$ 460,649</u>

TOKIO MILLENNIUM RE AG

Consolidated Statement of Cash Flows (continued)

Years Ended December 31, 2015 and 2014
(Expressed in thousands of United States Dollars)

	<u>2015</u>	<u>2014</u>
Cash flows from investing activities		
Interest received	\$ 38,062	\$ 42,707
Purchase of investments	(1,109,741)	(893,417)
Proceeds on sales and maturities of investments	1,036,079	553,198
Purchase of property and equipment	(2,068)	(4,566)
Purchase of intangible assets	(5,298)	(5,658)
Payable for investments purchased	<u>8,748</u>	<u>—</u>
Net cash used in investing activities	<u>(34,218)</u>	<u>(307,736)</u>
Cash flows from financing activities		
Dividends paid	(71,270)	(140,000)
Proceeds from issuance of note payable	<u>—</u>	<u>25,000</u>
Net cash used in financing activities	<u>(71,270)</u>	<u>(115,000)</u>
Net increase in cash and cash equivalents	106,974	37,913
Foreign exchange gains on cash and cash equivalents	4,303	2,622
Cash and cash equivalents at beginning of year	<u>167,760</u>	<u>127,225</u>
Cash and cash equivalents at end of year	<u>\$ 279,037</u>	<u>\$ 167,760</u>

See accompanying notes to consolidated financial statements

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

1. General

Tokio Millennium Re AG (the "Company" or "TMR AG"), formerly known as Tokio Millennium Re Ltd., is a Swiss-based reinsurance company and is licensed and regulated by the Swiss Financial Market Supervisory Authority ("FINMA"). TMR AG's registered office is located at Beethovenstrasse 33, 8002 Zurich, Switzerland. The Company is a wholly-owned subsidiary of Tokio Marine and Nichido Fire Insurance Co., Ltd. The ultimate parent company is Tokio Marine Holdings, Inc., a company incorporated in Japan.

The Company was formed in Bermuda on March 15, 2000 and redomesticated to Switzerland on October 15, 2013. TMR AG has become subject to Swiss law without liquidation and re-establishment.

The Company participates in various excess of loss property catastrophe, workers' compensation catastrophe, crop/hail and terrorism reinsurance contracts. Catastrophe reinsurance covers unpredictable events such as hurricanes, windstorms, hailstorms, earthquakes, fires, freezes, floods and other man-made or natural disasters. The Company also offers non-catastrophe property and casualty covers on both proportional and per risk excess of loss treaties, with an emphasis on the higher frequency/lower severity category of exposures. Casualty lines of business include motor, general liability, excess casualty, auto liability, employer's liability, professional liability, workers' compensation, directors and officers, errors and omissions and medical malpractice. In addition, TMR AG assumes credit insurance contracts.

The Company also provides non-traditional customised reinsurance and financial solutions for its clients' worldwide property and casualty exposures on both a treaty and facultative basis.

A branch in the United Kingdom ("TMRUK") was formed on September 17, 2014. On April 8, 2015, TMR AG received authorisation from the Prudential Regulation Authority to operate as a branch in the U.K. TMRUK commenced writing business on July 1, 2015 which included the new and renewal business formerly written by TMR AG's affiliate, Tokio Millennium Re (UK) Ltd.

The Company formed a branch in the United States ("TMRUS") and was issued a license by the New York State Department of Financial Services on June 2, 2014. TMRUS was established to further expand TMR AG's non-catastrophe portfolio and focuses on non-catastrophe product lines.

TMR Management, Inc. ("TMRM"), a wholly-owned subsidiary of the Company, was incorporated in the State of Connecticut, United States of America on December 18, 2013, with an initial share capital of \$1,000 (authorised and issued shares of 1,000 at \$1 per share). TMRM, pursuant to a management agreement with TMR AG, acts as a manager for TMRUS.

On October 15, 2013, the Company formed a branch in Bermuda and is licensed as a Class 3B reinsurer under the Insurance Act, 1978 of Bermuda and related regulations to write all classes of property and casualty business. The Company's branch in Switzerland, originally formed on August 31, 2010, was discontinued as part of the redomestication of the Company effective October 15, 2013.

Tokio Millennium Agency Ltd. ("TMA"), a wholly-owned subsidiary of the Company, was incorporated in Bermuda on May 28, 2003, with an initial share capital of \$12,000. Its primary activity was to facilitate risk swap agreements between Tokio Marine and Nichido Fire Insurance Co., Ltd. and other insurance companies for which it received agency fees. In 2012, TMA was renamed Tokio Solution Management Ltd. ("TSM"). The Bermuda Monetary Authority ("BMA") issued a license to TSM to conduct business as an insurance management company on August 24, 2012.

TSM manages and facilitates transactions through Shima Reinsurance Ltd. ("Shima Re") or other third party vehicles. In addition, TSM facilitates clients' fronting and leveraging agreements and also provides professional claims and loss reserving services.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

1. General (continued)

The Company's wholly owned subsidiary, Shima Re, a Class 3 segregated accounts company, was incorporated under the laws of Bermuda on July 30, 2012 and registered under the Segregated Companies Act of 2000. With TSM as its manager, Shima Re provides its clients with a platform to transform either fronted or direct reinsurance transactions.

The Company formed a branch in Australia on October 22, 2010. The Australian Prudential Regulation Authority ("APRA") issued a license to the Company's Australian branch to conduct business as a general insurer on March 1, 2011.

2. Basis of preparation

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

When IFRS is silent, as it is in respect of the measurement of certain insurance products, the IFRS framework (IFRS 4, *Insurance Contracts*) allows reference to another comprehensive body of accounting principles. Accordingly, to the extent that IFRS 4 does not specify the recognition or measurement of insurance contracts, transactions reported in these consolidated financial statements have been prepared in accordance with another comprehensive body of accounting principles for insurance contracts, namely U.S. GAAP.

(b) Basis of measurement

The consolidated financial statements are presented in U.S. dollars, which is the Company's reporting currency. They are compiled on a going concern basis. The consolidated financial statements have been prepared on the historical cost basis. See Note 3 for exceptions to this.

(c) Use of estimates and judgments

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

The most significant estimate made by management is in relation to outstanding losses and loss expenses. Estimates in relation to losses and loss expenses are discussed in Note 3(b) – Insurance Contracts. Also refer to Note 17 – Insurance Liabilities.

3. Summary of significant accounting policies

(a) Basis of consolidation

The financial statements consolidate the accounts of the Company, its branches and its wholly owned subsidiaries. A subsidiary is an entity that is controlled by TMR AG. TMR AG controls an entity when it is exposed to or has the rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of the subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies. All significant intercompany transactions and balances are eliminated on consolidation.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(b) Insurance Contracts

Classification

Contracts that transfer significant insurance risk are considered insurance contracts, while contracts without significant insurance risk are classified as investment contracts.

Reinsurance premiums assumed and acquisition costs

Reinsurance premiums assumed are recorded on the accruals basis and are included in income over the period of exposure to risk with the unearned portion deferred in the consolidated balance sheet. Premiums assumed are stated before the deductions of brokerage, commissions and taxes.

For excess of loss contracts, the ultimate premium is estimated at contract inception. Subsequent premium adjustments, if any, are recorded in the period in which they are determined. For proportional treaties, the amount of premium is normally estimated at inception by management based on information provided by the ceding company. The Company accounts for such premium using initial estimates, which are reviewed regularly with respect to the actual premium reported by the ceding company. Changes in estimates are recognised in the period in which they are determined.

For certain property catastrophe contracts, the Company earns reinstatement premiums upon the occurrence of a loss under the reinsurance contract. Reinstatement premiums are calculated in accordance with the contract terms based upon the ultimate loss estimate associated with each contract.

Premiums for retroactive exposures in reinsurance contracts are earned at inception of the contract, as all of the underlying loss events covered by these exposures occurred in the past. Any underwriting profit at inception related to retroactive exposures in a reinsurance contract is deferred and recognised over the estimated future payout of the outstanding losses and loss expenses. Any underwriting loss at inception related to retroactive exposures in a reinsurance contract is recognised immediately.

Premiums receivable from brokers, insureds and cedants are recognised when due and 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 expenses, mainly commissions and brokerage, related to unearned premiums are deferred and amortised to income over the periods in which the premiums are earned. The method followed in determining the deferred acquisition expenses limits the amount of the deferral to its realisable value, by giving consideration to losses and expenses expected to be incurred as premiums are earned.

Where applicable, no claims bonuses and profit commissions are accrued based on claims experience.

Reinsurance premiums ceded

Reinsurance premiums ceded comprise the cost of reinsurance contracts entered into. Premiums ceded are accounted for in the period in which the contract is bound and are similarly earned over the period of exposure to risk, with the unearned portion being deferred in the consolidated balance sheet as prepaid reinsurance premiums.

Premiums payable to agents and brokers are recognised when due.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(b) Insurance Contracts (continued)

Outstanding losses and loss expenses

Losses and loss expenses paid are recorded when advised by the ceding insurance companies. Outstanding losses comprise estimates of the amount of reported losses and loss expenses received from the ceding insurance companies plus a provision for losses incurred but not reported ("IBNR"). The IBNR provision is estimated by management based on reports from industry sources, including initial estimates of aggregate industry losses, individual loss estimates received from ceding companies and brokers, output from commercially available catastrophe loss models and actuarial analysis using historical data available to the Company on the business assumed together with industry data.

Given the inherent nature of major catastrophic events, considerable uncertainty underlies the assumptions and associated estimated reserve for losses and loss expenses. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments, if any, are reflected in income in the period in which they are determined.

Due to the inherent uncertainty in estimating the liability for losses and loss expenses, there can be no assurance that the ultimate liability will not be settled for a significantly greater or lesser amount than that recorded.

Based on the current assumptions used, management believes that the Company's recorded amount is a reasonable estimate of the ultimate cost of losses incurred to the consolidated balance sheet date. Reserves for non-catastrophe property and casualty covers are based on individual claims, case reserve and other reserve estimates reported by insureds and ceding companies as well as the Company's actuarial estimates of ultimate losses. Inherent in the estimates of ultimate losses are expected trends in claim severity and frequency and other factors which could vary significantly as claims are settled. The Company does not have the benefit of a significant amount of its own historical experience with non-catastrophe lines of business. Accordingly, the setting and reserving for incurred losses in these lines of business could be subject to greater variability.

Ultimate losses may vary materially from the amounts provided in the consolidated financial statements. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments, if any, are reflected in the consolidated statement of comprehensive income in the period in which they become known and are accounted for as changes in estimates.

Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities. Reinsurance recoverable on dual trigger reinsurance contracts require the Company to estimate its ultimate losses applicable to these contracts as well as estimate the ultimate amount of industry losses that will be reported by the applicable statistical reporting agency, as per contract terms.

Liability adequacy tests

At each balance sheet date, the Company performs a liability adequacy test using current best estimates of future cash outflows generated by its reinsurance contracts, plus any investment income thereon. If, as a result of these tests, the carrying amount of the Company's reinsurance 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.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(c) *Financial Instruments*

Cash and cash equivalents

The Company considers all cash at bank and on hand, short-term deposits and other short-term highly liquid investments that are subject to insignificant risk of changes in fair value as cash and cash equivalents. Cash equivalents are financial investments with less than three months to maturity at the date of acquisition.

Cash and cash equivalents are carried in the consolidated balance sheet at amortised cost. Carrying amounts approximate fair value due to the short-term nature and high liquidity of the instruments.

Funds withheld

Funds withheld are contractual receivables due to reinsurers from their clients; they are valued at original cost (nominal amount) at the date of acquisition. In addition, there are amounts arising from the application of the deposit method of accounting included. Appropriate allowance is made for credit risks.

Investments

The Company's investments comprise of short-term investments and investments in fixed interest, equity and other securities and catastrophe bonds. The classification is determined at the time of initial purchase. Purchases and sales of investments are recognised at fair value, including transaction costs, on the trade date.

The cost of investments is adjusted for amortisation of premiums and discounts. Realised gains and losses on investments are recognised in net investment income using the specific identification method. Interest income on investments is accrued to the consolidated balance sheet date.

Investments are derecognised when the Company has transferred substantially all of the risks and rewards of ownership. On derecognition of an available for sale investment, previously recorded unrealised gains and losses are removed from accumulated other comprehensive income in shareholder's equity and included in current period income.

The Company, together with its investment managers, reviews investments on an individual security basis for evidence of impairment on at least a quarterly basis as part of the financial close process. Impairment losses are recognised when there is objective evidence that the Company will be unable to collect all amounts due according to contractual terms of the individual security.

An available for sale debt security is impaired if there is objective evidence that a loss event has occurred after initial recognition of the security and up to the relevant consolidated balance sheet date, and that loss event has negatively affected the estimated future cash flows, i.e., amounts due according to the contractual terms of the security are not considered collectible. Impairment losses on available for sale debt securities are recognised by reclassifying the losses from accumulated other comprehensive income to the consolidated statement of comprehensive income. The amount reclassified is the difference between the amortised cost and the current fair value, less any impairment loss previously recognised in profit or loss. If the fair value of an impaired available for sale debt security subsequently increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through profit or loss; otherwise it is reversed through other comprehensive income.

An available for sale equity security is considered to be impaired if there is objective evidence that the cost may not be recovered. Objective evidence that the cost may not be recovered, in addition to qualitative impairment criteria, includes a significant or prolonged decline in the fair value below cost. If an available for sale equity security is impaired, any further declines in the fair value at subsequent reporting dates are recognised as impairments. Therefore, at each reporting period, for an equity security that was determined to be impaired, additional impairments are recognised for the difference between the fair value and the original cost basis, less any previously recognised impairment. Reversals of impairments of available for sale equity securities are not recorded through the income statement but recycled out of other comprehensive income when sold.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(c) *Financial Instruments (continued)*

Investments (continued)

The identification of impairment is an inherently uncertain process involving various assumptions and factors, including the financial condition of the counterparty, expected future cash flows, observable market prices, etc. Estimates and assumptions are based on management's judgment and other information available prior to the issuance of the consolidated financial statements. Significantly different results can occur as circumstances change and additional information becomes known.

The Company's investments are managed following prudent standards of diversification. Specific provisions limit the allowable holdings of a single issue and issuers.

Short-term investments

Short-term investments represent bank deposits and investments in money market funds with an original term of greater than 90 days but less than one year. The carrying value reported in the consolidated balance sheet for these short-term investments approximates their fair value due to the short-term nature of the investments.

Fixed interest securities – fair value through profit or loss

This consists of debt securities held for trading and those designated at fair value through profit or loss since acquisition. Any unrealised gains and losses are included in profit or loss. The Company had a New Zealand dollar ("NZD") investment portfolio used to hedge its foreign currency exposure to NZD liabilities. It was designated at fair value through profit and loss upon adoption of IFRS and the portfolio was liquidated in April 2015.

Fixed interest securities – available for sale

This consists of debt securities which are classified as available for sale and are carried at fair value, with any unrealised gains and losses (difference between amortised cost and fair value), with the exception of currency valuation differences, included in accumulated other comprehensive income as a separate component of equity. The amortisation and currency valuation differences are included in profit or loss.

The fair value of fixed interest securities is based on prices provided by internationally recognised independent pricing services. The independent pricing sources obtain actual transaction prices for securities that have quoted prices in active markets. For securities that are not actively traded, the pricing services typically uses "matrix pricing" which uses observable inputs including reported trades, benchmark yields, broker/dealer quotes, interest rate spreads, prepayment spreads and other such inputs from market sources to determine a reasonable fair value.

