

CITADEL REINSURANCE COMPANY LIMITED

Consolidated Financial Statements
(With Independent Auditor's Report Thereon)

Years Ended December 31, 2015 and 2014



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INDEPENDENT AUDITOR'S REPORT

The Board of Directors and Shareholder of
Citadel Reinsurance Company Limited

We have audited the accompanying consolidated financial statements of Citadel Reinsurance Company Limited, which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of operations, changes in shareholder's equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 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, the auditor considers internal control relevant to the entity's preparation and fair presentation of 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. 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 consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly in all material respects, the financial position of Citadel Reinsurance Company Limited and its subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG Audit Limited

Chartered Professional Accountants
Hamilton, Bermuda
June 14, 2016

CITADEL REINSURANCE COMPANY LIMITED


Consolidated Balance Sheets

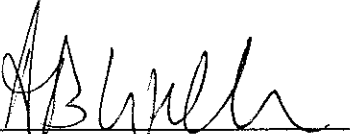
December 31, 2015 and 2014
 (Expressed in United States Dollars)

	Note	As at December 31,	
		2015	2014
ASSETS			
Marketable securities	4	\$ 32,009,772	\$ 28,390,082
Cash and cash equivalents	5	20,995,978	27,727,198
Restricted cash	5	-	77,294
Accounts receivable and accrued interest		5,746,080	3,873,267
Insurance and reinsurance balances receivable		10,974,600	9,845,273
Deposit assets	5, 6	39,459,909	50,701,171
Goodwill	7	1,633,739	1,633,739
Property, plant and equipment		614,246	523,495
Total assets		\$ 111,434,324	\$ 122,771,519
LIABILITIES			
Loss and loss adjustment expense reserves	3	\$ 28,190,093	\$ 26,248,602
Unearned premiums	8	8,743,257	5,748,430
Insurance and reinsurance balances payable		10,724,240	11,375,791
Unearned service fee		596,956	761,307
Deposit liabilities	9	39,265,761	51,884,723
Accounts payable and accruals		2,347,358	3,620,999
Total liabilities		89,867,665	99,639,852
EQUITY			
Share capital	10	20,000,000	20,000,000
Retained earnings		2,369,707	3,936,282
Equity attributable to shareholder of Citadel Reinsurance Company Limited		22,369,707	23,936,282
Non-controlling interests in subsidiaries	14	(803,048)	(804,615)
Total equity		21,566,659	23,131,667
Total equity and liabilities		\$ 111,434,324	\$ 122,771,519

See accompanying notes to consolidated financial statements

Signed on behalf of the Board

 Director

 Director

CITADEL REINSURANCE COMPANY LIMITED

Consolidated Statements of Operations

December 31, 2015 and 2014
(Expressed in United States Dollars)

	Note	For the years ended December 31,	
		2015	2014
REVENUES			
Gross premiums written		\$ 46,898,679	\$ 33,939,490
Premiums ceded		(27,382,934)	(21,684,697)
Net premiums written		19,515,745	12,254,793
Change in net unearned premiums		(1,785,680)	5,857,636
Net premiums earned		17,730,065	18,112,429
Net investment income		1,394,173	1,518,592
Net realized and unrealized losses on investments		(302,244)	(317,960)
Other income		4,116,062	4,118,638
Total revenues		<u>22,938,056</u>	<u>23,431,699</u>
EXPENSES			
Loss and loss adjustment expenses		17,205,724	13,257,997
Acquisition costs		(1,022,431)	2,007,751
General and administrative expenses		8,868,424	9,948,169
Amortization of goodwill		-	10,217
Net foreign exchange losses		295,972	233,558
Total expenses		<u>25,347,689</u>	<u>25,457,692</u>
Loss before income tax credit		(2,409,633)	(2,025,993)
Income tax credit	13	(844,625)	(926,144)
Net Loss		<u>(1,565,008)</u>	<u>(1,099,849)</u>
Profit (loss) attributable to non-controlling interest		1,567	(52,745)
Net loss attributable to shareholder of Citadel Reinsurance Company Limited		<u>\$ (1,566,575)</u>	<u>\$ (1,047,104)</u>

