



**April 28, 2021**

**Report of Independent Auditors**

**To the Board of Directors of HCC Reinsurance Company Limited**

We have audited the accompanying condensed consolidated financial statements of HCC Reinsurance Company Limited and its subsidiaries, which comprise the condensed consolidated balance sheets and condensed consolidated statements of capital and surplus as of December 31, 2020 and 2019, and the related condensed consolidated statements of income for the years then ended, and the related notes to the condensed consolidated financial statements.

**Management's responsibility for the condensed consolidated financial statements**

Management is responsible for the preparation and fair presentation of the condensed consolidated financial statements in accordance with the financial reporting provisions of the Insurance Act 1978, amendments thereto and the Insurance Account Rules 2016 with respect to condensed general purpose financial statements (the 'Legislation'). Management is also responsible for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of condensed consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the condensed consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the condensed consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the condensed 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 Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the condensed consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



**Basis for adverse opinion on U.S. generally accepted accounting principles**

As described in Note 3 of the condensed consolidated financial statements, the condensed consolidated financial statements are prepared by the Company on the basis of the financial reporting provisions of the Legislation, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the condensed consolidated financial statements of the variances between the regulatory basis of accounting described in Note 3 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

**Adverse opinion on U.S. generally accepted accounting principles**

In our opinion, because of the significance of the matter discussed in the “Basis for adverse opinion on U.S. generally accepted accounting principles” paragraph, the condensed consolidated financial statements referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the Company and its subsidiaries as of December 31, 2020 and 2019, or the results of their operations or their cash flows for the years then ended.

**Opinion on regulatory basis of accounting**

In our opinion, the condensed consolidated financial statements referred to above present fairly, in all material respects, the financial position of HCC Reinsurance Company Limited and its subsidiaries as of December 31, 2020 and 2019, and the results of their operations for the years then ended in accordance with the financial reporting provisions of the Legislation described in Note 3.

*PricewaterhouseCoopers Ltd.*

**Chartered Professional Accountants**

**CONDENSED CONSOLIDATED BALANCE SHEET**

HCC Reinsurance Company Limited

As at **December 31, 2020**

expressed in ['000s]

**United States Dollars**

LINE No.		2020	2019
1.	CASH AND CASH EQUIVALENTS	69,586	15,175
2.	QUOTED INVESTMENTS:		
(a)	Bonds and Debentures		
	i. Held to maturity		
	ii. Other	293,665	251,370
(b)	Total Bonds and Debentures	293,665	251,370
(f)	Total quoted investments	293,665	251,370
3.	UNQUOTED INVESTMENTS:		
(f)	Total unquoted investments	-	-
4.	INVESTMENTS IN AND ADVANCES TO AFFILIATES		
(h)	Total investments in and advances to affiliates	-	-
5.	INVESTMENTS IN MORTGAGE LOANS ON REAL ESTATE:		
(c)	Total investments in mortgage loans on real estate	-	-
6.	POLICY LOANS		
7.	REAL ESTATE:		
(c)	Total real estate	-	-
8.	COLLATERAL LOANS		
9.	INVESTMENT INCOME DUE AND ACCRUED	1,614	1,705
10.	ACCOUNTS AND PREMIUMS RECEIVABLE:		
(a)	In course of collection	3,383	3,253
(b)	Deferred - not yet due	64,041	54,812
(c)	Receivables from retrocessional contracts	-	-
(d)	Total accounts and premiums receivable	67,424	58,065
11.	REINSURANCE BALANCES RECEIVABLE:		
(a)	Foreign affiliates		
(b)	Domestic affiliates		
(c)	Pools & associations		
(d)	All other insurers	28	-
(e)	Total reinsurance balance receivable	28	-
12.	FUNDS HELD BY CEDING REINSURERS	38,461	33,067
13.	SUNDRY ASSETS:		
(a)	Derivative instruments	8,637	8,862
(b)	Segregated accounts companies - long-term business - variable annuities		
(c)	Segregated accounts companies - long-term business - other		
(d)	Segregated accounts companies - general business		
(e)	Deposit assets		
(f)	Deferred acquisition costs	31,045	30,359
(g)	Net receivables for investments sold		
(h)	Airplane	24,901	-
(i)	Income Tax Receivable	12,945	
(j)	Amounts due from affiliates	446	
(k)	Total sundry assets	77,974	39,221
14.	LETTERS OF CREDIT, GUARANTEES AND OTHER INSTRUMENTS		
(a)	Letters of credit		
(b)	Guarantees		
(c)	Other instruments		
(e)	Total letters of credit, guarantees and other instruments	-	-
15.	TOTAL	548,752	398,603
<b>TOTAL INSURANCE RESERVES, OTHER LIABILITIES AND STATUTORY CAPITAL AND SURPLUS</b>			
16.	UNEARNED PREMIUM RESERVE		
(a)	Gross unearned premium reserves	169,514	180,950
(b)	Less: Ceded unearned premium reserve		
	i. Foreign affiliates	10,826	11,730
	ii. Domestic affiliates		
	iii. Pools & associations		
	iv. All other insurers	30,381	34,747
(c)	Total ceded unearned premium reserve	41,207	46,477
(d)	Net unearned premium reserve	128,307	134,473
17.	LOSS AND LOSS EXPENSE PROVISIONS:		