Investments in catastrophe bonds – available for sale

The Company's investments in catastrophe bonds are classified as available for sale and are carried at fair value, with any unrealised gains and losses (difference between amortised cost and fair value), with the exception of currency valuation differences, included in accumulated other comprehensive income as a separate component of equity. The amortisation and currency valuation differences are included in profit or loss.

Equity securities – available for sale

The Company's equity securities are classified as available for sale and are carried at fair value, with any unrealised gains and losses, with the exception of currency valuation differences, included in accumulated other comprehensive income as a separate component of equity. Currency valuation differences are included in profit or loss.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(c) *Financial Instruments (continued)*

Other securities – fair value through profit and loss

Other securities consist of investments in investment funds organised as limited partnerships and investments in funds organised as limited liability companies. These are designated at fair value through profit or loss since acquisition.

Derivative financial instruments

From time to time, the Company enters into catastrophe swap derivatives, under which certain catastrophe reinsurance exposures are ceded to or assumed from the swap counterparty. The Company does this to facilitate institutional investors who seek to diversify their portfolios by adding non-correlated reinsurance risks to their portfolio. The Company transforms such risks by selling reinsurance and buying derivatives from the institutional investors, or vice versa. The Company earns a fee for its role in facilitating such transactions. Since there is no right of offset, all transactions are presented on a gross basis in the consolidated financial statements. Although the derivatives provide an economic hedge against the assumed or ceded reinsurance contract, the Company designates its derivatives as non-hedging derivative instruments based upon criteria established by IAS 39, *Financial Instruments: Recognition and Measurement*. Catastrophe swaps are recorded at fair value with changes in fair values recorded in the consolidated statement of comprehensive income. Fair value is estimated by management primarily based on the unexpired period of risk, an evaluation of the probability of loss and other unobservable inputs. The Company's catastrophe swap derivatives are initially priced at fair value in a non-stressed market and amortisation reflects the change in fair value in the absence of any loss events. The inputs for catastrophe swap derivatives are purely based on management's evaluation and are unobservable.

Receivables

The Company's receivables have fixed or determinable payments and are carried at cost less any provision for impairment in value. Refer to Note 3(b) for discussion on receivables arising from reinsurance contracts.

Impairment of financial assets

Objective factors that are considered when determining whether a financial asset or group of financial assets may be impaired include, but are not limited to, the following:

- negative rating agency announcements in respect of investment issuers, reinsurers and debtors;
- significant reported financial difficulties of investment issuers, reinsurers and debtors;
- actual breaches of credit terms such as persistent late payments or actual default;
- the disintegration of the active market(s) in which a particular asset is traded or deployed; and
- adverse economic or regulatory conditions that may restrict future cash flows and asset recoverability.

(d) *Deposit assets and liabilities*

Certain contracts do not transfer sufficient insurance risk and are accounted for using the deposit method of accounting. Management exercises judgment in determining whether contracts contain sufficient risk to be accounted for as reinsurance contracts. Under the deposit method of accounting, the deposit asset or liability is initially measured based on the consideration paid or received. In subsequent periods, the deposit asset or liability is adjusted by calculating the effective yield on the deposit to reflect actual receipts or payments to date and future expected receipts or payments.

The Company earns fee income for the provision of these contracts. Fee income is based upon the terms of the contracts, with the unearned portion deferred in the consolidated balance sheet, as deferred fee income. The revenue and expense recorded for such contracts is included in other underwriting income.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(e) *Property and equipment*

Property and equipment are stated at cost less accumulated depreciation calculated on a straight-line basis over the estimated useful lives of the assets. The specific depreciable rates of the significant asset classes are as follows:

Computer equipment	3 years
Fixtures and fittings	5 years
Leasehold improvements	Over the term of the underlying lease
Motor vehicles	5 years
Office equipment	4 years

(f) *Intangible assets*

Intangible assets are stated at cost less amortisation calculated on a straight-line basis over the estimated useful lives of the assets. The Company's intangible assets comprise of computer software with a specific amortisation rate of 3 years.

(g) *Impairment of non-financial assets*

Assets that are subject to amortisation are tested for impairment when there is an indication of a possible impairment at the reporting date.

Objective factors that are considered when determining whether a non-financial asset (such as an intangible asset or item of property and equipment) or group of non-financial assets may be impaired include, but are not limited to, the following:

- adverse economic, regulatory or environmental conditions that may restrict future cash flows and asset usage and/or recoverability;
- the likelihood of accelerated obsolescence arising from the development of new technologies and products; and the disintegration of the active market(s) to which the asset is related.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units).

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior periods. A reversal of an impairment loss is recognised as income immediately.

(h) *Bad debt provision*

The Company reviews receivables on a quarterly basis and bad debt provision is recorded only to the extent that repayment is unlikely or no longer expected in full amount. In addition, the Company considers known and emerging credit events to determine if other provisions are necessary.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(i) Translation of foreign currencies

The consolidated financial statements of the Company are 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 profit or loss. 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 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 shareholder's equity.

The functional currency of the Bermuda and U.S. branches is the U.S. dollar. The functional currencies of the Company's Swiss, Australian and U.K. operations are the Euro, Australian dollar and Pound Sterling, respectively. In translating the financial results of those entities whose functional currency is other than the U.S. dollar reporting currency, assets and liabilities are converted into U.S. dollars using the rates of exchange in effect at the balance sheet dates, and revenues and expenses are converted using the average foreign exchange rates for the period. The effect of translation adjustments are reported in the consolidated balance sheet and consolidated statement of changes in shareholder's equity as a foreign currency translation adjustment, a separate component of accumulated other comprehensive income.

(j) Leases

All leases are classified as operating leases and are not recognised in the consolidated balance sheet. Rentals payable under operating leases are charged to income on a straight-line basis over the lease term.

(k) Long term incentive compensation plan

In 2008, the Board approved a compensation program for employees. The compensation program consists of accumulation units which are based on movements in the net asset value of the Company and are settled in cash once a cliff vesting service period has been rendered. The Company accounts for the compensation program in accordance with IFRS 2, *Share-based Payment*. As a liability award, the cost is remeasured at each reporting period until the settlement date. The cost of such services is recognised over the service period in the consolidated statement of comprehensive income. The grant date of the units is determined to be upon authorisation of the awards in accordance with the Company's governance structure.

(l) Taxation

The Switzerland based operating entity and the Australia, United States and United Kingdom branches of the Company operate in jurisdictions where they are subject to taxation. Income taxes have been provided in accordance with the provisions of IAS 12, *Income Taxes*. Current and deferred income taxes are charged or credited to profit or loss. Deferred income taxes are provided for all temporary differences between the bases of assets and liabilities used in the consolidated balance sheet and those used in the various jurisdictional tax returns. Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

The Company recognises a tax benefit relating to uncertain tax positions only where the position is probable to be sustained assuming examination by tax authorities. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

(l) *Taxation (continued)*

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.

(m) *Retirement benefit obligation*

Defined contribution plans

TMR AG has defined contribution plans where the Company pays fixed contributions into a separate entity from which post-employment and other benefits are paid. The Company has no legal or constructive obligation to pay further contributions if the plan does not hold sufficient assets to pay employees the benefits relating to employee service in the current and prior periods. Payments to the defined contribution plans are recognised as an expense when employees have rendered services entitling them to the contributions. This is generally in the year of contribution. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

Defined benefit plan

The Company also has a defined benefit post-retirement plan in relation to the Switzerland operation. The net retirement benefit obligation in relation to this plan is based on, among other things, assumptions of the discount rate, estimate return on plan assets, and salary increases. The cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at the end of each reporting period. Actuarial gains and losses are recognised in other comprehensive income. Past service costs are recognised immediately in the period of the plan amendment. The Company recognises the overfunded or underfunded status of the defined benefit post-retirement plan as an asset or liability in its consolidated balance sheet and recognises changes in the funded status in the year in which the changes occur through other comprehensive income. Any asset resulting from this calculation is limited to the sum of any cumulative unrecognised net losses and the present value of any economic benefits available in the form of refunds or reductions in future contributions to the plan.

Accounting standards and amendments issued but not yet adopted

Accounting standards issued and amendments to published standards that are not yet effective up to the date of issuance of the Company's consolidated financial statements are listed below. The Company intends to adopt these standards when they become effective.

IFRS 9, *Financial Instruments*

IFRS 9, published in July 2014, replaces the existing guidance in IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 includes revised guidance on the classification and measurement of financial statements, including a new expected credit loss model for calculating impairment of financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

IFRS 9 is effective for annual reporting periods beginning on or after January 1, 2018, with early adoption permitted. The new standard may have an effect on the classification and measurement of the Company's financial assets. The Company is in the process of analysing the impact of this Standard on its consolidated financial statements.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

Accounting standards and amendments issued but not yet adopted (continued)

Amendments to IAS 16, Property, plant and equipment, and IAS 38, Intangible assets, regarding depreciation and amortisation

These amendments to IAS 16 and IAS 38, published in May 2014, have clarified that the use of revenue-based methods to calculate depreciation of an asset is not appropriate because the revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The IASB has also clarified that the revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. These amendments are applicable for annual periods beginning on or after January 1, 2016 and are not expected to have an impact on the Company's results.

Amendments to IAS 27, Separate financial statements, regarding the equity method

These amendments to IAS 27, published in August 2014, allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. These amendments are applicable for annual periods beginning on or after January 1, 2016 and are not expected to have a material impact on the Company's results.

Amendments to IFRS 10, Consolidated financial statements, and IAS 28, Investments in associates and joint ventures

These amendments to IFRS 10 and IAS 28, published in September 2014, address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. These amendments are applicable for annual periods beginning on or after January 1, 2016 and are not expected to have a material impact on the Company's results.

Annual improvements to IFRSs 2012--2014 Cycle

In September 2014, the IASB published its annual amendments to IFRSs and the related bases for conclusions and guidance. The IASB uses the annual improvements process to make necessary, but non-urgent, amendments to IFRSs that will not be included as part of a major project. These amendments affect four standards, namely: IFRS 5, *Non-current assets held for sale and discontinued operations*, regarding methods of disposal; IFRS 7, *Financial instruments: Disclosures* (with consequent amendments to IFRS 1), regarding servicing contracts; IAS 19, *Employee benefits*, regarding discount rates; and IAS 34, *Interim financial reporting*, regarding disclosure of information. The amendments primarily remove inconsistencies and clarify wording. The amendments are effective for annual periods beginning on or after January 1, 2016 and will have no material impact on the Company's consolidated financial statements.

Amendments to IAS 1, Presentation of financial statements, on the disclosure initiative

These amendments to IAS 1, published in December 2014, are part of IASB's initiative to improve presentation and disclosure in financial reports. These amendments clarify guidance in IAS 1 on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies. The amendments are effective for annual periods beginning on or after January 1, 2016 and will have no material impact on the Company's consolidated financial statements.

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Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

3. Summary of significant accounting policies (continued)

Accounting standards and amendments issued but not yet adopted *(continued)*

IFRS 15, Revenue from contracts with customers

IFRS 15, published in May 2014, is a converged standard from the IASB and FASB on revenue recognition. IFRS 15 will improve the financial reporting of revenue and improve comparability of the top line in financial statements globally. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

IFRS 16, Leases

On January 13, 2016, the IASB published IFRS 16, *Leases*, which replaces the current guidance in IAS 17, *Leases*. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a "right-of-use asset" for virtually all lease contracts. The IASB included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for a consideration.

IFRS 16 is effective for annual reporting periods beginning on or after January 1, 2019. Earlier application is permitted, but only in conjunction with IFRS 15, *Revenue from contracts with customers*. The Company is in the process of analysing the impact of this Standard on its consolidated financial statements.

4. Risk Disclosures

The Company, through its Enterprise Risk Management Unit ("ERM"), Risk Management Working Group and Risk Management Committee ("RMC"), seeks to identify all material risks inherent in its business including emerging risks; to understand the manifestations of each risk; and to assess, control, mitigate and manage these risks appropriately.

The objectives of TMR AG's risk management process are to ensure that:

- all material risks are proactively identified;
- the potential to cause losses or generate profits is understood and assessed;
- appropriate action is taken to manage the assumption of each risk based on that assessment and the Company's stated risk appetite;
- an appropriate level of capital is held to cover financial and non-financial risks from all sources; and
- following a severe catastrophic event(s), appropriate capital action can be executed to remain solvent and meet its obligations under reinsurance contracts.

The oversight of the Company's risk management program is provided by the Board of Directors and senior management who are assisted by the RMC. The Board is charged with setting the orientation of TMR AG's business. It pays particular attention to business strategy, capital allocation, risk control framework and ensures that they are implemented.

The Company is exposed to risks from several sources. These include underwriting risk, market risk, credit risk, liquidity risk, operational risk and strategic risk.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

A. Underwriting Risk

Underwriting risk consists of premium risk, catastrophe risk and reserve risk.

Underwriting risk may be due to either the acceptance of risks that do not comply with the Company's underwriting guidelines and corporate strategy, or the acceptance of risks that result in losses and expenses greater than it had anticipated at the time of underwriting.

As a reinsurance company, TMR AG is in the business of taking underwriting risk and therefore has a high appetite for underwriting risk. TMR AG's risk limits are defined in the TMR AG Risk Appetite and Risk Tolerance/Limit Policy for underwriting risk and reserve risk combined.

The Company has underwriting guidelines in place that clearly define the territorial scope, risks to be written, business to be avoided, acceptance limits, maximum policy period, maximum net retention, outward reinsurance, security requirement (for retrocessionaires) and underwriting authority.

As a part of the risk control strategy and governance at TMR AG, all contracts must be reviewed and approved by an Underwriting Committee before they can be bound.

The Company employs experienced catastrophe analysts and modelers, as well as experienced and credentialed actuaries, to perform pricing analyses to ensure that each risk is adequately priced.

Premium Risk

Premium risk is the risk that the premium to be earned over the next twelve-month period from the in-force, new or renewal reinsurance contracts is insufficient to cover the claim costs, claim adjustment expenses as well as the acquisition costs to be incurred by those contracts over the same period.

The Company has purchased retrocessions in the past several years to enhance the diversity of the portfolio, improve capital efficiency, manage the net retention and protect the capital of TMR AG. The Company will continue to utilize this important risk management tool when the pricing and risk mitigation impact justifies doing so.

Details of annual premiums assumed by geographic area of risk insured are provided below:

<u>Geographic area of risk insured</u>	2015		2014	
	<u>Reinsurance premiums assumed</u>	<u>Percentage of total</u>	<u>Reinsurance premiums assumed</u>	<u>Percentage of total</u>
North America	\$ 1,260,401	81.5 %	\$ 899,041	76.7 %
Europe	150,418	9.7 %	156,261	13.3 %
Worldwide	71,857	4.7 %	62,860	5.4 %
Australasia	41,912	2.7 %	48,806	4.2 %
Other	21,700	1.4 %	5,198	0.4 %
Total	<u>\$ 1,546,288</u>	<u>100.0 %</u>	<u>\$ 1,172,166</u>	<u>100.0 %</u>

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

A. Underwriting Risk (continued)

Premium Risk (continued)

Details of annual premiums assumed by line of business are provided below:

<u>Line of business</u>	2015		2014	
	<u>Reinsurance premiums assumed</u>	<u>Percentage of total</u>	<u>Reinsurance premiums assumed</u>	<u>Percentage of total</u>
Property	\$ 861,052	55.7 %	\$ 556,801	47.5 %
Casualty	535,488	34.6 %	517,982	44.2 %
Specialty	94,936	6.1 %	76,757	6.5 %
Multi-line	54,812	3.6 %	20,626	1.8 %
Total	<u>\$ 1,546,288</u>	<u>100.0 %</u>	<u>\$ 1,172,166</u>	<u>100.0 %</u>

Catastrophe Risk

Catastrophe risk is the risk that the premium to be earned over the next twelve-month period from the catastrophe exposed reinsurance contracts (in-force, new or renewal) is insufficient to cover potential claim costs, claim adjustment expenses as well as the acquisition costs associated with those contracts that may originate from extreme or exceptional catastrophic events over the same period, such as hurricanes, earthquakes, windstorms, landslides and terrorist attacks.