See accompanying notes to consolidated financial statements

CITADEL REINSURANCE COMPANY LIMITED

Consolidated Statements of Changes in Shareholder's Equity

December 31, 2015 and 2014
(Expressed in United States Dollars)

	Shareholder's Equity			
	Total equity	Retained earnings	Share capital (Note 10)	Non-controlling interest in subsidiaries (Note 14)
Balance at December 31, 2013	\$ 24,231,516	\$ 4,983,386	\$ 20,000,000	\$ (751,870)
Net Loss	(1,099,849)	(1,047,104)	--	(52,745)
Balance at December 31, 2014	<u>23,131,667</u>	<u>3,936,282</u>	<u>20,000,000</u>	<u>(804,615)</u>
Net Income	(1,565,008)	(1,566,575)	--	1,567
Balance at December 31, 2015	<u>\$ 21,566,659</u>	<u>\$ 2,369,707</u>	<u>\$ 20,000,000</u>	<u>\$ (803,048)</u>

See accompanying notes to consolidated financial statements

CITADEL REINSURANCE COMPANY LIMITED

Consolidated Statements of Cash Flows

December 31, 2015 and 2014
(Expressed in United States Dollars)

	For the years ended December 31,	
	2015	2014
Cash flows from operating activities:		
Net Loss	\$ (1,565,008)	\$ (1,099,849)
Adjustments for:		
Net realized and unrealized losses on investments	302,244	317,960
Net unrealized foreign exchange losses	242,459	218,321
Depreciation expense	120,682	99,800
Loss on disposal of property, plant and equipment	33,394	-
Amortization of goodwill	-	10,217
Changes in assets and liabilities:		
Accounts receivable and accrued interest	(1,872,813)	(730,830)
Insurance and reinsurance balances receivable	(1,129,327)	(2,846,672)
Deposit assets	11,241,262	6,552,365
Deferred acquisition costs	-	3,240,714
Loss and loss adjustment expense reserves	1,941,491	8,428,176
Unearned premiums	2,994,827	(7,322,583)
Insurance and reinsurance balances payable	(651,551)	5,956,180
Unearned service fee	(164,351)	(419,331)
Deposit liabilities	(12,618,962)	(6,259,427)
Accounts payable and accruals	(1,273,641)	(1,874,731)
Net cash (used in) provided by operating activities	(2,399,294)	4,270,310
Cash flows from investing activities:		
Proceeds on disposal of marketable securities	18,956,212	11,558,266
Purchases of marketable securities	(23,120,605)	(17,330,694)
Purchases of property, plant and equipment	(244,827)	(408,238)
Change in restricted cash	77,294	5,862
Net cash used in investing activities	(4,331,926)	(6,174,804)
Decrease in cash and cash equivalents	(6,731,220)	(1,904,494)
Cash and cash equivalents - beginning of year	27,727,198	29,631,692
Cash and cash equivalents - end of year	\$ 20,995,978	\$ 27,727,198

See accompanying notes to consolidated financial statements

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014

(Expressed in United States Dollars)

1. NATURE OF BUSINESS

Citadel Reinsurance Company Limited (the "Company"), which underwrites insurance and reinsurance, was incorporated under the laws of Bermuda on January 4, 1984 and is registered as a Class 3A insurer under The Insurance Act 1978, amendments thereto and related regulations ("The Act"). The Company is managed and has its principal place of business in Bermuda. The Company's ultimate parent company is Sirius International Limited, a company incorporated in Bermuda.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

These consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of financial statements in accordance with generally accepted accounting principles, requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the balance sheet date. Estimates also affect the reported amounts of income and expenses for the reporting period. Actual results could differ from those estimates. The Company's principal estimates relate to the development or determination of the following:

- the valuation of investments and determination of hierarchical inputs used to measure fair value of investments;
- outstanding loss and loss expenses;
- premium revenue recognition;
- acquisition accounting.