**CONDENSED CONSOLIDATED BALANCE SHEET**

HCC Reinsurance Company Limited

As at **December 31, 2020**

expressed in ['000s] **United States Dollars**

LINE No.		2020	2019
(a)	Gross loss and loss expense provisions	122,480	5,584
(b)	Less : Reinsurance recoverable balance		
	i. Foreign affiliates		
	ii. Domestic affiliates		-
	iii. Pools & associations		
	iv. All other reinsurers	1,145	293
(c)	Total reinsurance recoverable balance	1,145	293
(d)	Net loss and loss expense provisions	121,335	5,291
18.	OTHER GENERAL BUSINESS INSURANCE RESERVES		
19.	TOTAL GENERAL BUSINESS INSURANCE RESERVES	249,642	139,764
	<b>LONG-TERM BUSINESS INSURANCE RESERVES</b>		
20.	RESERVE FOR REPORTED CLAIMS		
21.	RESERVE FOR UNREPORTED CLAIMS		
22.	POLICY RESERVES - LIFE		
23.	POLICY RESERVES - ACCIDENT AND HEALTH		
24.	POLICYHOLDERS' FUNDS ON DEPOSIT		
25.	LIABILITY FOR FUTURE POLICYHOLDERS' DIVIDENDS		
26.	OTHER LONG-TERM BUSINESS INSURANCE RESERVES		
27.	TOTAL LONG-TERM BUSINESS INSURANCE RESERVES		
(d)	<b>Total Net Long-Term Business Insurance Reserves</b>	-	-
	<b>OTHER LIABILITIES</b>		
28.	INSURANCE AND REINSURANCE BALANCES PAYABLE	2,977	2,451
29.	COMMISSIONS, EXPENSES, FEES AND TAXES PAYABLE	10,287	15,877
30.	LOANS AND NOTES PAYABLE		
31.	(a) INCOME TAXES PAYABLE	-	1,284
	(b) DEFERRED INCOME TAXES	3,754	3,274
32.	AMOUNTS DUE TO AFFILIATES	-	2,181
33.	ACCOUNTS PAYABLE AND ACCRUED LIABILITIES	131	38
34.	FUNDS HELD UNDER REINSURANCE CONTRACTS:		
35.	DIVIDENDS PAYABLE		
36.	SUNDRY LIABILITIES:		
(a)	Derivative instruments	8,470	10,700
(b)	Segregated accounts companies		
(c)	Deposit liabilities		
(d)	Net payable for investments purchased	-	-
(e)	Holdback and earnout liability	10,084	9,982
(f)	Reinsurers' portion of airplane	10,232	
(h)	Total sundry liabilities	28,786	20,682
37.	LETTERS OF CREDIT, GUARANTEES AND OTHER INSTRUMENTS:		
(d)	Total letters of credit, guarantees and other instruments	-	-
38.	TOTAL OTHER LIABILITIES	45,935	45,787
39.	TOTAL INSURANCE RESERVES AND OTHER LIABILITIES	295,577	185,551
	<b>CAPITAL AND SURPLUS</b>		
40.	TOTAL CAPITAL AND SURPLUS	253,175	213,052
41.	TOTAL	548,752	398,603

TRUE

TRUE

**CONDENSED CONSOLIDATED STATEMENT OF INCOME**

HCC Reinsurance Company Limited  
 As at **December 31, 2020**  
 expressed in ['000s] **United States Dollars**

LINE No.		2020	2019
	<b>GENERAL BUSINESS UNDERWRITING INCOME</b>		
1.	GROSS PREMIUMS WRITTEN		
	(a) Direct gross premiums written	3,856	11,825
	(b) Assumed gross premiums written	41,894	49,790
	(c) Total gross premiums written	45,750	61,615
2.	REINSURANCE PREMIUMS CEDED	93	3,779
3.	NET PREMIUMS WRITTEN	45,657	57,836
4.	INCREASE (DECREASE) IN UNEARNED PREMIUMS	6,166	(15,972)
5.	NET PREMIUMS EARNED	51,823	41,864
6.	OTHER INSURANCE INCOME	1,000	-
7.	TOTAL GENERAL BUSINESS UNDERWRITING INCOME	52,823	41,864
	<b>GENERAL BUSINESS UNDERWRITING EXPENSES</b>		
8.	NET LOSSES INCURRED AND NET LOSS EXPENSES INCURRED	120,436	4,258
9.	COMMISSIONS AND BROKERAGE	10,801	9,837
10.	TOTAL GENERAL BUSINESS UNDERWRITING EXPENSES	131,237	14,095
11.	<b>NET UNDERWRITING PROFIT (LOSS) - GENERAL BUSINESS</b>	(78,414)	27,769
	<b>LONG-TERM BUSINESS INCOME</b>		
12.	GROSS PREMIUMS AND OTHER CONSIDERATIONS:		
	(a) Direct gross premiums and other considerations		
	(b) Assumed gross premiums and other considerations		
	(c) Total gross premiums and other considerations	-	-
13.	PREMIUMS CEDED		
14.	NET PREMIUMS AND OTHER CONSIDERATIONS:		
	(a) Life		
	(b) Annuities		
	(c) Accident and health		
	(d) Total net premiums and other considerations	-	-
15.	OTHER INSURANCE INCOME		
16.	TOTAL LONG-TERM BUSINESS INCOME	-	-
	<b>LONG-TERM BUSINESS DEDUCTIONS AND EXPENSES</b>		
17.	CLAIMS - LIFE		
18.	POLICYHOLDERS' DIVIDENDS		
19.	SURRENDERS		
20.	MATURITIES		
21.	ANNUITIES		
22.	ACCIDENT AND HEALTH BENEFITS		
23.	COMMISSIONS		
24.	OTHER		
25.	TOTAL LONG-TERM BUSINESS DEDUCTIONS AND EXPENSES	-	-
26.	INCREASE (DECREASE) IN POLICY RESERVES (ACTUARIAL LIABILITIES):		
	(a) Life		
	(b) Annuities		
	(c) Accident and health		
	(d) Total increase (decrease) in policy reserves	-	-
27.	TOTAL LONG-TERM BUSINESS EXPENSES	-	-