Catastrophe risk is classified as a separate and distinct class of underwriting risk mainly due to its low-frequency and high severity characteristics, its potential to affect numerous contracts simultaneously and inflict significant erosion of TMR AG's capital.

A core element of TMR AG's book of business continues to be property catastrophe reinsurance. Therefore, TMR AG has a high appetite for catastrophe risk as long as this business is adequately priced. The Company writes reinsurance risks for periods of mainly one year so that the contracts can be assessed for pricing and terms and adjusted to reflect any changes in market conditions.

The Company has made a series of strategic moves to diversify, spread and dilute its catastrophic exposures as well as optimise its underwriting portfolio through geographical diversification and by writing casualty and specialty lines and lower layers of business.

Catastrophe risk is the dominant contributor and driver of TMR AG's total risk. TMR AG's catastrophe exposures are managed by limiting the amount of exposure in any one geographic zone.

Retrocession is purchased to enhance the diversity of TMR AG's portfolio, maintain the net retention and even out peak exposures and more effectively manage the volatility of TMR AG's book of business.

Reserve Risk

Reserve risk is the risk that the best (point) estimate of unpaid loss and loss adjustment expense reserves are inadequate to cover all future payments for the full settlement of claims from all prior accident years (on or prior to the valuation date).

Reserve risk is distinct from premium risk and is related to exposures that have already been earned and claims that have already been incurred but have not yet been reported ("IBNR") or fully settled.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

A. Underwriting Risk (continued)

Reserve Risk (continued)

TMR AG has focused on short-tailed property lines of business and has increased its appetite for longer-tailed casualty and specialty lines of business. TMR AG's risk limits are not defined separately for catastrophe risk, non-catastrophe premium risk and reserve risk, but are defined for insurance risk as a whole.

To manage reserving risk, TMR AG's actuarial team use a range of recognised actuarial techniques to project gross premiums written, monitor claims development patterns and stress test ultimate insurance liability balances. An independent actuary also performs a quarterly review for the Company.

A full analysis of loss and loss adjustment expense reserves is performed on a quarterly basis. The reserve analyses are reviewed by and discussed with underwriters, actuaries, claims, finance and senior management prior to submission to the Reserve Committee. The Reserve Committee is appointed by the Executive Committee to review the sufficiency of the estimated loss reserves and to appraise the adequacy and effectiveness of the loss reserving practices of TMR AG. The Reserve Committee is comprised of the Chief Executive Officer ("CEO"), Chief Risk Officer ("CRO"), Chief Operating Officer ("COO"), Chief Financial Officer ("CFO"), Claims unit leader and the reserving actuary.

The table below illustrates the development of the estimates of ultimate cumulative claims for the Company after the end of the underwriting year, illustrating how amounts estimated have changed from the first estimate made.

Estimate of gross ultimate liability

	2009	2010	2011	2012	2013	2014	2015	Total
At end of accident year	\$ 43,975	191,957	515,356	324,587	306,172	431,405	559,407	
One year later	46,829	206,494	529,491	318,895	306,962	428,287		
Two years later	45,644	213,431	504,483	317,360	296,375			
Three years later	45,104	222,238	523,370	308,435				
Four years later	48,962	231,680	517,826					
Five year later	46,231	223,342						
Six years later	46,105							
Ultimate liability 2009 – 2015	46,105	223,342	517,826	308,435	296,375	428,287	559,407	2,379,777
Ultimate liability pre – 2009								445,242
								2,825,019
Payments made 2009 – 2015	(45,756)	(161,273)	(478,942)	(244,999)	(207,156)	(243,633)	(147,670)	(1,529,429)
Payments made pre – 2009								(437,890)
								(1,967,319)
Gross liability at December 31, 2015	\$							857,700

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

A. Underwriting Risk (continued)

Reserve Risk (continued)

Estimate of net ultimate liability

	2009	2010	2011	2012	2013	2014	2015	Total
At end of accident year	\$ 31,810	170,263	377,402	254,757	305,924	386,508	552,426	
One year later	38,565	169,950	389,664	251,442	306,438	383,075		
Two years later	38,249	167,065	369,326	246,004	297,565			
Three years later	38,064	181,156	389,245	242,263				
Four years later	42,028	190,598	383,064					
Five year later	39,312	183,547						
Six years later	39,314							
Ultimate liability 2009 – 2015	39,314	183,547	383,064	242,263	297,565	383,075	552,426	2,081,254
Ultimate liability pre – 2009								392,827
								2,474,081
Payments made 2009 – 2015	(39,034)	(118,509)	(347,870)	(181,682)	(206,975)	(242,826)	(146,607)	(1,283,503)
Payments made pre – 2009								(385,608)
								(1,669,111)
Net liability at December 31, 2015	\$							804,970

A summary of changes in outstanding losses and loss expenses for 2015 and 2014, including outstanding losses recoverable from reinsurers, is presented in Note 17.

The reserves established can be more or less than adequate to meet individual claims arising. The level of uncertainty varies significantly from class to class but can arise from inadequate case reserves for known large losses and catastrophes or from inadequate provision for IBNR. The Company believes that the loss reserves established are adequate, however a 1% improvement/deterioration in the total estimated losses would have an impact on profit before tax of \$8.6 million gain/loss (2014 - \$7.0 million). There was no change to the Company's reserving methodology during the year.

B. Market Risk

Market risk refers to the risk of financial loss due to a change in the value of the financial assets in TMR AG's investment portfolio or a change of market risk factors that affect the value of such assets. TMR AG has identified interest rate risk, foreign exchange risk, revaluation risk, equity price risk and credit spread risk as its main sources of market risk.

Interest Rate Risk

Interest rate risk is a function of general economic and financial market factors (such as the level, trend and volatility of interest rates) as well as the characteristics of the individual fixed interest securities held in TMR AG's investment portfolio. TMR AG cannot control the former but it can control the latter.

Investment guidelines are established to manage this risk. These guidelines set parameters within which the external investment manager must operate. The guidelines are set by the Investment Committee. The Investment Guidelines specify the limitations on the maximum percentage of assets that can be invested in a single issuer or in a single asset class. There are also specific limitations on the maximum maturity for various classes of fixed interest securities and the minimum requirements of credit ratings.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

B. Market Risk (continued)

Interest Rate Risk (continued)

The Company reviews the composition, duration and asset allocation of its investment portfolio on a regular basis in order to respond to changes in interest rates and other market conditions. The Company also mitigates interest rate risk on the investment portfolio by establishing and monitoring duration ranges in its investment guidelines.

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

<u>At December 31, 2015</u>	<u>Fair value</u>	<u>Percentage of portfolio</u>
U.S. treasuries	\$ 280,148	16.7%
Non-U.S. government	59,274	3.5%
Corporate	733,798	43.7%
Agency residential mortgage-backed	219,470	13.1%
Commercial mortgage-backed	57,029	3.4%
Asset-backed	75,622	4.5%
Collateralised debt obligations	161,348	9.6%
Municipals	<u>92,228</u>	<u>5.5%</u>
Total fixed interest securities	<u>\$ 1,678,917</u>	<u>100.0%</u>

<u>At December 31, 2014</u>	<u>Fair value</u>	<u>Percentage of portfolio</u>
U.S. treasuries	\$ 305,657	22.0%
Non-U.S. government	27,595	2.0%
Corporate	612,636	44.0%
Agency residential mortgage-backed	294,456	21.2%
Asset-backed	<u>150,060</u>	<u>10.8%</u>
Total fixed interest securities	<u>\$ 1,390,404</u>	<u>100.0%</u>

The sensitivity of the Company's fixed interest investment portfolio to interest rate movements is detailed below, assuming linear movements in interest rates:

<u>Immediate shift in yield (basis points)</u>	<u>2015</u>	<u>%</u>	<u>2014</u>	<u>%</u>
100	\$ (52,451)	(3.1)	\$ (41,547)	(3.0)
75	(39,413)	(2.3)	(31,126)	(2.2)
50	(26,340)	(1.6)	(20,702)	(1.5)
25	(13,049)	(0.8)	(10,302)	(0.7)
(25)	12,977	0.8	9,943	0.7
(50)	25,849	1.5	17,734	1.3
(75)	37,426	2.2	24,029	1.7
(100)	47,430	2.8	29,773	2.1

The durations of the managed portfolios are as follows:

	<u>2015</u>	<u>2014</u>
Fixed interest securities	3.2	2.93

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

Foreign Exchange Risk

The Company operates internationally and its exposures to foreign exchange risk arise primarily with respect to the U.S. dollar, Australian dollar, Euro, Pound Sterling and New Zealand dollar. The presentation currency of the Company is the U.S. dollar in which the Company reports its consolidated financial results. The effect of this on foreign exchange risk is that TMR AG is exposed to fluctuations in exchange rates for non-U.S. dollar denominated transactions and net assets.

The Company hedges non-U.S. dollar liabilities with non-U.S. dollar assets to mitigate against this risk. The Company's assets and liabilities, categorised at their translated carrying amounts as at December 31, 2015, are as follows:

Assets	US\$	AU\$	Euro	NZ\$	GBP	Other	Total
Cash and cash equivalents	\$ 162,327	\$ 14,260	\$ 29,869	\$ 52,628	\$ 8,750	\$ 11,203	\$ 279,037
Funds withheld	56,891	—	21,972	—	—	133	78,996
Investments	1,666,886	118,100	206,796	—	—	1,995	1,993,777
Accrued interest receivable	8,013	1,151	2,871	—	—	—	12,035
Premiums receivable	596,648	19,335	35,113	1,203	40,271	23,829	716,399
Deposit assets	—	—	296,177	—	—	—	296,177
Prepaid reinsurance premiums	35,062	1,500	—	161	247	706	37,676
Fair value of derivative assets	1,751	—	—	—	—	3,022	4,773
Outstanding losses recoverable from reinsurers	47,157	4,484	721	—	—	368	52,730
Deferred acquisition expenses	300,777	9,114	5,327	135	7,136	5,449	327,938
Unearned profit commission	5,599	357	20	—	16	79	6,071
Deferred tax asset	—	287	—	—	—	2,734	3,021
Property and equipment	9,290	105	2,386	—	59	—	11,840
Intangible assets	8,118	—	301	—	10	—	8,429
Other assets	5,495	1,265	13,633	—	—	1,464	21,857
Total assets at December 31, 2015	\$ 2,904,014	\$ 169,958	\$ 615,186	\$ 54,127	\$ 56,489	\$ 50,982	\$ 3,850,756
Liabilities	US\$	AU\$	Euro	NZ\$	GBP	Other	Total
Outstanding losses and loss expenses	\$ 673,440	\$ 28,501	\$ 61,505	\$ 76,059	\$ 1,439	\$ 16,756	\$ 857,700
Liability for collateral held on behalf of counterparties	3,942	16	229,659	—	—	—	233,617
Reinsurance balances payable	69,373	13,036	968	75	289	5,366	89,107
Deposit liabilities	—	—	296,177	—	—	—	296,177
Payable for investments purchased	8,748	—	—	—	—	—	8,748
Unearned premiums	925,818	51,918	34,554	1,092	47,584	22,381	1,083,347
Fair value of derivative liabilities	1,203	—	—	—	—	3,104	4,307
Deferred commission income	3,220	174	—	21	26	70	3,511
Accounts payable and accrued expenses	25,080	2,053	—	—	6,357	3,075	36,565
Retirement benefit obligation	—	—	—	—	—	3,284	3,284
Deferred fee income	1,950	—	—	—	—	843	2,793
Deferred tax liability	706	—	—	—	—	—	706
Note payable	25,000	—	—	—	—	—	25,000
Total liabilities at December 31, 2015	\$ 1,738,480	\$ 95,698	\$ 622,863	\$ 77,247	\$ 55,695	\$ 54,879	\$ 2,644,862

TOKIO MILLENNIUM RE AG

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(Expressed in thousands of United States Dollars)

4. Risk Disclosures (continued)

Foreign Exchange Risk (continued)

The Company's assets and liabilities, categorised at their translated carrying amounts as at December 31, 2014, are as follows:

Assets	US\$	AU\$	Euro	NZ\$	GBP	Other	Total
Cash and cash equivalents	\$ 86,097	\$ 16,050	\$ 22,294	\$ 33,197	\$ 324	\$ 9,798	\$ 167,760
Funds withheld	39,226	—	13,543	—	—	32	52,801
Investments	1,534,850	114,834	291,037	27,595	—	—	1,968,316
Accrued interest receivable	5,939	1,276	33	351	—	—	7,599
Premiums receivable	377,918	21,495	37,523	661	1,980	35,006	474,583
Deposit assets	—	—	337,677	—	—	—	337,677
Prepaid reinsurance premiums	31,382	2,268	275	—	106	169	34,200
Fair value of derivative assets	1,806	—	—	—	—	—	1,806
Outstanding losses recoverable from reinsurers	50,928	204	—	—	—	341	51,473
Deferred acquisition expenses	178,517	8,061	1,971	91	233	12,655	201,528
Unearned profit commission	1,346	435	9	—	—	—	1,790
Deferred tax asset	—	468	—	—	—	3,462	3,930
Property and equipment	11,491	93	2,185	—	—	—	13,769
Intangible assets	6,939	—	251	—	—	—	7,190
Other assets	3,672	282	21,342	—	—	738	26,034
Total assets at December 31, 2014	\$ 2,330,111	\$ 165,466	\$ 728,140	\$ 61,895	\$ 2,643	\$ 62,201	\$ 3,350,456
Liabilities	US\$	AU\$	Euro	NZ\$	GBP	Other	Total
Outstanding losses and loss expenses	\$ 476,827	\$ 17,420	\$ 72,116	\$ 123,699	\$ —	\$ 9,243	\$ 699,305
Liability for collateral held on behalf of counterparties	4,928	20	310,302	—	—	—	315,250
Reinsurance balances payable	42,686	5,778	966	2,238	239	1,116	53,023
Deposit liabilities	—	—	337,677	—	—	—	337,677
Unearned premiums	559,251	50,229	26,681	756	2,328	49,582	688,827
Fair value of derivative liabilities	2,550	—	—	—	—	—	2,550
Deferred commission income	2,506	289	15	—	11	19	2,840
Accounts payable and accrued expenses	13,715	2,545	—	—	—	2,988	19,248
Retirement benefit obligation	—	—	—	—	—	2,874	2,874
Deferred fee income	3,599	—	—	—	—	—	3,599
Deferred tax liability	948	—	—	—	—	—	948
Note payable	25,000	—	—	—	—	—	25,000
Total liabilities at December 31, 2014	\$ 1,132,010	\$ 76,281	\$ 747,757	\$ 126,693	\$ 2,578	\$ 65,822	\$ 2,151,141

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Notes to Consolidated Financial Statements

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4. Risk Disclosures (continued)

Foreign Exchange Risk (continued)

As at December 31, 2015, the Company used closing rates of exchange for major currencies of: US\$ 1: AU\$ 1.37; US\$ 1: Euro 0.91; US\$ 1: NZ\$ 1.46 and US\$ 1: GBP 0.67.

The impact on net income of a proportional foreign exchange movement of 10 per cent up and 10 per cent down against the U.S. dollar at the year end closing rates, applied on foreign currency net assets, would be an increase or decrease of \$4.0 million (2014: \$0.1 million). This analysis assumes that all other variables, in particular interest rates, remain constant and that the underlying valuation of assets and liabilities in their base currency is unchanged.