Consolidation

These financial statements include the operations of the Company and its wholly-owned subsidiaries, (collectively, the 'Group') namely Citadel International Reinsurance Company Limited ("CIRCL"), Citadel Risk Services UK Limited, Citadel Group Representatives, Inc, Citadel Risk Management, Inc, ("CRMI"), Citadel Risk Services, Inc. ("CRS"), American Millennium Insurance Company ("AMIC") and Green Park (US) Incorporated.

CIRCL is a segregated account company, incorporated in Bermuda. There are eight segregated cells (2014 – seven) within CIRCL, three of which have been consolidated into these financial statements on the basis that the Company owns 100% of the preferred shares in two of the cells and 65% of the preferred shares in the other. The remaining 35% of the latter cell's income is recognised as a minority interest. To the extent the cell has a deficiency in excess of its share capital the full amount of the deficiency is consolidated into these financial statements. To the extent that the cell's retained earnings exceed its share capital the non-controlling 35% interest is accrued on the balance sheet.

The Company and CRS jointly own 81.21% (2014 - 73.35%) of Great Falls Holding Company ("GFH"), a company incorporated in Delaware, U.S.A. GFH has a wholly owned subsidiary, Great Falls Insurance Company ("GFI"), which is engaged in the business of writing workers compensation insurance in the State of Maine, U.S.A. The operations of GFH and GFI have been consolidated in these financial statements on the basis that the Company owns 81.21% of the issued capital. The remaining 18.79% (2014 - 26.65%) is recognised as a non-controlling interest (Note 14).

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Premiums and Acquisition Costs

Written premiums comprise the premiums on insurance contracts entered into during the accounting period and are disclosed gross of commission payable to intermediaries and exclude taxes and duties levied on premiums. Premiums are recognised when receivable and are earned on either a daily or monthly pro-rata basis over the term of the related policies.

The Group assumes and cedes reinsurance in the normal course of business, with retention limits varying by line of business. Premiums on reinsurance business are recognised in the same manner as they would be if the reinsurance were considered direct business. Gains or losses on buying retroactive reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised.

The provision for unearned premiums represents that portion of the premiums written in respect of the current and prior years, which is attributable to the unexpired term of the corresponding policy in force.

Acquisition costs are comprised of ceding commissions, brokerage, premium taxes, profit commissions and other expenses that relate directly to the writing of insurance and reinsurance contracts. Acquisition costs that are incremental and directly attributable to new and renewal business that has been secured are deferred and amortized over the underlying term of the related policy.

Loss and Loss Adjustment Expense Reserves

Loss and loss adjustment expenses include all claims for losses incurred during the year, whether reported or not, related handling costs, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years. Estimates for loss and loss adjustment expense reserves are established based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claims handling costs. The estimated provisions established for the Group's reinsurance business is determined in a similar manner to direct business, and is based on reports received from the company ceding the insurance business.

Loss and loss adjustment expense provisions are derived from actuarial methods based upon known facts and interpretation of circumstances and is therefore a complex and dynamic process influenced by a large variety of factors. In establishing a provision for unpaid claims and claims expenses, management considers facts currently known, the current state of laws and litigation and current estimates of reported losses and loss expenses. Liabilities are recognized for known claims when sufficient information has been developed to indicate the involvement of a specific policy and management can reasonably estimate the Company's liability. In addition, a provision for adverse development for reported notifications and incurred but not reported claims is recorded based on the recommendations of an independent actuary using the past loss history of the Company and industry data.

Management believes that the provision for losses and loss adjustment expenses at December 31, 2015 is adequate to cover the ultimate net cost of losses incurred, however, such liability is necessarily based on estimates and no representation is made that the ultimate liability may not exceed such estimates. Subsequent revisions to estimated ultimate losses will be reflected in operations in the period in which they are determined.