**CONDENSED CONSOLIDATED STATEMENT OF INCOME**

HCC Reinsurance Company Limited  
 As at **December 31, 2020**  
 expressed in ['000s] **United States Dollars**

LINE No.	2020	2019
28. <b>NET UNDERWRITING PROFIT (LOSS) - LONG-TERM BUSINESS</b>	-	-
29. <b>COMBINED NET UNDERWRITING RESULTS BEFORE THE UNDERNOTED ITEMS</b>	(78,414)	27,769
<b>UNDERNOTED ITEMS</b>		
30. <b>COMBINED OPERATING EXPENSE</b>		
(a) General and administration	1,308	1,093
(b) Personnel cost		
(c) Other	1	-
(d) Total combined operating expenses	1,309	1,093
31. <b>COMBINED INVESTMENT INCOME - NET</b>	7,333	8,179
32. <b>COMBINED OTHER INCOME (DEDUCTIONS)</b>	1,153	1,902
33. <b>COMBINED INCOME BEFORE TAXES</b>	(71,237)	36,757
34. <b>COMBINED INCOME TAXES (IF APPLICABLE):</b>		
(a) Current	(14,229)	7,189
(b) Deferred	(634)	776
(c) Total	(14,863)	7,965
35. <b>COMBINED INCOME BEFORE REALIZED GAINS (LOSSES)</b>	(56,374)	28,792
36. <b>COMBINED REALIZED GAINS (LOSSES)</b>	2,311	2,974
37. <b>COMBINED INTEREST CHARGES</b>		
38. <b>NET INCOME</b>	(54,063)	31,766

**CONDENSED CONSOLIDATED STATEMENT OF CAPITAL AND SURPLUS**

HCC Reinsurance Company Limited  
 As at December 31, 2020  
 expressed in ['000s] United States Dollars

LINE No.		2020	2019
1.	<b>CAPITAL:</b>		
(a)	Capital Stock		
	(i) Common Shares	120	120
	authorized 120,000 shares of par		
	value \$ 1,000 each issued and		
	fully paid 120,000 shares		
	(ii)		
	(A) Preferred shares:		
	authorized _____ shares of par		
	value _____ each issued and		
	fully paid _____ shares		
	aggregate liquidation value for –		
	2020 _____		
	2019 _____		
	(B) Preferred shares issued by a subsidiary:		
	authorized _____ shares of par		
	value _____ each issued and		
	fully paid _____ shares		
	aggregate liquidation value for –		
	2020 _____		
	2019 _____		
	(iii) Treasury Shares		
	repurchased _____ shares of par		
	value _____ each issued		
(b)	Contributed surplus	173,865	83,865
(c)	Any other fixed capital		
	(i) Hybrid capital instruments		
	(ii) Guarantees and others		
	(iii) Total any other fixed capital	-	-
(d)	Total Capital	173,985	83,985
2.	<b>SURPLUS:</b>		
(a)	Surplus - Beginning of Year	129,067	91,680
(b)	Add: Income for the year	(54,063)	31,766
(c)	Less: Dividends paid and payable	-	-
(d)	Add (Deduct) change in unrealized appreciation (depreciation) of investments	4,186	5,621
(e)	Add (Deduct) change in any other surplus		
(f)	Surplus - End of Year	79,190	129,067
3.	<b>MINORITY INTEREST</b>		
4.	<b>TOTAL CAPITAL AND SURPLUS</b>	253,175	213,052

**HCC REINSURANCE COMPANY LIMITED**  
**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2020 and 2019**  
**(expressed in United States Dollars)**

PART I

1. HCC Reinsurance Company Ltd. (the Company) is a wholly-owned subsidiary of HCC Insurance Holdings, Inc. (HCC), a Delaware Corporation, which is ultimately owned by Tokio Marine Holdings, Inc. (TMHD), a Japanese Corporation. HCC Re Agency Ltd., a Bermuda corporation, and wholly-owned subsidiary of the Company is consolidated in the financial statements. The Company holds a Class 3A license under the Insurance Act of 1978.
2. The Company primarily writes business directly and assumes business from affiliated insurance companies. The Company primarily writes medium to large limit aircraft and commercial real estate residual value, title, mortgage guarantee and excess tax insurance policies. Additionally, the Company writes crisis management, eminent domain policies and during 2020, the Company assumed a book of surety and stop loss business from an affiliated insurance company.
3. The condensed consolidated general purpose financial statements have been prepared in conformity with the financial reporting provisions of the Insurance Act 1978, amendments thereto and the Insurance Account Rules 2016 with respect to Condensed General Purpose Financial Statements (the "Legislation"). The condensed consolidated general purpose financial statements are based upon accounting principles generally accepted in the United States of America ("US GAAP"), but are in accordance with reporting requirements of the Legislation, which varies in certain respects from US GAAP. The more significant variances are as follows:
  - A consolidated statement of cash flow is not included;
  - A consolidated statement of comprehensive income is not included;
  - The presentation and classification of financial statement line items is in accordance with Schedules IX and XI of the Insurance Account Rules 2016 and differ from the expected presentation and classification under US GAAP.
  - The notes included in the condensed consolidated general purpose financial statements have been prepared in accordance with Schedule X of the Insurance Account Rules 2016 and exclude certain information required under US GAAP.