Revaluation risk

The Company is subject to revaluation risk as a result of the translation into the Company's U.S. dollar reporting currency of the consolidated balance sheet of the Company's Swiss, Australian and United Kingdom operations, whose functional currencies are the Euro, Australian dollar and Pound Sterling, respectively.

Equity price risk

TMR AG is exposed to equity price risk through its holdings of equity investments. The Company holds equity investments to diversify its investment portfolio and take advantage of expected long-term returns. Strategic asset allocation benchmarks and investment limits are used to manage and monitor these exposures. Equity investments are limited to a relatively small proportion of TMR AG's overall investment portfolio and the equity holdings involved are diversified over a number of companies.

Risks from changes in equity prices are normally associated with decreasing share prices and increasing equity price volatilities. As stock markets also might increase, opportunities may arise from equity investments.

As of December 31, 2015, TMR AG's equity investments amounting to a fair value of \$35.6 million (2014 - \$nil), would have lost \$3.6 million in value assuming equity markets declined by 10%. A 10% upward movement is estimated to have an equal but opposite effect.

Credit spread risk

Our investment strategy acknowledges the risk of declining market values for our fixed interest securities due to the widening of credit spreads. However, for internal risk management and appetite, the Company also takes into account the underlying economics of its business model. The advantage of being able to invest in long duration securities gives the Company the opportunity to invest in securities yielding spreads over the risk-free return and earning this additional yield component.

C. Credit Risk

Credit risk is the risk of potential financial loss due to unexpected default, or deterioration in the credit ratings, of the debtors or counterparties of TMR AG.

Asset credit risk may arise from the unexpected default, or deterioration in the credit ratings, of the debtors or issuers of the financial instruments that TMR AG holds in its investment portfolio, which may cause them to lose value.

Credit risk on premiums receivable from cedants is managed by conducting business with reputable broking organisations, with whom the Company has established relationships, and by rigorous cash collection procedures. The Company also has a broker approval process in place.

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4. Risk Disclosures (continued)

C. Credit Risk (continued)

The table below presents an analysis of the Company's major exposures to counterparty credit risk, based on Standard & Poor's (S&P) or equivalent rating.

	2015						
	Cash and cash equivalents	Funds withheld	Investments (1)	Premiums receivable	Deposit assets	Losses recoverable	Derivative assets
AAA	\$ --	\$ --	\$ 228,460	\$ --	\$ --	\$ --	\$ --
AA+,AA,AA-	61,906	56,045	720,179	156,816	--	--	--
A+,A,A-	217,131	16,941	458,827	266,961	--	42,243	--
BBB+,BBB,BBB-	--	3,933	451,167	23,629	--	--	--
Other/Unknown (2)	--	2,077	135,144	268,993	296,177	10,487	4,773
Total	\$ 279,037	\$ 78,996	\$ 1,993,777	\$ 716,399	\$ 296,177	\$ 52,730	\$ 4,773

	2014						
	Cash and cash equivalents	Funds withheld	Investments (1)	Premiums receivable	Deposit assets	Losses recoverable	Derivative assets
AAA	\$ --	\$ --	\$ 599,122	\$ --	\$ --	\$ --	\$ --
AA+,AA,AA-	63,712	34,103	819,640	35,492	--	--	--
A+,A,A-	104,048	13,281	287,954	179,406	--	43,874	--
BBB+,BBB,BBB-	--	3,164	221,214	32,204	--	--	--
Other/Unknown (2)	--	2,253	40,386	227,481	337,677	7,599	1,806
Total	\$ 167,760	\$ 52,801	\$ 1,968,316	\$ 474,583	\$ 337,677	\$ 51,473	\$ 1,806

- (1) Investments comprise of short-term investments, fixed interest securities, catastrophe bonds, equity securities and other securities
(2) Losses recoverable, deposit assets and derivative assets classified as "Other/Unknown" are fully collateralised

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

	2015	2014
Less than 90 days past due	\$ 18,021	\$ 16,754
Between 91 and 180 days past due	921	341
Over 180 days past due	466	309
Total	\$ 19,408	\$ 17,404

TMR AG has a medium credit risk appetite and elects to take limited credit risk. TMR AG's investment portfolio is appropriately diversified to limit the amounts of credit exposure with respect to particular rating categories and any one issuer. The Investment Committee has established comprehensive guidelines for the Company's investment managers regarding the type, duration and quality of investments acceptable to TMR AG. The performance of investment managers is regularly reviewed to confirm adherence to these guidelines.

TMR AG is also exposed to various counterparty credit risks in the course of conducting its underwriting activities. For example, the Company may have a significant amount of premiums receivables held by its brokers, clients or retrocessionaires.

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4. Risk Disclosures (continued)

C. Credit Risk (continued)

The Company may have posted funds or collateral with clients or other parties as required by the reinsurance contracts. It may have cash deposits in a number of banking institutions. A retrocessionaire may fail to meet its obligations under the retrocession contracts.

This type of credit risk is called counterparty credit risk, which is modeled as a set of frequency-severity distributions resulting from the scenario analyses conducted and maintained by the ERM Unit using TMR AG's risk register.

To control and mitigate counterparty credit risk, the rules of the Risk Appetite and Risk Limit policy concerning counterparty credit risk apply. Most of the retrocessions are either collateralised or placed with highly-rated reinsurers. TMR AG transacts most of its reinsurance businesses through major and reputable brokers and spreads its cash deposits across a number of reputable commercial banks.

In addition, a retrocession arrangement may be made with a retrocessionaire who does not meet the criteria in the Risk Appetite and Risk Limit Policy if collateral with an equivalent or better rating than the minimum A- rating is obtained for an amount at least equal to 100% of the retroceded limit.

At December 31, 2015, the Company's credit risk exposure in relation to losses recoverable from unrated counterparties to reinsurance ceded agreements is \$10.5 million (2014 - \$7.6 million), which is fully collateralised by letters of credit and assets held in trusts by the reinsurance counterparty for the benefit of the Company.

At December 31, 2015, the Company's exposure to credit risk of the counterparties to catastrophe swap agreements is \$4.8 million (2014 - \$1.8 million), which is fully collateralised by letters of credit and assets held in trusts by the reinsurance counterparty for the benefit of the Company.

D. Liquidity Risk

Liquidity risk is the risk that the Company is unable to meet its contractual obligations in a timely manner due to the inability of its investment assets to be sold without causing a significant movement in the price and with minimum loss of value.

TMR AG aims to keep liquidity risk as low as possible so that the Company will be able to meet its contractual obligations in a timely manner, even under stressed scenarios such as following a major catastrophic event. The Company maintains sufficient liquid assets, or assets that can be converted into cash at short notice and without any significant capital loss, to meet expected cash flow requirements. These liquid assets are regularly monitored using cash flow forecasting to ensure that surplus funds are invested to achieve a higher rate of return. The Company also monitors market changes and outlooks and reallocates assets as deemed necessary.

Liquidity risk can be an outcome or consequence of the Company's exposures to catastrophe risk and market risk. However, for the purpose of monitoring risk limits, liquidity risk is included in and shares the risk limit with the market risk category.

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4. **Risk Disclosures (continued)**

D. Liquidity Risk (continued)

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

	<u>2015</u>	<u>2014</u>
Less than one year	\$ 90,810	\$ 88,060
Between one and two years	302,488	206,976
Between two and three years	238,889	300,874
Between three and four years	159,737	122,990
Between four and five years	118,616	92,107
Over five years	162,680	134,881
Agency residential mortgage-backed	219,470	294,456
Commercial mortgage-backed	57,029	-
Asset-backed securities	75,622	150,060
Collateralised debt obligations	161,348	-
Municipals	92,228	-
Total fixed interest securities	<u>\$ 1,678,917</u>	<u>\$ 1,390,404</u>

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

As at December 31, 2015	Years until liability becomes due				Total
	Less than one	One to three	Three to five	Over five	
Outstanding losses and loss expenses	\$ 259,398	\$ 280,655	\$ 123,654	\$ 193,993	\$ 857,700
Liability for collateral held on behalf of counterparties	63,939	82,483	40,146	47,049	233,617
Reinsurance balances payable	88,948	159	-	-	89,107
Deposit liabilities	59,981	82,483	40,146	113,567	296,177
Fair value of derivative liabilities	3,537	770	-	-	4,307
Accounts payable and accrued expenses	29,584	4,521	1,738	722	36,565
Note payable	-	25,000	-	-	25,000
Total	<u>\$ 505,387</u>	<u>\$ 476,071</u>	<u>\$ 205,684</u>	<u>\$ 355,331</u>	<u>\$ 1,542,473</u>

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4. Risk Disclosures (continued)

D. Liquidity Risk (continued)

As at December 31, 2014	Years until liability becomes due				Total
	Less than one	One to three	Three to five	Over five	
Outstanding losses and loss expenses	\$ 227,319	\$ 217,888	\$ 100,481	\$ 153,617	\$ 699,305
Liability for collateral held on behalf of counterparties	79,850	119,954	65,047	50,399	315,250
Reinsurance balances payable	51,428	1,595	—	—	53,023
Deposit liabilities	74,901	119,954	65,047	77,775	337,677
Fair value of derivative liabilities	2,550	—	—	—	2,550
Accounts payable and accrued expenses	17,362	1,361	525	—	19,248
Note payable	—	25,000	—	—	25,000
Total	\$ 453,410	\$ 485,752	\$ 231,100	\$ 281,791	\$1,452,053

While the estimation of the ultimate liability for outstanding losses and loss expenses is complex and incorporates a significant amount of judgment, the timing of payment of outstanding losses and loss expenses is also uncertain and cannot be predicted as simply as for other financial liabilities. Actuarial and statistical techniques, past experience and management's judgment have been used to determine a likely settlement pattern.

E. Operational Risk

Operational risk refers to the risk of financial or other loss, or potential damage to the Company's reputation resulting from inadequate or failed internal processes, people and systems or from external events.

The following are some of the examples of operational risks facing the Company:

- Legal and compliance risk;
- Information technology risk;
- Loss of key officers or employees;
- System failure and business disruption;
- Execution errors;
- Employment practice liability; and
- Internal and external fraud.

Through the scenario analysis process, TMR AG has also made efforts to identify and assess the financial impact of various operational risks. These risks are managed through internal control and monitoring tools such as the risk register.

TMR AG has a low appetite for operational risk. Unlike underwriting and investment risks, operational risk has no upside and only downside and therefore should be avoided if feasible and cost-effective.

Operational risk is difficult to quantify but can be controlled through appropriate corporate governance and internal control measures. The Company has developed a number of policies and procedures aimed to control or mitigate the negative impact that may potentially result from operational risk events.

TOKIO MILLENNIUM RE AG

Notes to Consolidated Financial Statements

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4. Risk Disclosures (continued)

F. Strategic Risk

Strategic risk is the risk to earnings or capital arising from adverse business decisions or improper implementation of those decisions or inability to act in response to business opportunities or to adapt to changes in its operating environment.

The following are examples of strategic risks facing the Company:

- Industry overcapacity that results in prolonged soft market conditions;
- Flawed response plans to market price cycles, including maintaining premium volume and market share during market declines and improper performance incentives for underwriters and others;
- Planning processes (e.g., plan loss ratio setting, target premium volume) that are not fully integrated with internal financial indicators and external benchmarks or are based on forecasts that are inherently optimistic;
- Expansion into new lines or territories with inadequate underwriting expertise, pricing systems, price monitoring capabilities, understanding of regulatory requirements, claims handling staff; and
- Failure of large information technology and infrastructure projects to achieve the specified goals.

Strategic risks can be split into two components, one being the risk emanating from making business decisions (active) such as the last two risks in the list above, and the other emanating from a lack of response to industry challenges (passive) such as the first three risks in the list above.

Strategic risk is especially important for TMR AG because it has aimed to improve and optimise the risk profile of its business by growing those lines of business which help to diversify its current concentration in catastrophe exposures. Therefore it has strong interest in growing its current book of business profitably and developing new lines of business or markets.

Although there is inherent risk in strategic expansion into new lines and geographical areas, there are also many benefits. In setting TMR AG's appetite for this risk, both the risk and the benefits are taken into consideration.

TMR AG identifies and assesses various strategic risks within its risk register and performs scenario analyses to evaluate the potential financial impact that may arise from such risks.

New business will be evaluated periodically to determine whether or not it has met the strategic goals of the Company.

Capital Model

The Company attempts to identify and appropriately define all material risks internal and external to the Company, understand the manifestations of each risk, and ensure that risks are managed, controlled or mitigated. To the extent that a risk is not fully mitigated, the Company will measure the financial impact of the risk and include it in its capital adequacy assessment and measurement framework. The internal capital model covers all of the material risks identified above, including regulatory obligations.

Each of the material risks is measured and modeled by TMR AG's internal or third-party vendor models. The results are aggregated into a probability distribution of the Company's profit and loss (via Monte Carlo simulation) in order to provide a holistic view of all risks facing the Company. In the risk aggregation process, both risk correlation and diversification effects are taken into account. From the probability distribution, the Company's overall capital requirements using various risk measures and under various capital standards can be determined.

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5. Cash and cash equivalents

Cash and cash equivalents represent cash at bank of \$279.0 million at December 31, 2015 (2014 - \$167.8 million).

6. Funds withheld

Funds withheld at December 31, 2015 totalling \$79.0 million (2014 - \$52.8 million) represents funds furnished by the Company to its cedants and held in trust by trustees. The funds do not trigger any cash flows and cannot be realised by cedants without the Company's consent. In the event of default on such a deposit, the Company's reinsurance commitment would be reduced to the same extent.

7. Investments

Investments comprise of the following:

	<u>2015</u>	<u>2014</u>
Short-term investments	\$ 255,624	\$ 537,526
Fixed interest securities, designated at fair value through profit and loss	-	27,595
Fixed interest securities, available for sale	1,678,917	1,362,809
Investment in catastrophe bonds, available for sale	10,276	40,386
Equity securities, available for sale	35,646	-
Other securities, at fair value through profit and loss	13,314	-
	<u>\$ 1,993,777</u>	<u>\$ 1,968,316</u>

(a) Short-term investments

The Company's short-term investments represent bank deposits and investments in money market funds with an original term of greater than 90 days but less than one year. At December 31, short-term investments comprised of the following:

	<u>2015</u>	<u>2014</u>
Money market funds	\$ 137,524	\$ 422,691
Long-term fixed deposits	118,100	114,835
	<u>\$ 255,624</u>	<u>\$ 537,526</u>

(b) Fixed interest securities, designated at fair value through profit and loss

The Company had fixed interest securities designated at fair value through profit and loss related to Non U.S. government bonds in 2014, which matured in 2015. These bonds had a rating of AA+ as assigned by Standard & Poor's. These securities were measured at fair value with all changes from one accounting period to the next being recorded in the consolidated statement of comprehensive income.

The book value, fair value and unrealised gains and losses on fixed interest securities designated at fair value through profit and loss were as follows:

<u>At December 31, 2014</u>	<u>Amortised cost</u>	<u>Unrealised gains</u>	<u>Unrealised losses</u>	<u>Fair value</u>
Non-U.S. government	\$ 29,809	\$ -	\$ (2,214)	\$ 27,595

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7. Investments (continued)

(c) Fixed interest securities, available for sale

(i) The amortised cost, fair value and unrealised gains and losses of investments in available for sale fixed interest securities are as follows:

At December 31, 2015	Amortised cost	Unrealised gains	Unrealised losses	Fair value
U.S. treasuries	\$ 277,824	\$ 2,681	\$ (357)	\$ 280,148
Non-U.S. government	58,841	433	-	59,274
Corporate	742,075	1,215	(9,492)	733,798
Agency residential				
mortgage-backed	220,927	1,259	(2,716)	219,470
Commercial mortgage-backed	59,629	4	(2,604)	57,029
Asset-backed	76,004	-	(382)	75,622
Collateralised debt obligations	165,737	64	(4,453)	161,348
Municipals	89,986	2,271	(29)	92,228
Total	\$ 1,691,023	\$ 7,927	\$ (20,033)	\$ 1,678,917
At December 31, 2014	Amortised cost	Unrealised gains	Unrealised losses	Fair value
U.S. treasuries	\$ 301,760	\$ 4,296	\$ (399)	\$ 305,657
Corporate	610,663	3,626	(1,653)	612,636
Agency residential				
mortgage-backed	292,743	3,493	(1,780)	294,456
Asset-backed	150,124	308	(372)	150,060
Total	\$ 1,355,290	\$ 11,723	\$ (4,204)	\$ 1,362,809

Of the \$1,678.9 million available for sale fixed interest securities as at December 31, 2015 (2014 - \$1,362.8 million), \$193.9 million (2014 - \$nil) relates to securities held by the Company for the purpose of funding future claim payments in relation to a loss portfolio transfer agreement ("LPTA"). The securities related to the LPTA consist of non-U.S. government securities of \$59.3 million, corporate securities of \$132.9 million and asset-backed securities of \$1.7 million as at December 31, 2015 (2014 - \$nil). The net unrealised gain on the LPTA securities of \$0.4 million at the end of the year 2015 (2014 - \$nil) has been offset against the corresponding liability for collateral held on behalf of counterparties. The LPTA is referred to in Note 12 – Deposit Contracts.

In the normal course of business, available for sale fixed interest securities and cash and cash equivalents with fair value of \$177.1 million as at December 31, 2015 (2014 - \$301.9 million), were deposited in trust for the benefit of ceding companies and credit institutions.

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(Expressed in thousands of United States Dollars)

7. Investments (continued)

(c) Fixed interest securities, available for sale (continued)

(ii) The amortised cost and estimated fair value of available for sale fixed interest securities as of December 31, 2015, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to repay obligations with or without prepayment penalties.

	Amortised cost	Fair value
Within one year	\$ 90,628	\$ 90,810
From one to five years	822,587	819,730
From five to ten years	<u>165,525</u>	<u>162,680</u>
Subtotal	1,078,740	1,073,220
Agency residential mortgage-backed	220,927	219,470
Commercial mortgage-backed	59,629	57,029
Asset-backed	76,004	75,622
Collateralised debt obligations	165,737	161,348
Municipals	<u>89,986</u>	<u>92,228</u>
Total	<u>\$ 1,691,023</u>	<u>\$ 1,678,917</u>

(iii) The Company's available for sale fixed interest securities carry a weighted average credit rating of AA- as assigned by Standard & Poor's (S&P).

The rating profile of the Company's available for sale fixed interest securities, based on S&P or equivalent rating, is shown in the table below.

	<u>2015</u>	<u>2014</u>
AAA	\$ 150,904	\$ 177,524
AA+,AA,AA-	644,927	676,118
A+,A,A-	415,744	287,954
BBB+,BBB,BBB-	391,434	221,213
Below investment grade	23,341	-
Not rated	<u>52,567</u>	<u>-</u>
	<u>\$ 1,678,917</u>	<u>\$ 1,362,809</u>

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7. Investments (continued)

(d) Investments in catastrophe bonds, available for sale

The Company's investments in catastrophe bonds comprise of three bonds. All catastrophe bonds, with the exception of one, are rated by internationally recognised rating agencies. For those which are rated they have an equivalent Standard and Poor's credit rating of BB+ to BB-. These bonds mature in 2016 and 2017. The issuers of these securities have used the proceeds raised to collateralise certain catastrophe reinsurance obligations, mainly North American and European wind and earthquake risks. The investment in these securities is therefore at risk of loss, in whole or in part, if a covered catastrophe occurs.

The cost, fair value and unrealised gains and losses of investments in catastrophe bonds were as follows:

<u>At December 31, 2015</u>	<u>Cost</u>	<u>Unrealised gains</u>	<u>Unrealised losses</u>	<u>Fair value</u>
Catastrophe bonds	\$ 10,280	\$ 19	\$ (23)	\$ 10,276
<u>At December 31, 2014</u>	<u>Cost</u>	<u>Unrealised gains</u>	<u>Unrealised losses</u>	<u>Fair value</u>
Catastrophe bonds	\$ 40,078	\$ 312	\$ (4)	\$ 40,386

Unrealised losses on catastrophe bonds held in 2015 and 2014 comprise an accumulation of unrealised losses on a security by security basis caused by general market movements rather than credit events. As of December 31, 2015 and 2014, the Company had no unrealised losses caused by other factors or circumstances, including issuer specific credit risks or due to exposures to catastrophe events.

(e) Equity securities, available for sale

The acquisition cost, fair value and unrealised gains and losses of investments in available for sale equity securities are as follows:

<u>At December 31, 2015</u>	<u>Acquisition cost</u>	<u>Unrealised gains</u>	<u>Unrealised losses</u>	<u>Fair value</u>
Common stock	\$ 18,789	\$ 328	\$ (1,302)	\$ 17,815
Mutual funds	10,000	-	(734)	9,266
Real estate investment trusts	10,063	-	(1,498)	8,565
Total	\$ 38,852	\$ 328	\$ (3,534)	\$ 35,646

There were no investments in equity securities at December 31, 2014.

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7. **Investments (continued)**

(f) Other securities, at fair value through profit and loss

The acquisition cost, fair value and unrealised gains and losses of investments in other securities at fair value through profit and loss are as follows:

At December 31, 2015	Acquisition cost	Unrealised gains	Unrealised losses	Fair value
Investments in:				
Limited partnerships	\$ 12,231	\$ 49	\$ (216)	\$ 12,064
Limited liability companies	<u>1,250</u>	<u>—</u>	<u>—</u>	<u>1,250</u>
Total	<u>\$ 13,481</u>	<u>\$ 49</u>	<u>\$ (216)</u>	<u>\$ 13,314</u>

There were no investments in other securities at December 31, 2014.

(g) Components of investment income

The components of net investment income for the years ended December 31, 2015 and 2014 were as follows:

December 31, 2015	Interest and dividends	Net realised gains (losses)	Net change in unrealised gains/losses	Impairment losses	Net investment income
Cash and cash equivalents	\$ 1,086	\$ —	\$ —	\$ —	\$ 1,086
Funds withheld	2,143	—	—	—	2,143
Short-term investments	3,580	—	—	—	3,580
Fixed interest securities – FVTPL	172	—	84	—	256
Fixed interest securities – AFS	29,011	3,171	—	(209)	31,973
Catastrophe bonds	3	—	—	—	3
Equity securities – AFS	1,471	—	—	(2,289)	(818)
Other securities – FVTPL	<u>—</u>	<u>(307)</u>	<u>(167)</u>	<u>—</u>	<u>(474)</u>
Sub-total	\$ 37,466	\$ 2,864	\$ (83)	\$ (2,498)	\$ 37,749
Investment management fees					<u>(2,439)</u>
Net investment income					<u>\$ 35,310</u>

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Notes to Consolidated Financial Statements

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(Expressed in thousands of United States Dollars)

7. Investments (continued)

(h) Components of investment income (continued)

December 31, 2014	Interest and dividends	Net realised gains	Net change in unrealised gains/losses	Impairment losses	Net investment income
Cash and cash equivalents	\$ 1,015	\$ -	\$ -	\$ -	\$ 1,015
Funds withheld	2,846	-	-	-	2,846
Short-term investments	4,129	-	-	-	4,129
Fixed interest securities – FVTPL	1,749	-	-	-	1,749
Fixed interest securities – AFS	25,399	3,309	(800)	-	27,908
Catastrophe bonds	<u>19</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>19</u>
Sub-total	\$ 35,157	\$ 3,309	\$ (800)	\$ -	\$ 37,666
Investment management fees					<u>(1,246)</u>
Net investment income					<u>\$ 36,420</u>

8. Fair value measurements

Fair values measurements are established in accordance with the framework provided by IFRS 13, *Financial Instruments: Disclosures*. IFRS 13 establishes a fair value hierarchy with the highest priority given to quoted prices in active markets and the lowest priority given to unobservable inputs.

The following are the levels within the fair value hierarchy.

- Level 1 - Valuations based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these instruments does not entail a significant degree of judgment.
- Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals, broker quotes and certain pricing indices.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement. These measurements include circumstances where there is little, if any, market activity for the asset or liability. In these cases, significant management assumptions can be used to establish management's best estimate of the assumptions used by other market participants in determining the fair value of the asset or liability.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement of the asset or liability. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and the Company considers factors specific to the asset or liability.

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8. Fair value measurements (continued)

Below is a summary of the assets and liabilities that are measured at fair value on a recurring basis:

<u>At December 31, 2015</u>	<u>Total</u>	<u>Quoted prices in active markets for identical assets (Level 1)</u>	<u>Other observable inputs (Level 2)</u>	<u>Unobservable inputs (Level 3)</u>
<u>Financial assets</u>				
<u>Investments</u>				
Short-term investments	\$ 255,624	\$ 255,624	\$ —	\$ —
Fixed interest securities				
U.S. treasuries	280,148	280,148	—	—
Non-U.S. government	59,274	59,274	—	—
Corporate	733,798	—	698,795	35,003
Agency residential mortgage-backed	219,470	—	219,470	—
Commercial mortgage backed	57,029	—	46,198	10,831
Asset-backed	75,622	—	75,622	—
Collateralised debt obligations	161,348	—	123,503	37,845
Municipals	92,228	—	92,228	—
Investments in catastrophe				
bonds	10,276	—	10,276	—
Equity securities	35,646	26,380	—	9,266
Other securities	<u>13,314</u>	<u>—</u>	<u>—</u>	<u>13,314</u>
Sub-total	1,993,777	621,426	1,266,092	106,259
Derivative assets	<u>4,773</u>	<u>—</u>	<u>—</u>	<u>4,773</u>
Total	1,998,550	621,426	1,266,092	111,032
<u>Financial liabilities</u>				
Derivative liabilities	<u>(4,307)</u>	<u>—</u>	<u>—</u>	<u>(4,307)</u>
Total	<u>\$ 1,994,243</u>	<u>\$ 621,426</u>	<u>\$ 1,266,092</u>	<u>\$ 106,725</u>

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8. Fair value measurements (continued)

<u>At December 31, 2014</u>	<u>Total</u>	Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Unobservable inputs (Level 3)
<u>Financial assets</u>				
<i>Investments</i>				
Short-term investments	\$ 537,526	\$ 537,526	\$ —	\$ —
<i>Fixed interest securities</i>				
U.S. treasuries	305,657	305,657	—	—
Non-U.S. government	27,595	—	27,595	—
Corporate	612,636	—	612,636	—
Agency residential mortgage-backed	294,456	—	294,456	—
Asset-backed	150,060	—	150,060	—
Investments in catastrophe				
bonds	<u>40,386</u>	<u>—</u>	<u>40,386</u>	<u>—</u>
Sub-total	1,968,316	843,183	1,125,133	—
Derivative assets	<u>1,806</u>	<u>—</u>	<u>—</u>	<u>1,806</u>
Total	1,970,122	843,183	1,125,133	1,806
<u>Financial liabilities</u>				
Derivative liabilities	<u>(2,550)</u>	<u>—</u>	<u>—</u>	<u>(2,550)</u>
Total	<u>\$ 1,967,572</u>	<u>\$ 843,183</u>	<u>\$ 1,125,133</u>	<u>\$ (744)</u>

There were no transfers made between Levels 1, 2 and 3 of the fair value hierarchy in 2015 and 2014.

Short-term investments

Short-term investments, which comprise securities due to mature within one year of the date of purchase, that are traded in active markets are classified within Level 1 as fair values are based on quoted market prices.

Fixed interest securities

The Company's fixed interest securities are priced using pricing services, such as index providers and pricing vendors. The pricing vendors provide pricing for a high volume of liquid securities that are actively traded. For securities that do not trade on an exchange, the pricing services generally utilize market data and other observable inputs in pricing models to determine prices. Prices are generally verified using third party data. The techniques generally used to determine the fair value of our fixed interest securities are detailed below by asset class.

U.S. treasuries

These securities are primarily priced by pricing vendors. When pricing these securities, the vendor may utilize daily data from many real time market sources, including active trades, as such, the Company considers its U.S. treasury fixed interest securities as Level 1.

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8. Fair value measurements (continued)

Non-U.S. government

Fixed interest securities included in non-U.S. government are primarily priced by pricing vendors. When evaluating these securities, the vendor may gather information from market sources and integrate other observations from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trades, when available. For securities in which trade volume is relatively high, the vendor may utilise data from active trades, as such, these are included as Level 1. For securities in which trade volume is low, the pricing vendor may also utilise data from more frequently traded securities with similar attributes. These are considered observable inputs therefore, the fair value of such securities are classified as Level 2.

Corporate

Corporate securities primarily include fixed rate corporate bonds and floating rate notes. The Company's corporate fixed interest securities are primarily priced by pricing vendors. When evaluating these securities, the vendor may gather information from market sources regarding the issuer of the security, obtain credit data, as well as other observations from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trades, when available. The pricing vendor may also consider the specific terms and conditions of the securities, including any specific features which may influence risk. These are considered observable inputs therefore, the fair value of such securities are classified as Level 2.

The Company's corporate securities also include private placements, for which there is limited observable input on which to measure fair value, are classified as Level 3. The fair value of these private placements is estimated to be equal to its amortised cost.

Residential ("RMBS") and commercial mortgage-backed ("CMBS") securities

The vendor uses various valuation techniques and pricing models to measure the fair value of its investments in RMBS and CMBS, including option-adjusted spread models, volatility-driven multi-dimensional single cash flow stream models and matrix correlation to comparable securities. RMBS include U.S. agency securities and collateralised mortgage obligations. Inputs utilised in connection with the valuation techniques include monthly payment and performance information, including prepayments, default severity, delinquencies, market indices and the amounts of the tranches in the particular structure which are senior or subordinate, as applicable, to the tranche represented by the Company's investment. Valuations may also be corroborated by daily active market quotes. As of December 31, 2015, 96% of the Company's investment in mortgage-backed securities are valued using observable inputs and therefore are categorised as Level 2 of the fair value hierarchy. The remaining mortgage-backed securities are valued using non-binding broker quotes which rely on unobservable inputs and thus these securities are categorised in Level 3 of the fair value hierarchy.

Asset-backed

The underlying collateral for the Company's asset-backed fixed interest securities primarily consists of automobile and credit card loans. Securities held in this sector are primarily priced by pricing vendors and are considered as Level 2 by the Company as inputs are observable. The pricing vendor may apply dealer quotes and other available trade information such as bid and offers, prepayment spreads which may be adjusted for the underlying collateral or current price data, the U.S. treasury curve, swap curve and TBA values as well as cash settlement.

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8. Fair value measurements (continued)

Collateralised debt obligations

Collateralised debt obligations consist of collateralised loans. The pricing vendor's valuation techniques utilise non-binding broker quotes as the key input for a majority of the portfolio. As such inputs are generally unobservable, these collateralised debt obligations are categorised as Level 3 of the fair value hierarchy. For the remaining securities, valuation is determined utilising observable inputs including monthly payment information, prepayment data, default severity and delinquencies. These securities are categorised as Level 2 of the fair value hierarchy.

Municipals

These include bonds or notes issued by U.S. municipalities. Inputs utilised include recently executed transactions and other market data, spreads, benchmark curves including treasury and other benchmarks, trustee reports, material event notices, new issue data, and issuer financial statements. These inputs are generally observable and as such, these securities are categorised as Level 2 of the fair value hierarchy.