The condensed consolidated general purpose financial statements include the accounts of the Company and its subsidiary. All significant intercompany transactions and balances have been eliminated.

4. SIGNIFICANT ACCOUNTING POLICIES

a. Premiums earned and reinsurance premiums

Premiums are written on an accrual basis, net of reinsurance, and are generally included in earnings on a pro-rata basis over the lives of the related policies and the unearned portion is recognized as a liability on the balance sheet and is computed by pro-rata method. Premiums for commercial title insurance policies are recognized in earnings on the effective date of the contract.

b. Loss and loss expenses provisions

Loss and loss expenses provisions are based on undiscounted estimates of payments to be made for reported losses, net of reinsurance. Estimates for reported losses are based on all available information, including reports received from ceding companies on assumed business. Estimates for incurred but not reported losses are based on the Company's and industry experience. While management believes that amounts included in the accompanying financial statements are adequate, such estimates may be more or less than the amounts ultimately paid when the claims are settled. The estimates are continually reviewed and any changes are reflected in current operations.

c. Foreign currency translation

Assets and liabilities recorded in foreign currencies are revalued at current exchange rates. Revenue and expenses recorded in foreign currencies are revalued based on the effective date of the original transaction. Gains and losses from foreign currency transactions are included in combined other income (deductions).

d. Reinsurance

All reinsurance amounts are calculated and recorded in a manner consistent with the underlying reinsured contracts. The Company reviews the collectability of the reinsurance recoverables and has recorded no allowance for uncollectible reinsurance. The estimate utilized to calculate the allowance is subject to change and this could affect the level of reserve required. Certain reinsurance agreements allow for reinsurance premiums to be held by the ceding entity as prescribed in the contract. The Company records these applicable reinsurance transactions as funds held by ceding reinsurers.

e. Cash and cash equivalents

The Company considers all certificates of deposit with original maturities of three months or less and money market funds to be cash equivalents. Cash and cash equivalents include restricted fiduciary funds of \$8,220,000 as of December 31, 2020 and \$5,766,000 as of December 31, 2019 held in accordance with an acquisition agreement. The corresponding liability is included with sundry liabilities.

f. Investments

Bonds and debentures are classified as available for sale and reported at fair value. There were no restricted bonds and debentures as of December 31, 2020 compared to bonds and debentures including restricted fiduciary funds of \$1,239,000 as of December 31, 2019.

A security has an impairment loss when its fair value is less than its cost or amortized cost at the balance sheet date. The Company evaluated impaired securities for possible other-than-temporary impairment loss at each quarter end, considering various factors including: 1) amount by which the security's fair value is less than its cost, 2) length of time the security has been impaired, 3) whether the Company intended to sell the security, 4) if it is more likely than not that the Company will sell the security before recovery of its amortized cost basis, 5) whether the impairment is due to an issuer-specific event, credit issues or change in market interest rates, 6) the security's credit rating and any recent downgrades and 7) stress testing of expected cash flows under various scenarios. The Company recognized no other-than-temporary impairment losses in 2020 and 2019.

Realized investment gains or losses are determined based on specific identification and included in earnings on the trade date. If a structured security fails to pay the full amount of expected principal, the Company recognizes the unpaid amount as a realized loss in the period due and permanently reduces the security's cost basis. If a security or loan is non-income producing, it is placed on a non-accrual status and any cash proceeds are applied as a reduction of principal when received.



**HCC REINSURANCE COMPANY LIMITED**  
**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2020 and 2019**  
**(expressed in United States Dollars)**

PART I (con't)

g. Derivative instruments

During 2004, the Company assumed a transaction whose underlying exposure is the value of a portfolio of home mortgages over a 22 year period as measured by the Halifax Price Index. The fair value of this contract is reported as a derivative asset and was \$4,826,000 and \$4,047,000 as of December 31, 2020 and December 31, 2019, respectively.

During 2016, the Company wrote a transaction whose underlying exposure is the value of an investment portfolio over a 10 year period. This transaction is reported as a derivative liability. The Company ceded 45% of this transaction to an unaffiliated entity. The ceded portion is reported as a derivative asset. At December 31, 2020, the related derivative liability and asset were \$8,470,000 and \$3,812,000, respectively, compared to \$10,700,000 and \$4,815,000 respectively, at December 31, 2019.

5. THE BASIS OF RECOGNITION OF THE FOLLOWING ITEMS ARE:

- a. Premiums - Premiums are written on an accrual basis, net of reinsurance, and are included in earnings on a pro-rata basis over the lives of the related policies. The unearned portion is recognized as a liability on the balance sheet and is computed by pro-rata method.
- b. Investment income is earned on the accrual basis of accounting.
- c. Commission Income - Commission costs are deferred and charged to earnings proportionate with premiums earned.

6. TRANSLATION METHODS

Assets and liabilities recorded in foreign currencies are revalued at current exchange rates. Revenue and expenses recorded in foreign currencies are revalued based on the effective date of the original transaction. Translation gains and losses are recorded in combined other income (deductions) on the condensed consolidated statement of income.