Investments in catastrophe bonds

The Company's investments in catastrophe bonds are recorded at fair value based on quoted market prices, or when such prices are not available, by reference to published broker or underwriter bid and offer indications. As such, the Company considers its investments in catastrophe bonds as Level 2.

Equity securities

This is comprised of common stock, mutual funds and real estate investment trusts. Equities are generally included as Level 1 in the fair value hierarchy as prices are obtained from market exchanges in active markets. Investments in mutual funds, where the fair value of the fund is estimated to be the net asset value reported by the fund administrator at the balance sheet date, are classified as Level 3.

Other securities

Other securities consist of investments in investment funds organised as limited partnerships, investment in funds organised as limited liability companies, real estate investments held by limited liability companies and trading account securities.

For private equity investments, since quoted market prices are not available, the transaction price is used as the best estimate of fair value at inception. When evidence is believed to support a change to the carrying value from the transaction price, adjustments are made to reflect expected exit values. Ongoing valuation reviews are based on assessments of each underlying investment and the inputs utilised in these reviews include, among other things, the evaluation of financing and sale transactions with third parties, expected cashflows, material events and market-based information. These investments are included in Level 3 of the fair value hierarchy.

For investments in funds organised as limited liability companies, the funds' financial statements constitute the key valuation input. The value calculated using the equity method of accounting with respect to the investment in this limited liability company was reflective of the fair market value of such investment, and therefore such investments are categorised as Level 3 of the fair value hierarchy.

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8. Fair value measurements (continued)

Fair value of derivative assets and liabilities

Included in Level 3 are the Company's catastrophe swap derivatives. Catastrophe swap derivatives are stated at fair value as estimated by management primarily based on the unexpired period of risk, an evaluation of the probability of loss and other unobservable inputs. The Company's catastrophe swap derivatives are initially priced at fair value in a non-stressed market and amortisation reflects the change in fair value in the absence of any loss events. The fair value of derivative contracts is sensitive to loss triggering events. In the event of a loss, the Company would adjust the fair value of the derivative to account for a recovery or liability in accordance with the contract terms and the estimate of exposure under the contract. The inputs for catastrophe swap derivatives are based on management's evaluation and are unobservable.

The following tables provide reconciliations for Level 3 assets measured at fair value on a recurring basis for the years ended December 31, 2015 and 2014.

At December 31, 2015	2014	Net gains (losses) included in earnings	Net gains (losses) included in other comprehensive income	Purchases	Sales	2015
<u>Financial assets</u>						
Corporate	\$ -	\$ 50	\$ -	\$ 34,953	\$ -	\$ 35,003
Commercial mortgage backed	-	65	(137)	10,903	-	10,831
Collateralised debt obligations	-	40	4	37,801	-	37,845
Equity securities	-	-	(734)	10,000	-	9,266
Other securities	-	(231)	-	13,545	-	13,314
Derivative assets	1,806	(13,446)	-	16,413	-	4,773
Sub-total	1,806	(13,522)	(867)	123,615	-	111,032
<u>Financial liabilities</u>						
Derivative liabilities	(2,550)	22,201	-	-	(23,958)	(4,307)
Total	\$ (744)	\$ 8,679	\$ (867)	\$ 123,615	\$ (23,958)	\$ 106,725

At December 31, 2014	2013	Net gains (losses) included in earnings	Net gains (losses) included in other comprehensive income	Purchases	Sales	2014
<u>Financial assets</u>						
Derivative assets	\$ 14,039	\$ (20,309)	\$ -	\$ 8,076	\$ -	\$ 1,806
<u>Financial liabilities</u>						
Derivative liabilities	(10,665)	32,723	-	-	(24,608)	(2,550)
Total	\$ 3,374	\$ 12,414	\$ -	\$ 8,076	\$ (24,608)	\$ (744)

Net gains (losses) on investments and on derivative assets and liabilities are included in net investment income and net derivative income, respectively, in the consolidated statement of comprehensive income.

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8. Fair value measurements (continued)

Investments included in Level 3

As at December 31, 2015, investments included in Level 3 amounted to \$106.3 million (2014 - \$nil).

If models are used to measure financial assets and liabilities included in level 3 under which the adoption of alternative inputs lead to a material change in fair value, IFRS 13 requires disclosure of the effects of these alternative assumptions.

Equity securities and other securities classified as Level 3 are mainly priced based on the (adjusted) net asset value method. The key unobservable input is net asset value which is provided by the respective fund manager. Since the Company has limited insight into the specific inputs used by the fund managers in estimating fair value, the effects of using alternative inputs within the meaning of IFRS 13 cannot be reasonably established.

Mortgage loans and private placements are valued at amortised cost, which reasonably approximate fair value for these securities as those securities were just purchased before the year end. The key unobservable input for fair value measurement would be a risk adjusted interest rate benchmark (market interest rate for the same tenor and the respective credit risk). The application of alternative inputs and assumptions has no material effect on the consolidated financial statements.

Commercial mortgage backed securities and collateralised debt obligations classified as Level 3 are mainly priced based on the income approach by brokers and traders. The primary unobservable input used in the discounted cash flow method is a risk adjusted interest rate benchmark. A significant yield increase of this benchmark in isolation could result in a decreased fair value, while a significant yield decrease could result in an increased fair value. However, a simplified 10% stress of this main non-market observable input has no material impact to the fair value at December 31, 2015.

Derivative assets and liabilities included in Level 3

As at December 31, 2015, derivative assets comprise unearned derivative expense of \$4.8 million (2014 - \$1.8 million).

As at December 31, 2015, derivative liabilities comprise unearned derivative income of \$4.3 million (2014 - \$2.5 million).

The following methods and assumptions are used by the Company in estimating fair value disclosures for other financial instruments:

Cash and cash equivalents, Short-term investments and Liability for collateral held on behalf of counterparties

The carrying amounts reported in the consolidated balance sheet for these instruments approximate their fair values.

Other assets and liabilities

The fair value of funds withheld, accrued interest receivable, premiums receivable, deposit assets, other assets, reinsurance balances payable, deposit liabilities, accounts payable, note payable and accrued expenses approximates their carrying value due to their short-term nature. The estimates of fair values are subjective in nature and are not necessarily indicative of the amounts that the Company would actually realise in a current market exchange. However, any differences would not be expected to be material. Certain instruments such as prepaid reinsurance premiums, outstanding losses recoverable from reinsurers, deferred acquisition expenses, unearned profit commission, property and equipment, intangible assets, other assets, outstanding losses and loss expenses, unearned premiums, deferred commission income and deferred fee income are excluded from fair value disclosure.

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8. Fair value measurements (continued)

Other assets and liabilities (continued)

Thus, the total fair value amounts cannot be aggregated to determine the underlying economic value of the Company.

9. Net derivative income

Net derivative income consists of catastrophe swap derivative premiums earned of \$8.8 million (2014 - \$16.5 million) offset by payments made under the Company's catastrophe swap derivatives of \$0.1 million (2014 - \$2.2 million net recovery).

As discussed in Note 4 under 'Credit Risk', the Company's maximum exposure to unrated counterparties is fully collateralised.

10. Collateral held on behalf of counterparties

Collateral received in the form of cash, which is not legally segregated from the Company, is recognised as an asset in the consolidated balance sheet with a corresponding liability for the repayment. In addition, amounts arising from the application of the deposit method of accounting to ceded retrocession or reinsurance contracts are included.

11. Reinsurance and other assets

	<u>2015</u>	<u>2014</u>
Premiums receivable	\$ 716,399	\$ 474,583
Deposit assets	296,177	337,677
Accrued interest receivable	12,035	7,599
Outstanding losses recoverable from reinsurers	52,730	51,473
Other assets	21,857	26,034
	<u>\$ 1,099,198</u>	<u>\$ 897,366</u>

The current and non-current portions are expected to be as follows:

	<u>2015</u>	<u>2014</u>
Current portion	\$ 700,221	\$ 518,296
Non-current portion	398,977	379,070
	<u>\$ 1,099,198</u>	<u>\$ 897,366</u>

The Company assesses its reinsurance receivables for impairment on a quarterly basis by reviewing counterparty payment history. The carrying amounts disclosed above reasonably approximate the fair value at the reporting date.

12. Deposit contracts

Effective July 1, 2014, Tokio Millennium Re AG – Bermuda branch ("TMRB") entered into a loss portfolio transfer agreement ("LPTA"). TMRB accepted, on a fully collateralised basis, the liability of a loss portfolio with an aggregate limit capped at Euro 366 million. Through a quota share retrocession agreement, TMRB retroceded 100% of its liability to another party. TMRB is compensated through a ceding commission as a percentage of the initial aggregate limit, which is earned from the LPTA effective date to expected contract termination date.

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13. Deferred acquisition expenses and deferred commission income

The reconciliation of opening and closing deferred acquisition costs incurred and ceded is as follows:

	<u>2015</u>				<u>2014</u>			
	<u>Gross</u>	<u>Ceded</u>	<u>Other</u>	<u>Net</u>	<u>Gross</u>	<u>Ceded</u>	<u>Other</u>	<u>Net</u>
At January 1	\$ 201,528	\$ (2,840)	\$ (702)	\$ 197,986	\$ 135,916	\$ (1,838)	\$ (188)	\$ 133,890
Expense deferred	403,393	(22,234)	(927)	380,232	304,198	(15,330)	(1,017)	287,851
Amortisation	(273,487)	21,511	430	(251,546)	(235,780)	14,350	503	(220,927)
Other	(3,496)	52	-	(3,444)	(2,806)	(22)	-	(2,828)
At December 31	<u>\$ 327,938</u>	<u>\$ (3,511)</u>	<u>\$ (1,199)</u>	<u>\$ 323,228</u>	<u>\$ 201,528</u>	<u>\$ (2,840)</u>	<u>\$ (702)</u>	<u>\$ 197,986</u>

The current and non-current portions are expected to be as follows:

	<u>2015</u>	<u>2014</u>
Current portion	\$ 214,364	\$ 145,122
Non-current portion	<u>108,864</u>	<u>52,864</u>
	<u>\$ 323,228</u>	<u>\$ 197,986</u>

14. Taxation

The Swiss operation is subject to Swiss cantonal and federal taxes of 21.15% (2014: 21.15%). The Company has branches that operate in Australia, United States and United Kingdom which are subject to income taxes at statutory rates of 30%, 35% and 21.5% respectively.

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

Income tax

The Swiss standard rate of tax is 21.15% (2014: 21.15%), whereas the tax charges for the year ended December 31, 2015 as a percentage of profit before tax is 1.14% (2014: 4.35%). The reasons for this difference are explained below:

	<u>2015</u>	<u>2014</u>
Profit before income tax	\$ 109,050	\$ 74,514
Tax calculated at the standard corporation tax rate applicable in Switzerland: 21.15% (2014: 21.15%)	23,064	15,759
Non-taxable income	(22,731)	(22,316)
Tax rate differences on foreign branches	784	954
Deferred tax adjustment in respect of prior years	(1,644)	1,589
Tax rate adjustment	-	5,623
Tax losses for which no deferred tax asset is recognised	1,013	1,644
Other	752	(9)
Actual expense for income tax	<u>\$ 1,238</u>	<u>\$ 3,244</u>

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14. Taxation (continued)

The following table presents the major components of the income tax expense:

	<u>2015</u>		<u>2014</u>
Corporation tax charge for the year	\$ (2)	\$	3,410
Deferred tax charge (credit) for the year	1,234		(1,755)
Adjustments in respect of prior year deferred tax	6		1,589
Total tax charge	<u>\$ 1,238</u>	\$	<u>3,244</u>

Deferred tax

	<u>2015</u>		<u>2014</u>
Deferred tax asset	\$ 3,021	\$	3,930
Deferred tax liability	(706)		(948)
Total net deferred tax asset	<u>\$ 2,315</u>	\$	<u>2,982</u>

The Company's deferred tax asset results from an operating loss carry forward and IFRS versus tax basis accounting differences. The deferred tax asset of \$3.0 million as at December 31, 2015 (2014: \$3.9 million) has been recognised as the Company expects the business to produce taxable profits in future periods against which the tax losses can be offset. A deferred tax asset of \$1.6 million was written down to nil in 2014 for tax benefits which management determined will not be realised against future taxable profits.

In accordance with IAS 12, to avoid the need for detailed scheduling of the timing of the reversal of each temporary difference, TMR AG has offset its deferred tax asset against its deferred tax liability, as they relate to the same taxable entities and relate to income taxes levied by the same taxation authorities.

Net deferred tax assets analysed by balance sheet headings and after appropriate netting are as follows:

	<u>2014</u>	<u>Income statement</u>	<u>Transfer from equity</u>	<u>Foreign currency translation</u>	<u>2015</u>
As at December 31		(charge)/credit			
Outstanding losses and loss expenses \$	195	\$ 2,400	\$ -	\$ (25)	\$ 2,570
Unearned premiums	-	31,055	-	-	31,055
Deferred acquisition expenses	491	267	-	(61)	697
Accounts payable and accrued expenses	119	1,417	-	(14)	1,522
Operating losses	7,528	21,811	-	(91)	29,248
Retirement benefit obligation	86	6	-	-	92
Other	103	989	-	(6)	1,086
Total deferred tax assets	<u>\$ 8,522</u>	<u>\$ 57,945</u>	<u>\$ -</u>	<u>(197)</u>	<u>\$ 66,270</u>
Investment assets	\$ (950)	\$ (30)	\$ 717	\$ -	\$ (263)
Premiums receivable	(735)	391	-	(8)	(352)
Outstanding losses and loss expense	(3,855)	(682)	-	61	(4,476)
Deferred acquisition expenses	-	(58,864)	-	-	(58,864)
Total deferred tax liabilities	<u>\$ (5,540)</u>	<u>\$ (59,185)</u>	<u>\$ 717</u>	<u>\$ 53</u>	<u>\$ (63,955)</u>
Net deferred tax assets	<u>\$ 2,982</u>	<u>\$ (1,240)</u>	<u>\$ 717</u>	<u>\$ (144)</u>	<u>\$ 2,315</u>

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15. Property and equipment

Property and equipment at December 31, 2015 comprise:

	Computer equipment	Fixtures and fittings	Leasehold improvements	Motor vehicles	Office equipment	Total
<u>Cost</u>						
At January 1, 2015	\$ 9,546	\$ 3,364	\$ 14,203	\$ 127	\$ 20	\$ 27,260
Additions	700	208	1,783	—	—	2,691
Disposals	—	—	(2,778)	—	—	(2,778)
At December 31, 2015	\$ 10,246	\$ 3,572	\$ 13,208	\$ 127	\$ 20	\$ 27,173
<u>Accumulated depreciation</u>						
At January 1, 2015	\$ 6,947	\$ 1,854	\$ 4,580	\$ 93	\$ 17	\$ 13,491
Charge for the year	1,407	409	2,171	10	—	3,997
Disposals	—	—	(2,155)	—	—	(2,155)
At December 31, 2015	\$ 8,354	\$ 2,263	\$ 4,596	\$ 103	\$ 17	\$ 15,333
<u>Net book value</u>						
At December 31, 2015	\$ 1,892	\$ 1,309	\$ 8,612	\$ 24	\$ 3	\$ 11,840
At January 1, 2015	\$ 2,599	\$ 1,510	\$ 9,623	\$ 34	\$ 3	\$ 13,769

Property and equipment at December 31, 2014 comprise:

	Computer equipment	Fixtures and fittings	Leasehold improvements	Motor vehicles	Office equipment	Total
<u>Cost</u>						
At January 1, 2014	\$ 8,271	\$ 2,753	\$ 11,521	\$ 129	\$ 20	\$ 22,694
Additions	1,286	611	2,682	27	—	4,606
Disposals	(11)	—	—	(29)	—	(40)
At December 31, 2014	\$ 9,546	\$ 3,364	\$ 14,203	\$ 127	\$ 20	\$ 27,260
<u>Accumulated depreciation</u>						
At January 1, 2014	\$ 5,481	\$ 1,508	\$ 2,881	\$ 101	\$ 16	\$ 9,987
Charge for the year	1,477	346	1,699	13	1	3,536
Disposals	(11)	—	—	(21)	—	(32)
At December 31, 2014	\$ 6,947	\$ 1,854	\$ 4,580	\$ 93	\$ 17	\$ 13,491
<u>Net book value</u>						
At December 31, 2014	\$ 2,599	\$ 1,510	\$ 9,623	\$ 34	\$ 3	\$ 13,769
At January 1, 2014	\$ 2,790	\$ 1,245	\$ 8,640	\$ 28	\$ 4	\$ 12,707

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16. Intangible assets

Intangible assets at December 31, 2015 comprise:

	<u>Computer software</u>
<u>Cost</u>	
At January 1, 2015	\$ 28,660
Additions	5,298
Disposals	—
At December 31, 2015	<u>\$ 33,958</u>
<u>Accumulated amortisation</u>	
At January 1, 2015	\$ 21,470
Charge for the year	4,059
Disposals	—
At December 31, 2015	<u>\$ 25,529</u>
<u>Net book value</u>	
At December 31, 2015	<u>\$ 8,429</u>
At January 1, 2015	<u>\$ 7,190</u>
	<u>Computer software</u>
<u>Cost</u>	
At January 1, 2014	\$ 23,002
Additions	5,658
Disposals	—
At December 31, 2014	<u>\$ 28,660</u>
<u>Accumulated amortisation</u>	
At January 1, 2014	\$ 17,735
Charge for the year	3,735
Disposals	—
At December 31, 2014	<u>\$ 21,470</u>
<u>Net book value</u>	
At December 31, 2014	<u>\$ 7,190</u>
At January 1, 2014	<u>\$ 5,267</u>

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17. Insurance liabilities

(a) Outstanding losses and loss expenses and losses recoverable from reinsurers

The summary of changes in outstanding losses and loss expenses is as follows:

	Outstanding losses and loss expenses	Outstanding losses recoverable from reinsurers	Net
As at December 31, 2013	\$ 583,691	\$ (30,669)	\$ 553,022
Incurred losses related to:			
Current year	431,405	(1,022)	430,383
Prior years	36,265	(3,217)	33,048
Adverse development cover	–	(43,875)	(43,875)
Loss assumed by novation	73	–	73
Net effect of foreign currency exchange rate changes	(15,892)	91	(15,801)
Total incurred	451,851	(48,023)	403,828
Paid losses related to:			
Current year	112,598	(600)	111,998
Prior years	223,639	(26,619)	197,020
Total paid	336,237	(27,219)	309,018
As at December 31, 2014	\$ 699,305	\$ (51,473)	\$ 647,832
Incurred losses related to:			
Current year	523,014	(6,981)	516,033
Prior years	(13,500)	4,897	(8,603)
Adverse development cover	–	1,632	1,632
Loss portfolio transfer	36,393	–	36,393
Net effect of foreign currency exchange rate changes	(26,091)	838	(25,253)
Total incurred	519,816	386	520,202
Paid losses related to:			
Current year	147,670	(1,063)	146,607
Prior years	213,751	2,706	216,457
Total paid	361,421	1,643	363,064
As at December 31, 2015	\$ 857,700	\$ (52,730)	\$ 804,970

The current and non-current portions of the outstanding losses and loss expenses are expected to be as follows:

	Outstanding losses and loss expenses	Outstanding losses recoverable from reinsurers	Net
2015			
Current	\$ 259,398	\$ (30,485)	\$ 228,913
Non-current	598,302	(22,245)	576,057
	\$ 857,700	\$ (52,730)	\$ 804,970
2014			
Current	\$ 227,319	\$ (7,141)	\$ 220,178
Non-current	471,986	(44,332)	427,654
	\$ 699,305	\$ (51,473)	\$ 647,832

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17. Insurance liabilities (continued)

(a) Outstanding losses and loss expenses and losses recoverable from reinsurers (continued)

During 2015, the Company incurred net losses of \$507.4 million (2014 - \$463.4 million), which mostly relate to attritional losses on proportional and non-catastrophe excess of loss property and casualty contracts, as well as loss development from prior years. Furthermore, \$8.5 million was related to the New South Wales East Coast Low event in April 2015 and another \$2.1 million on windstorm events which impacted Texas in 2015.

The Company experienced net favourable development of \$8.6 million (2014 – adverse development of \$33.0 million) attributable to prior years. Of this total, \$2.3m and \$1.0m development relate to Hurricane Ike and an aggregate treaty loss following receipt of updated loss information from cedants. A \$16.6 million adverse development on a 2012 quota share deal was also recorded in 2015, which had offset other favourable loss developments in the year.

During 2014, the Company incurred net losses of \$463.4 million, of which \$38.4 million related to the adverse development on the 2010 and 2011 New Zealand earthquake, \$10.6 million related to the June 2014 European hailstorm and \$12.3 million related to two 2014 aggregate treaty losses.

The remaining net losses in 2014 mostly related to expected losses on proportional and non-catastrophe property and casualty contracts, as well as loss development from prior years.

For certain catastrophic events, there is considerable uncertainty underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Reserves are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments could require a material change in the amount estimated. The uncertainty surrounding reserves for property catastrophe exposures arises from problems such as policy coverage issues, multiple events affecting one geographic area and the impact on claims adjusting by ceding companies. These issues can cause significant delays to the timing of notification of changes to loss estimates reported by ceding companies. In particular, the estimates for the New Zealand earthquakes have been based on a review of contracts affected by the events, information received from both clients and brokers, industry insured loss estimates, output from both industry and proprietary models and management judgment. It has also been assumed that underlying policy terms and conditions are upheld during the loss adjustment process. There remains the potential for legal and regulatory issues arising regarding the scope of coverage. Consequently, the ultimate net impact of losses from these events on the Company's net income might differ substantially from the foregoing estimate. Such adjustments, if necessary, are reflected in results of operations in the period in which they become known.

(b) Unearned premiums

The current and non-current portions of the unearned premiums are expected to be as follows:

	<u>2015</u>	<u>2014</u>
Current portion	\$ 714,157	\$ 501,569
Non-current portion	369,190	187,258
	<u>\$ 1,083,347</u>	<u>\$ 688,827</u>

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18. Reinsurance and other liabilities

	<u>2015</u>	<u>2014</u>
Outstanding losses and loss expenses	\$ 857,700	\$ 699,305
Liability for collateral held on behalf of counterparties	233,617	315,250
Reinsurance balances payable	89,107	53,023
Deposit liabilities	296,177	337,677
Fair value of derivative liabilities	4,307	2,550
Accounts payable and accrued expenses	36,565	19,248
Note payable	25,000	25,000
	<u>\$ 1,542,473</u>	<u>\$ 1,452,053</u>

The current and non-current portions are expected to be as follows:

	<u>2015</u>	<u>2014</u>
Current portion	\$ 505,386	\$ 453,410
Non-current portion	1,037,087	998,643
	<u>\$ 1,542,473</u>	<u>\$ 1,452,053</u>

19. Note payable

The company issued a private catastrophe bond ("Omamori") using a segregated account of Shima Re which provides TMR AG with a source of fully-collateralised second event retrocessional reinsurance protection against United States earthquakes and named storms. The Omamori catastrophe bond is a three-year deal which inceptioned on January 17, 2014. The transaction was facilitated by TSM as insurance manager of Shima Re. In accordance with IFRS 10, *Consolidated Financial Statements*, as TMR AG has control over the Omamori segregated account, it has been consolidated with the Company's financial statements. As a result of this transaction, a note payable of \$25.0 million as at December 31, 2015 (2014: \$25.0 million) has been recorded in the consolidated balance sheet. It pays a 5% annual coupon rate to noteholders and as such, related interest expense and payable are recorded in the consolidated financial statements.

20. Retirement benefit obligation

(a) Defined benefit scheme

The Company's Switzerland operation offers a defined benefit pension plan to its employees. The plan offers mandatory benefits as prescribed by the Law on Occupational Benefits in Switzerland as well as voluntary benefits. These mandatory benefits comprise guarantees regarding the level of interest paid annually on accrued pension savings as well how the rates on these accrued savings are converted into a pension payment at the time of retirement. The Company and the members contribute a defined percentage of salary to the pension arrangement. Credit accumulation is granted on these contributions. At retirement, the accumulated contributions are converted into a pension. The liability shown relates solely to active members and disability pensioners since the responsibility for meeting old-age pensions in payment is irrevocably transferred to an insurance company. Independent actuarial reviews of the ongoing benefit obligations were undertaken at December 31, 2015.

The principal assumptions used for the purposes of the actuarial valuations were as follows:

	<u>2015 % pa</u>	<u>2014 % pa</u>
Discount rate	0.90	1.20
Expected rate of salary increase	2.60	2.60
Interest credit rate	1.25	1.75
Demographic assumptions	BVG2010GT	BVG2010GT

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20. Retirement benefit obligation (continued)

(a) Defined benefit scheme (continued)

The table below shows the impact on the defined benefit obligation that a change in certain key assumptions would have:

<i>Assumption change</i>	<i>Defined benefit obligation \$</i>
(Increase)/decrease in discount rate by 0.25%	(16,089)/17,538
(Decrease)/increase in salary by 0.25%	(16,622)/16,964

Amounts recognised in the consolidated statement of comprehensive income in respect of the defined benefit scheme are as follows:

	<u>2015</u>	<u>2014</u>
Current service cost	\$ 1,072	\$ 739
Interest cost	174	217
Interest on plan assets	(137)	(200)
Past service cost	(254)	-
Administration costs	31	28
Prior year adjustment	-	(41)
	<u>\$ 886</u>	<u>\$ 743</u>

The amount included in the consolidated balance sheet arising from the Company's obligations with respect to its defined benefit scheme is as follows:

	<u>2015</u>	<u>2014</u>
Present value of defined benefit obligations	\$ 16,790	\$ 11,997
Fair value of plan assets	(13,506)	(9,123)
Retirement benefit obligation	<u>\$ 3,284</u>	<u>\$ 2,874</u>

Movements in the present value of the defined benefit obligation during the year are as follows:

	<u>2015</u>	<u>2014</u>
As at January 1	\$ 11,997	\$ 7,834
Current service cost	1,072	739
Interest cost	174	217
Contributions from plan participants	318	278
Actuarial loss	692	2,097
Net transfers	2,890	1,979
Past service cost	(254)	-
Administrative costs	31	28
Foreign currency translation adjustment	(130)	(1,175)
As at December 31	<u>\$ 16,790</u>	<u>\$ 11,997</u>

There were no actuarial gains or losses from changes in demographic assumptions. The actuarial loss in 2015 is primarily driven by the change in financial assumptions.

The average duration of the defined benefit obligations was 17.4 years in 2015 (2014: 18.6 years).

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20. Retirement benefit obligations (continued)

(a) Defined benefit scheme (continued)

Movements in the fair value of plan assets during the year are as follows:

	<u>2015</u>	<u>2014</u>
Opening fair value of plan assets	\$ 9,123	\$ 7,092
Interest income on plan assets	137	200
Actuarial gain (loss)	300	(187)
Contributions from plan participants	318	278
Employer contributions	855	693
Net transfers	2,890	1,979
Foreign currency translation adjustment	(117)	(932)
Closing fair value of plan assets	<u>\$ 13,506</u>	<u>\$ 9,123</u>

The analysis of the plan assets and the expected rate of return by asset class are not provided for the defined benefit scheme as the investment decisions are at the discretion of third parties to whom the Company has ceded investment risk under the insurance policies taken out to meet its obligations.

The Company expects to make a contribution of \$0.9 million (2014: \$0.7 million) to the defined benefit scheme during the next financial year.

(b) Defined contribution plan

The Company operates defined contribution plans in the Bermuda, Australia and United Kingdom branches. The total contributions for the year ended December 31, 2015 amounted to \$1.6 million (2014 - \$1.4 million).

The Company also maintains a defined contribution plan for employees of its US branch in accordance with Section 401(k) of the Internal Revenue Code. The total contribution for the year ended December 31, 2015 amounted to \$0.2 million (2014 - \$0.1 million).

21. Share capital

	<u>2015</u>	<u>2014</u>
Authorised, issued and fully paid, shares of CHF 0.91 (\$1) par value each	\$ 250,000	\$ 250,000
Contributed surplus	\$ 400,000	\$ 400,000

Fully paid issued shares, which have a par value of CHF 0.91 (\$1) each, carry one vote per share and carry a right to dividends.

Contributed surplus represents cash contributed by the shareholder in excess of the issued share capital.

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22. Ceded reinsurance

The Company uses retrocessional agreements to reduce its exposure to risk of loss on reinsurance assumed. These agreements generally provide for recovery of a portion of losses and loss expenses from retrocessionaires. The Company remains liable to its cedants to the extent that the retrocessionaires do not meet their obligations under these agreements. Failure of reinsurers to honour their obligations could result in losses to the Company. The Company defines rated reinsurers as companies with a minimum S&P or A.M. Best rating of A+, and net assets of more than \$100 million and where the retroceded amount is equal to or less than 10% of the reinsurer's net assets. The Company evaluates the financial condition of its rated reinsurers and monitors concentration of credit risk, on an ongoing basis, arising from similar geographic regions, activities, or economic characteristics of the reinsurers in order to minimise its exposure to significant losses from rated reinsurer insolvencies. Provisions are made for amounts considered potentially uncollectible.

The Company requires non-rated reinsurers to fully collateralise their reinsurance obligations. As further discussed in Note 4 under 'Credit Risk', the Company's maximum exposure to unrated reinsurers is fully collateralised.

In addition to purchasing retrocessional cover, the Company also uses derivative instruments to cover certain assumed reinsurance risks. Refer to Note 2 and Note 8.

23. Acquisition expenses

	<u>2015</u>	<u>2014</u>
Acquisition expenses	\$ 381,159	\$ 288,868
Change in deferred acquisition expenses	<u>(129,613)</u>	<u>(67,941)</u>
	<u>\$ 251,546</u>	<u>\$ 220,927</u>

24. Results of operating activities

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

	<u>2015</u>	<u>2014</u>
Depreciation of property and equipment	\$ 3,997	\$ 3,504
Amortisation of intangible assets	4,059	3,735
Operating lease charges	4,557	3,249
Foreign exchange (gains) losses	(5,087)	11,661

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25. Employee benefit expenses

	<u>2015</u>	<u>2014</u>
Wages and salaries	\$ 32,021	\$ 26,270
Long-term incentive compensation plan	5,361	1,481
Retirement benefit obligation costs - defined benefit scheme	886	743
Retirement benefit obligation costs - defined contribution scheme	1,855	1,613
Bonus and other benefits	16,794	12,153
	<u>\$ 56,917</u>	<u>\$ 42,260</u>

26. Commitments

- (a) The Company leases office space under operating leases which expire at various dates. The Company renews and enters into new leases in the ordinary course of business as required. Total rent expense with respect to these operating leases for the year ended December 31, 2015 was \$4.6 million (2014 - \$3.2 million).