7. FOREIGN CURRENCY CONTROL RESTRICTIONS - N/A

8. CONTINGENCIES

From time to time, the Company has ceded certain risks to other companies. Although the ceding of reinsurance does not discharge the primary insurer from liability to its policyholder, the Company participates in such agreements for the purpose of limiting its loss exposure and diversifying its business.

A contingent liability is present with respect to the Company's reinsurance which would become an actual liability to the extent that any reinsuring company failed to meet its obligations to the Company. However, in the opinion of management, with the experience of the companies involved, there is no exposure related to this scenario.

9. COMPANY DEFAULT - N/A

10. ARREARS DIVIDENDS - N/A

11. LOANS - N/A

12. RETIREMENT BENEFITS - N/A

13. INVESTMENTS - FAIR VALUE MEASUREMENTS

Items measured and reported at fair value by Levels 1, 2 and 3:

Level 1 - Inputs are based on quoted prices in active markets for identical instruments.

Level 2 - Inputs are based on observable market data (other than quoted prices), or are corroborated by observable market data. This category includes fixed maturity securities.

Level 3 - Inputs are observable and are not corroborated by market data.

The following tables summarize the Company's assets and liabilities measured and reported at fair value:

December 31, 2020:

Type of Financial Instrument	Level 1	Level 2	Level 3	Total
<b>Fixed maturity securities</b>				
Fixed income securities of states, municipalities, and political subdivisions	\$ -	\$ 17,141,000	\$ -	\$ 17,141,000
Special purpose revenue bonds of states, municipalities, and political subdivisions	-	79,117,000	-	79,117,000
Corporate securities	-	23,423,000	-	23,423,000
Residential mortgage-backed securities	-	84,398,000	-	84,398,000
Commercial mortgage-backed securities	-	21,590,000	-	21,590,000
Asset-backed securities	-	67,996,000	-	67,996,000
Total fixed maturity securities	-	293,665,000	-	293,665,000
Cash and short-term investments	44,388,000	15,268,000	-	59,656,000
Derivative instruments	-	-	8,637,000	8,637,000
<b>Total assets measured at fair value</b>	<b>\$ 44,388,000</b>	<b>\$ 308,933,000</b>	<b>\$ 8,637,000</b>	<b>\$ 361,958,000</b>
<b>Derivative instruments</b>				
Derivative instruments	-	-	8,470,000	8,470,000
Earnout liability	-	-	1,863,000	1,863,000
Holdback liability	-	8,220,000	-	8,220,000
<b>Total liabilities measured at fair value</b>	<b>\$ -</b>	<b>\$ 8,220,000</b>	<b>\$ 10,333,000</b>	<b>\$ 18,553,000</b>

**HCC REINSURANCE COMPANY LIMITED**  
**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2020 and 2019**  
**(expressed in United States Dollars)**

PART I (con't)

December 31, 2019:

Type of Financial Instrument	Level 1	Level 2	Level 3	Total
<b>Fixed maturity securities</b>				
Fixed income securities of states, municipalities, and political subdivisions	\$ -	\$ 13,839,000	\$ -	\$ 13,839,000
Special purpose revenue bonds of states, municipalities, and political subdivisions	-	69,741,000	-	69,741,000
Corporate securities	-	17,677,000	-	17,677,000
Residential mortgage-backed securities	-	68,584,000	-	68,584,000
Commercial mortgage-backed securities	-	17,015,000	-	17,015,000
Asset-backed securities	-	64,514,000	-	64,514,000
Total fixed maturity securities	-	251,370,000	-	251,370,000
Cash and short-term investments	1,128,000	12,686,000	-	13,814,000
Derivative instruments	-	-	8,862,000	8,862,000
<b>Total assets measured at fair value</b>	<b>\$ 1,128,000</b>	<b>\$ 264,056,000</b>	<b>\$ 8,862,000</b>	<b>\$ 274,046,000</b>
<b>Derivative instruments</b>				
Derivative instruments	-	-	10,700,000	10,700,000
Earnout liability	-	-	2,977,000	2,977,000
Holdback liability	-	7,005,000	-	7,005,000
<b>Total liabilities measured at fair value</b>	<b>\$ -</b>	<b>\$ 7,005,000</b>	<b>\$ 13,677,000</b>	<b>\$ 20,682,000</b>

14. INVESTMENTS - CONTRACTUAL MATURITY

The value of bonds at December 31, 2020 and 2019 by contractual maturity are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Fixed maturity securities:	<u>2020</u>	<u>2019</u>
Due within one year	\$ -	-
Due after one year through five years	11,188,000	11,213,000
Due after five years through ten years	29,842,000	23,964,000
Due after ten years	252,635,000	216,193,000
<b>Total fixed maturity securities</b>	<b>\$ 293,665,000</b>	<b>\$ 251,370,000</b>

15. RELATED PARTY TRANSACTIONS

Certain management functions are performed by affiliates of the Company, HCC Service Co. and HCC Service Co. UK Branch. Costs incurred by these affiliates are allocated to the Company pursuant to an intercompany cost allocation agreement. Additional intercompany payables are related to the timing of receivable and payables that arise in the course of business.

The Company reported amounts receivable/(payable) to affiliates as follows at December 31:

	<u>2020</u>	<u>2019</u>
HCC International Insurance Co.	\$ (154,000)	\$ (127,000)
HCC Service Company, Inc.	(96,000)	(2,081,000)
HCC Service Co. UK	-	(2,000)
HCCIG Agency	20,000	-
Houston Casualty Co.	647,000	-
U.S. Specialty Insurance Co.	29,000	29,000
<b>Total</b>	<b>\$ 446,000</b>	<b>\$ (2,181,000)</b>

At December 31, 2020, the Company had commissions payable of \$9,910,000 due to HCC Indemnity Guaranty, an affiliated company, and \$377,000 to unaffiliated companies.