Future minimum lease payments under the leases are expected to be as follows:

Year	
2016	\$ 3,205
2017	1,872
2018	1,481
2019	1,470
2020	574
Later	43
Total	<u>\$ 8,645</u>

- (b) The above lease agreements also include a maintenance commitment. Maintenance expense for the current year amounts to \$0.9 million (2014 - \$0.8 million) which has been included in general and administrative expenses.
- (c) Some lease agreements for office space provide an option to extend the lease beyond the expiration date.
- (d) Effective August 6, 2010, the Company entered into a Revolving Letter of Credit Facility Agreement ("Facility A") with Barclays Bank PLC ("Barclays Bank"). Facility A provided commitments from Barclays Bank in an aggregate amount of \$100.0 million and provided for the issuance and renewal of letters of credit which are used to support the Company's reinsurance obligations.

Facility A was amended effective September 12, 2014. Under the terms of the amended agreement the \$100.0 million commitment remained unchanged and the commitment termination date was extended to September 12, 2017. Under the terms of the amended agreement, letters of credit can now be issued in alternative currencies other than U.S. Dollars.

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26. Commitments (continued)

(d) (continued)

For letters of credit issued in Australian Dollars and subject to the applicable regulations of the Australian Prudential Regulation Authority, the final maturity date will not extend beyond September 12, 2019. For all other letters of credit issued the final maturity date will not extend beyond September 12, 2018.

Under Facility A, the Company is required to pledge cash or eligible securities with collateral value (as determined as therein provided) that equals or exceeds 100% of the aggregate amount of its outstanding letters of credit.

The unutilised portion of Facility A may be cancelled in whole or in part (if in part, in minimum amounts of \$0.5 million) by the Company without penalty upon due written notice of not less than five business days to Barclays Bank. Amounts so cancelled may not be re-instated. Facility A contains representations, warranties and covenants customary for facilities of this type. In addition to the customary covenants, the Company is required to promptly notify Barclays Bank on becoming aware of any negative change in outlook or downgrade in its current rating by any rating agency.

Effective August 9, 2011, the Company entered into a second Revolving Letter of Credit Facility Agreement ("Facility B") with Barclays Bank. Facility B provided commitments from Barclays Bank in an aggregate amount of Australian Dollar \$1.0 million. Facility B expired on December 31, 2014. Existing Australian Dollar letters of credit previously issued under Facility B are now issued under the alternative currency provisions which were included in the amendment to Facility A as outlined above.

At December 31, 2015, Barclays Bank has issued letters of credit of \$13.5 million (2014 - \$11.8 million) in favour of ceding companies under Facility A. The Company pledged as security \$20.8 million (2014 - \$62.7 million) of fixed interest securities and \$1.0 million (2014 - \$11.2 million) of cash to collateralise the letters of credit.

Effective May 14, 2012, the Company entered into a Revolving Letter of Credit Facility Agreement ("Mizuho Facility") with Mizuho Corporate Bank Ltd. ("Mizuho Bank"). The Mizuho Facility provided commitments from Mizuho Bank in an aggregate amount of \$300.0 million and provided for the issuance and renewal of letters of credit which are used to support the Company's reinsurance obligations. The Mizuho Facility was amended effective January 21, 2015 (the "Amended Mizuho Facility Agreement"). Under the Amended Mizuho Facility Agreement, the Mizuho Facility was increased to \$600.0 million and letters of credit can be issued in Australian Dollars. A further amendment effective January 16, 2016 extended the commitment termination date to January 16, 2017. The Mizuho Facility contains representations, warranties and covenants customary for facilities of this type.

At December 31, 2015, Mizuho Bank has issued letters of credit of \$470.1 million (2014 - \$395.3 million) in favour of ceding companies.

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*(Expressed in thousands of United States Dollars)***27. Long term incentive compensation plan**

The Company granted its accumulation units under its long term incentive compensation plan on April 1 of each calendar year from 2010 to 2015. The value of the units are based on movements in the net asset value of the Company and will be settled in cash four years from the date of issue if the fair value of units at that date exceeds the grant date fair value.

The units issued as at December 31, 2015 and grant date fair value per unit are summarised as follows:

Grant year	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Units issued	6,003,075	10,759,980	2,743,043	988,273
Fair value per unit at grant date	\$0.66	\$0.30	\$0.97	\$1.24

In accordance with IFRS 2, the fair value of options granted is estimated using a pricing model with the following assumptions:

Grant year	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Expected unit life	4 years	4 years	4 years	4 years
Expected volatility	20%	16%	13%	6%
Risk-free interest rate	1.4%	1.2%	0.8%	0.2%
Forfeiture rate	6%	15%	22%	23%

At December 31, 2015, the fair value per unit discounted at the risk free rates are summarised as follows:

Grant year	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Fair value per unit	\$0.85	\$0.49	\$0.72	\$2.16

The table below shows the recognised and unrecognised expense for grant years 2015, 2014, 2013 and 2012:

Grant year	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
	<u>\$'000</u>	<u>\$'000</u>	<u>\$'000</u>	<u>\$'000</u>
Expense during the year	\$ 957	\$ 1,723	\$ 1,112	\$ 856
Unrecognised expense (to be recognised over remaining service period)	\$ 4,146	\$ 2,966	\$ 617	\$ 133
Remaining service period (in months)	39	27	15	3

On March 31, 2015, accumulation units granted on April 1, 2011 were settled in cash. The total cash settlement awarded on March 31, 2015 was \$0.5 million.

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27. Long term incentive compensation plan (continued)

The activity during 2015 is summarised as follows:

Grant year	2015 Units	2014 Units	2013 Units	2012 Units	2011 Units
Outstanding at beginning of year	–	11,119,980	2,955,500	1,110,448	619,496
Granted	6,117,593	–	–	–	–
Exercised	–	–	(111,025)	(89,736)	(616,496)
Forfeited	(114,518)	(360,000)	(101,432)	(32,439)	–
Adjustment	–	–	–	–	–
Outstanding at end of year	<u>6,003,075</u>	<u>10,759,980</u>	<u>2,743,043</u>	<u>988,273</u>	<u>–</u>

On March 31, 2015, in accordance with an executive compensation agreement, accumulation units granted on April 1, 2012 and April 1, 2013 were settled in cash prior to the vesting date. The units were settled at the fair value per unit at grant date.

28. Related party disclosures

Transactions with affiliates

The following transactions were conducted with related parties during the year and are based on arm's length arrangements.

- a) The Company assumed several reinsurance agreements from related parties under common control. The reinsurance premiums assumed under these agreements totaled \$18.6 million (2014 - \$7.6 million) with associated acquisition expenses of \$0.6 million (2014 - \$0.7 million) and net loss and loss expenses incurred of \$3.2 million (2014 - \$4.6 million). As at December 31, 2015, the consolidated balance sheet includes \$2.7 million (2014 - \$1.9 million), \$1.8 million (2014 - \$0.8 million) and \$0.2 million (2014 - \$0.1 million) of premiums receivable, unearned premium and deferred acquisition costs, respectively.

In addition, the Company assumed a catastrophe swap derivative contract from a related party under common control during the year. The derivative premiums assumed under the agreement totalled \$4.1 million (2014 - \$nil).

- b) Effective July 1, 2015, Tokio Millennium Re AG – U.K. branch (“TMRUK”) entered into a loss portfolio transfer agreement (“LPTA”) with Tokio Marine Global Re Asia Ltd. (“TMG Re Asia”) for a consideration of \$43.8 million. Reserves (outstanding losses and loss expenses and unearned premiums) were transferred and recorded in TMRUK’s balance sheet. The LPTA has been accounted for under insurance accounting.

As at December 31, 2015, the consolidated balance sheet includes \$36.9 million, \$3.8 million, \$36.4 million, \$1.8 million and \$2.1 million of cash, premiums receivable, outstanding losses and loss expenses, deferred fee income and accounts payable, respectively, in relation to this LPTA. The amortisation of deferred fee income is based on the expected claims payout pattern and settlement period.

- c) Effective July 1, 2015, the Company established an investment management agreement with a related party under common control. The Company incurred investment management fees of \$1.0 million for the year ended December 31, 2015. The consolidated balance sheet includes \$0.6 million of accounts payable and accrued expenses as at December 31, 2015.

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28. Related party disclosures (continued)

Key management personnel compensation

The aggregate remuneration of Directors and key management was as follows:

	<u>2015</u>		<u>2014</u>
Wages and salaries	\$ 3,498	\$	3,740
Long term incentive compensation plan	1,527		537
Retirement benefit obligation costs	326		200
Bonus and other benefits	1,718		2,632
	<u>\$ 7,069</u>	\$	<u>7,109</u>

29. Statutory requirements

TMR AG is supervised by the Swiss Financial Market Supervisory Authority ("FINMA"), the Bermuda Monetary Authority ("BMA"), the Australian Prudential Regulation Authority ("APRA"), the New York State Department of Financial Services ("NYSDFS"), the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA").

The minimum required statutory capital and surplus is the amount of statutory capital and surplus necessary to satisfy regulatory requirements based on the Company's current operations.

(a) Switzerland

The Company (since redomestication) and the Swiss operating entity are regulated by FINMA pursuant to the Insurance Supervisory Law. The Company's accounts are prepared in accordance with the Swiss Code of Obligations, the Insurance Supervisory Law and the Insurance Supervisory Ordinance.

TMR AG is obligated to maintain a minimum level of capital based on the Swiss Code of Obligations and Insurance Supervisory Law. In addition, the Company is required to perform a minimum solvency margin calculation based on the Solvency I and Swiss Solvency Test ("SST") regulations as stipulated by the Insurance Supervisory Law. The SST is based on an economic view and required capital is derived from an internal capital model. The amount of dividends that TMR AG is permitted to distribute is restricted to freely distributable reserves which consist of retained earnings and the current year profit. The solvency and capital requirements must still be met following any distribution. As at December 31, 2015 the required solvency I margin was \$260.5 million and the actual amount was \$1,130.1 million. The Company met all its capital requirements at December 31, 2015.

(b) Bermuda

Tokio Millennium Re AG – Bermuda branch ("TMRB") is registered under The Insurance Act 1978 (Bermuda), Amendments thereto and Related Regulations (the "Insurance Act") as a Class 3B insurer. Under the Insurance Act, the Company is required to annually prepare and file statutory and IFRS financial statements and a statutory financial return. The Insurance Act also requires the Company to maintain minimum levels of statutory capital and surplus. At December 31, 2015 and 2014, this amount was \$201.2 million and \$151.1 million, respectively. Actual statutory capital and surplus was \$830.8 million and \$959.3 million, respectively.

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Notes to Consolidated Financial Statements

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29. Statutory requirements (continued)

(b) *Bermuda (continued)*

The Bermuda Solvency Capital Requirement (“BSCR”) is a risk-based capital model used to determine an enhanced capital requirement and target capital level (defined as 120% of the enhanced capital requirement) for Class 3B insurers. The prescribed form of capital and solvency return, comprises the insurer’s BSCR model, a schedule of fixed income investments by rating category, a schedule of net loss and loss expense provision by line of business, a schedule of premiums written by line of business, a schedule of risk management and a schedule of fixed income securities by security type. The BSCR includes a standardised model used to measure the risk associated with an insurer’s assets, liabilities and premiums, and a formula to take account of catastrophe risk exposure. The Authority requires all Class 3B insurers to maintain their capital at a target level which is 120% of the amount calculated in accordance with the BSCR or the Company’s approved internal model (the Enhanced Capital Requirement or “ECR”). In addition, TMRB is required to maintain a minimum solvency margin. Both requirements have been met.

The Insurance Act limits the maximum amount of annual dividends and distributions that may be paid by the Company in any year which would exceed 25% of its prior year statutory capital and surplus or reduce its prior year statutory capital by 15% or more, without the prior approval of the BMA. Furthermore, the Company is not permitted to declare or pay a dividend, or make a distribution out of contributed surplus, if the realisable value of its assets would be less than the aggregate of its liabilities, issued share capital and share premium accounts. During 2015, the Company distributed a total of \$71.3 million (2014: \$140.0 million) to Tokio Marine Holdings, Inc. and therefore no approval was required.

The Company is also required to maintain a minimum liquidity ratio whereby the value of its relevant assets is not less than 75% of the amount of its relevant liabilities and this has been met. Relevant assets include cash and cash equivalents, short-term investments, catastrophe bonds, fixed interest securities, accrued interest receivable, premiums receivable, funds withheld and other assets. Certain categories of assets do not qualify as relevant assets under the statute. Relevant liabilities are outstanding losses and loss expenses, unearned premiums, deferred fee income, funds withheld ceded, accounts payable and accrued expenses, net of outstanding losses recoverable from reinsurers and prepaid reinsurance premiums.

(c) *Australia*

Tokio Millennium Re AG – Australia branch (“TMRA”) is authorised to carry on insurance business under subsection 12(2) of the Insurance Act 1973. TMRA is regulated by the Australian Prudential Regulation Authority (“APRA”) in accordance with the Insurance Act 1973 and APRA Prudential Standards. TMRA’s regulatory reporting is prepared in accordance with the Australian Accounting Standards and APRA Prudential Standards. TMRA have complied with the APRA requirements in both 2015 and 2014.

APRA Prudential Standards require the maintenance of net assets in Australia in excess of a calculated Prescribed Capital Amount (“PCA”). The net assets in Australia at December 31, 2015 were \$79.7 million (2014 - \$88.9 million) and resulted in a surplus of \$40.2 million (2014 - \$39.6 million) above the PCA of \$39.5 million (2014 - \$49.3 million) estimated under the new Prudential Standards.

TMRA has an Internal Capital Adequacy Assessment Process (“ICAAP”) to ensure compliance with regulatory capital requirements. In accordance with ICAAP, TMRA monitors its capital adequacy in order to ensure compliance with the relevant capital targets.

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29. Statutory requirements (continued)

(d) United States

Tokio Millennium Re AG – US branch (“TMRUS”) is required to file a set of financial statements prepared in accordance with statutory accounting practices prescribed or permitted by the U.S. insurance regulators. Statutory net income and statutory surplus, as reported to the insurance regulatory authorities, differ in certain respect from the amounts prepared in accordance with IFRS and the main differences relate to the treatment of deferred acquisition costs, deferred income, unrealised appreciation or decline in value of investments and non-admitted assets and deferred income taxes.

Minimum required statutory capital and surplus is based on the greater of the Risk Based Capital (RBC) level that would trigger regulatory action or minimum requirements per state insurance regulation. At both December 31, 2015 and 2014, TMRUS exceeded the minimum required statutory capital and surplus requirement and also exceeded the RBC minimum required level. TMRUS is required to maintain a minimum combined statutory surplus of \$145.7 million. As of December 31, 2015, the statutory surplus was \$217.9 million (2014: \$102.8 million).

TMRUS as a U.S. Branch does not pay ordinary dividends and would need approval from the New York State Department of Financial Services for any return of capital to TMRAG. As of December 31, 2015, TMRUS did not return any capital to TMRAG. Any return of capital in subsequent periods would need to be approved by the NYSDFS based on the financial condition of TMRUS.

(e) United Kingdom

Tokio Millennium Re AG – UK branch (“TMRUK”) is authorised by the Prudential Regulation Authority (“PRA”), and regulated jointly by the PRA and Financial Conduct Authority (“FCA”). The PRA oversees compliance with established periodic auditing and reporting requirements, minimum solvency margins, and capital assessment requirements. Both the PRA and the FCA oversee compliance with risk assessment reviews and various other requirements.

At December 31, 2015, TMRUK was subject to the Solvency I regime. However, as a new UK branch, a waiver was submitted for the branch to be exempted from the Solvency I return submission, as this will be superseded by Solvency II. TMRUK is also not required to hold localised assets.

30. Subsequent events

The Company has completed its subsequent events evaluation for the period subsequent to the consolidated balance sheet date of December 31, 2015, through March 2, 2016, the date the consolidated financial statements were authorised for issue. There were no subsequent events that would warrant an adjustment to the consolidated financial statements.