The Company had amounts accounts and premium receivable due from affiliated companies of \$30,763,000 and \$24,346,000 at December 31, 2020 and December 31, 2019, respectively.

The Company has provided cash balances to affiliated ceding reinsurers as collateral against future losses incurred by the ceding reinsurers. Total funds held by ceding reinsurers at December 31, 2020 and 2019 were \$38,251,000 and \$33,067,000, respectively.

16. SUBSEQUENT EVENTS

On March 26, 2021, the Company commuted three reinsurance agreements providing stop-loss reinsurance to an affiliated Australian insurance company (see note 17). As part of the commutation, the Company paid total consideration of \$109.2 million, consisting of \$99.6 million of cash and the release of \$9.6 million of funds held. The commutation resulted in a loss of approximately \$300 thousands in the first quarter of 2021.

Subsequent events have been evaluated through April 28, 2021.

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PART I (cont)

17. ADDITIONAL DISCLOSURES

**Mortgage Insurance Collateral**

The Company reinsures excess losses on a portfolio of mortgage insurance policies that originated between 2009 and 2020. The Company provides collateral consisting of bonds, cash and accrued interest income of \$77,049,000 and \$63,717,000 at December 31, 2020 and December 31, 2019, respectively.

**COVID-19 and Assumed Australian Surety and Credit**

The outbreak of the novel strain of the coronavirus (COVID-19) was declared a global pandemic by the World Health Organization. This outbreak resulted in extended shutdowns of many businesses around the world, including the United States and Europe.

On June 30, 2020, the Company entered into three reinsurance agreements with an affiliated Australian insurance company, Tokio Marine and Nichido Fire Insurance Co., Limited – Australian Branch (TMNFA). The agreements provided stop-loss coverage to certain subsidiaries of TMNFA for a block of surety and credit business written through June 20, 2020 (the “Australian Surety and Credit” business). On June 30, 2020, the company recorded \$9.7 million of written premium and \$28.9 million of loss and loss expense provision. The Company also received a \$90.0 million capital contribution to provide additional capital support for any losses associated with the Australian Surety and Credit business. The loss and loss adjustment expense provision recorded on June 30, 2020, was based on an Actuarial Valuation Report performed by Taylor Fry, an unaffiliated actuary, as of March 31, 2020, and included significant losses related to the impact of COVID-19 on the Australian Surety and Credit business. We continued to monitor the exposure to COVID-19 and increased the loss and loss adjustment expense provision to \$109.7 million at December 31, 2020, based on an updated report from Taylor Fry. The Company commuted these reinsurance agreements with TMNFA on March 26, 2021 without significant additional loss.

PART II

A. 1 (a) CAPITAL STOCK

Authorized, issued and fully paid - 120,000 shares of US \$1.00 par value each - \$120,000.

1 (b) CONTRIBUTED SURPLUS

The Company received a \$90,000,000 capital contribution from HCC Insurance Holdings during 2020. There were no capital contributions during 2019.

2 (c) DIVIDENDS PAID AND PAYABLE

The Company did not pay any dividends during 2020 or 2019.

PART III

1. CASH AND CASH EQUIVALENTS

Cash consists of cash in banks and short term money market accounts. The Company considers all certificates of deposit with original maturities of three months or less and money market funds to be cash equivalents. Cash and cash equivalents include restricted fiduciary funds of \$8,220,000 as of December 31, 2020 and \$5,766,000 as of December 31, 2019 held in accordance with an acquisition agreement. The corresponding liability is included with sundry liabilities.

The Company reinsures excess losses on a portfolio of mortgage insurance policies that originated between 2009 and 2020. The Company provides collateral consisting of cash of \$9,475,000 and \$6,753,000 at December 31, 2020 and December 31, 2019, respectively.

2. QUOTED INVESTMENTS

Bonds and debentures are reported at fair value. Bonds and debentures are available for sale, but may be sold if the Company can reinvest the proceeds at a higher effective yield or if the security has credit-related issues. In 2020, the Company recorded bonds at fair value in the amount of \$293,665,000, compared to bonds at fair value in the amount of \$251,370,000 during 2019. There were no restricted bonds and debentures at December 31, 2020 compared to bonds and debentures including restricted fiduciary funds of \$1,239,000 as of December 31, 2019.

A security has an impairment loss when its fair value is less than its cost or amortized cost at the reporting date. The Company evaluates its securities for other-than-temporary impairment losses at each quarter end. For each impaired security, the Company determines: 1) it does not intend to sell the security and 2) it is more likely than not that the Company will not be required to sell the security before recovery of its amortized cost basis. If the Company cannot assert these conditions, it records a permanent reduction of the security's cost equal to the impairment loss. The Company also assesses whether the net present value of cash flows expected to be collected from an impaired security are less than the security's amortized cost basis. If there is a shortfall in expected cash flows, the Company recognizes a permanent reduction of the security's cost basis equal to the shortfall. The Company recognized no other-than-temporary impairment losses in 2020 and 2019.

The Company reinsures excess losses on a portfolio of mortgage insurance policies that originated between 2009 and 2020. The Company provides collateral consisting of bonds of \$67,402,000 and \$56,823,000 at December 31, 2020 and December 31, 2019, respectively.

3. UNQUOTED INVESTMENTS - N/A

4. INVESTMENT IN AND ADVANCES IN AFFILIATES - N/A

5. INVESTMENT IN MORTGAGE LOANS ON REAL ESTATE - N/A

6. POLICY LOANS - N/A

7. REAL ESTATE - N/A

8. COLLATERAL LOANS - N/A

9. INVESTMENT INCOME DUE AND ACCRUED

The Company had accrued investment income at December 31, 2020 and 2019 of \$1,614,000 and \$1,705,000, respectively.

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PART III (con't)

10. ACCOUNTS AND PREMIUMS RECEIVABLE

At December 31, 2020, the Company had amounts receivable of \$67,424,000, of which \$30,763,000 was due from affiliated companies, compared to amounts receivable at December 31, 2019 of \$58,065,000, of which \$24,346,000 was due from affiliated companies.

11. REINSURANCE BALANCES RECEIVABLE - N/A

The Company had \$28,000 of reinsurance balances receivable at December 31, 2020. The company did not have any reinsurance balances receivable at December 31, 2019.

12. FUNDS HELD BY CEDING REINSURERS

The Company has provided cash balances to affiliated ceding reinsurers as collateral against future losses incurred by the ceding reinsurers. Total funds held by ceding reinsurers at December 31, 2020 and 2019 were \$38,461,000 and \$33,067,000, respectively.

13. SUNDRY ASSETS

a. Derivative instruments

During 2004, the Company assumed a transaction whose underlying exposure is the value of a portfolio of home mortgages over a 22 year period as measured by the Halifax Price Index. The fair value of this contract is reported as a derivative asset and was \$4,826,000 and \$4,047,000 as of December 31, 2020 and December 31, 2019, respectively.

During 2016, the Company wrote a transaction whose underlying exposure is the value of an investment portfolio over a 10 year period. This transaction is reported as a derivative liability. The Company ceded 45% of this transaction to an unaffiliated entity. The ceded portion is reported as a derivative asset. At December 31, 2020, the related derivative liability and asset were \$8,470,000 and \$3,812,000, respectively, compared to \$10,700,000 and \$4,815,000 respectively, at December 31, 2019.

b. Deferred commissions - Commission costs are deferred and charged to earnings proportionate with premiums earned.

c. Airplane - During 2020, as a result of an RVI air claim, the Company took ownership of an Airbus A330 with a \$25,000,000 book value. The Company ceded approximately 41% of the transaction. The ceded portion is reported as a sundry liability. At December 31, 2020, the related sundry asset and liability were \$24,901,000 and \$10,232,000, respectively.

14. LETTERS OF CREDIT, GUARANTEES AND OTHER INSTRUMENTS

In the event that the Company is unable to pay any policyholder obligations within 30 days after the obligation becomes due, the Company has obtained a guarantee from its parent, HCC, and an additional separate guarantee from its ultimate parent, TMHD, to pay or cause to be paid such obligations.

16. UNEARNED PREMIUMS

Premiums are written on an accrual basis, net of reinsurance, and are generally included in earnings on a pro-rata basis over the lives of the related policies and the unearned portion is recognized as a liability on the balance sheet and is computed by pro-rata method. Premiums for commercial title insurance policies are recognized in earnings on the effective date of the contract.

17. LOSS AND LOSS EXPENSES PROVISIONS - See Part I, Note 4 (b)

(a) Loss and loss expenses provisions table for the years ended December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Gross loss and loss expense provisions at beginning of year	\$ 5,584,000	\$ 1,325,000
Less: Reinsurance recoverable at beginning of year	(293,000)	(238,000)
Net loss and loss expense provisions at beginning of year	<u>5,291,000</u>	<u>1,087,000</u>
Net Incurred Losses and Loss Expenses		
Current year	124,575,000	4,276,000
Prior years	(4,139,000)	(18,000)
Total net incurred losses and loss expenses	<u>120,436,000</u>	<u>4,258,000</u>
Net loss and loss expenses paid or payable related to:		
Current year	6,268,000	2,000
Prior years	18,000	52,000
Total losses and loss expense paid or payable	<u>6,286,000</u>	<u>54,000</u>
Foreign exchange and other	1,894,000	-
Net loss and loss expense provisions at end of year	121,335,000	5,291,000
Add: Reinsurance recoverable at end of year	<u>1,145,000</u>	<u>293,000</u>
Gross loss and loss expense provisions at end of year	<u>\$ 122,480,000</u>	<u>\$ 5,584,000</u>

(b) The Company had \$4,100,000 of favorable development in 2020 primarily related to a release of residual value reserves. Favorable loss development in 2019 of \$18,000 was due primarily to a release of reserves for workers' compensation claims.

During 2020, the Company increased its loss provision by \$109,738,000 to cover potential claims related to its surety and stop loss business. In addition, during 2020, the Company increased its loss provision by \$6,178,000 to cover potential claims, expenditures and commutation payments related to its residual value business. During 2019, the Company increased its IBNR by \$4,000,000 to cover potential claims, expenditures, and commutation payments related to its residual value business.

(c) At December 31, 2020 and 2019, the Company had unsecured policyholder obligations of \$122,480,000 and \$5,584,000, respectively. The Company did not have any restricted assets related to loss and loss expense provisions.

20. RESERVES FOR REPORTED CLAIMS - N/A

21. RESERVES FOR UNREPORTED CLAIMS - N/A

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PART III (con't)

22. POLICY RESERVES - LIFE - N/A

23. POLICY RESERVES ACCIDENT AND HEALTH - N/A

24. POLICYHOLDERS' FUNDS ON DEPOSIT - N/A

25. LIABILITY FOR FUTURE POLICYHOLDERS' DIVIDENDS - N/A

26. OTHER INSURANCE RESERVES - LONG TERM - N/A

27. TOTAL LONG-TERM BUSINESS INSURANCE RESERVES - N/A

28. INSURANCE AND REINSURANCE BALANCES

At December 31, 2020, the net amount payable by the Company for premiums and other balances under insurance or reinsurance contracts was \$2,977,000. At December 31, 2019, the net amount payable by the Company for premiums and other balances under insurance or reinsurance contracts was \$2,451,000.

29. COMMISSIONS, EXPENSES, FEES AND TAXES PAYABLE - N/A

At December 31, 2020, the Company had commission payable of \$10,287,000, of which, \$9,911,000 was due to an affiliated company.

30. LOANS AND NOTES PAYABLE - N/A

31. (a) INCOME TAXES PAYABLE

The Company is not subject to income tax in Bermuda. The Company has received an assurance from the Bermuda government to be exempted from all Bermuda taxes until March 31, 2035. However, the Company has elected to be treated as a U.S. domiciled company for U.S. income tax purposes. Therefore, income tax expense has been provided to record the Company's U.S. income taxes.

The Company is included in the consolidated Federal income tax return of HCC Insurance Holdings, Inc. and subsidiaries. The method of allocating taxes among the companies is subject to written agreement and approved by the Board of Directors. Under the terms of the agreement, income tax expense is allocated to companies with taxable income using a tax rate of 21%.

At December 31, 2020, the Company had a current Federal income tax receivable due from HCC Insurance Holdings, Inc. of \$12,945,000 and at December 31, 2019, had a current Federal income tax liability due to HCC Insurance Holdings, Inc. of \$1,284,000 in the consolidated balance sheet.

(b) DEFERRED INCOME TAXES

Deferred income tax is accounted for using the liability method, which reflects the tax impact of temporary differences between the bases of assets and liabilities for financial reporting purposes and such bases as measured by tax laws and regulations. The Company regularly reviews the deferred tax assets for recoverability and establishes a valuation allowance based on history of earnings, expectations for future earnings, taxable income in carryback years and the expected timing of the reversals of existing temporary differences. Due to the history of earnings, expectations for future earnings, and taxable income in carryback years, the Company expects to be able to fully realize the benefit of any net deferred tax asset, excluding amounts covered by valuation allowances, on a consolidated basis.

On December 31, 2020 and 2019, the Company had a net Federal deferred income tax liability of \$3,754,000 and \$3,274,000, respectively, primarily due to the difference in the timing of recognition of deferred policy acquisition costs, unrealized gains on investments and financial instruments, and deferred intercompany dividends offset by unearned premium revenue and discounting of loss reserves.

At December 31, 2020 and December 31, 2019, there were no valuation allowances, net operating losses or tax liabilities for unrecognized gross tax benefits related to uncertain tax positions.

32. AMOUNTS DUE TO AFFILIATES

The Company is not subject to any repayment terms, rate of interest and/or collateral for payables to affiliates. The Company is part of a consolidated group and is subject to allocation of general expenses from HCC Service Company and other affiliates.

33. ACCOUNTS PAYABLE AND ACCRUED INVESTMENT EXPENSE

The Company had \$131,000 in accounts payable and accrued investment expense at December 31, 2020 and \$38,000 at December 31, 2019.

34. FUNDS HELD UNDER REINSURANCE CONTRACTS - N/A

35. DIVIDENDS PAYABLE - N/A

36. SUNDRY LIABILITIES

During 2016, the Company wrote a transaction whose underlying exposure is the value of an investment portfolio over a 10 year period. This transaction was reported as a derivative financial instrument. See Part I, Note 4 (g).

The Company had a hold back liability to cover any losses that may occur related to a previously purchased insurance company, Indemnity and Guaranty International Reinsurance Limited (IGIRL), of \$8,220,000 and \$7,005,000 at December 31, 2020 and 2019, respectively. Also, the Company had an earnout liability related to the IGIRL purchase of \$1,863,000 and \$2,977,000 at December 31, 2020 and 2019, respectively.

See Note 13 for details on the Reinsurers' Portion of Airplane.

37. LETTERS OF CREDIT, GUARANTEES AND OTHER INSTRUMENTS - N/A

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PART VI

6. OTHER INSURANCE INCOME

The Company earned \$1,000,000 of other insurance income during 2020.

15. OTHER UNDERWRITING INCOME - N/A

32. COMBINED OTHER INCOME (DEDUCTIONS)

During 2020 and 2019, the Company recorded combined other income (deductions) consisting primarily of:

	<u>2020</u>	<u>2019</u>
Income from financing future premium on two RVI policies	\$ 2,295,000	\$ 2,029,000
Earnout expense related to IGIRL purchase	(86,000)	(124,000)
Foreign currency gain/(loss)	(1,060,000)	(3,000)
<u>Total</u>	<u>\$ 1,149,000</u>	<u>\$ 1,902,000</u>

36. COMBINED REALIZED GAINS (LOSSES)

During 2020 and 2019, the Company recorded realized gains from the sale of bonds of \$306,000 and \$812,000, respectively. During 2020 and 2019, the Company recorded unrealized gains from the change in fair value of derivatives of \$2,005,000 and \$2,162,000.