Deposit Assets and Deposit Liabilities

Insurance and reinsurance contracts that principally transfer finance risk and for which no insurance risk is assumed by the Group are accounted for directly through the balance sheet. The net fees or margins earned in accordance with the terms of the contracts are recorded in the consolidated statements of operations.

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

The insurance/reinsurance assets and liabilities related to the contracts are recorded at their gross amounts in the balance sheet within Deposit assets and Deposit liabilities. The provision for claims reflected as part of the Deposit liabilities is discounted based upon the liability after taking account of the known duration of such liability, the rate of return on the matching assets and the future reductions in deferred underwriting expenses and the provision for unearned premiums.

Cash and Cash Equivalents

Cash and cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Marketable Securities

In accordance with the Financial Instruments Topic of the FASB ASC, the Company differentiates between held-to-maturity marketable securities, which are recognised at amortized cost, and held-for-trading marketable securities, which are recognised at market value with unrealised gains and losses being reported as other income in the consolidated statement of operations.

The Company may sell securities it does not own in anticipation of a decline in market value of that security. Upon entering a short position, the Company records the proceeds in cash and cash equivalents and establishes an offsetting accounts payable for the securities due under the short sale agreement, which is subsequently marked to market. The Company will generally borrow the security sold short in order to make delivery to a buyer and then replace the borrowed security by purchasing it at the market price at the time of replacement. Until the security is replaced, the Company is required to pay the lender any interest or dividend earned, which is recorded as a reduction of other income to the Company. The Company realises a gain if the security declines in price between the date of the short sale and the date on which the Company replaces the borrowed security and the Company incurs a loss as a result of the short sale if the price of the security increases. Realized and unrealized gains and losses arising from short sales of securities are included in other income. There were no short positions open at year end, and all short positions have been covered.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired by the Company. Goodwill is recorded as an asset and is not amortized.

In accordance with the Intangibles – Goodwill and Other Topic of the FASB ASC, the Company performs, at a minimum, an annual valuation of its goodwill to test for impairment or more frequently if events or changes in circumstances indicate that the carrying amount may not be recoverable. For purposes of annual impairment evaluation, goodwill is assigned to the applicable reporting unit of the acquired entities giving rise to the goodwill. Fair value is determined using widely accepted valuation techniques, such as discounted cash flows and markets multiple models. These types of analyses contain uncertainties because they require management to make assumptions and to apply judgment to estimate industry economic factors and the profitability of future business strategies. It is the Company's policy to conduct impairment testing based on the Company's current business strategy in light of present industry and economic conditions, as well as the Company's future expectations. If, as a result of the assessment, the Company determines that the value of its goodwill and intangible assets are impaired, the Company will record an impairment charge in the period in which the determination is made.

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign Currency Translation

Monetary assets and liabilities are translated into U.S. dollars at year-end exchange rates and non-monetary assets and liabilities at the exchange rates prevailing when the assets were acquired or liabilities incurred. Income and expenses are translated at the rate of exchange prevailing at the transaction date. Translation gains and losses are included in foreign exchange gains or losses unless the gain or loss is a result of trading foreign currency as part of the Company's overall investment strategy, in which case the income is recognized as other income.

Fair Value of Financial Instruments

Fair values of financial instruments are disclosed in the notes to the financial statements when they differ from the carrying values. Where amounts receivable and payable are subject to normal credit terms, their carrying values are used as an approximation of their fair values.

Fair value is defined as the price to sell an asset or transfer a liability (i.e. the "exit price") in an orderly transaction between market participants. Assets and liabilities recorded at fair value in the consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value. An asset or a liability's categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation. The hierarchy is broken down into three levels as follows:

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 products does not entail a significant degree of judgment.

Level 2 – Valuations based on quoted prices in active markets for similar assets or liabilities, quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement. These are generally company generated inputs and are not market based inputs.

The Company used the following valuation technique and assumptions in estimating the fair value of financial instruments as well as the general classification of such financial instruments pursuant to the above fair value hierarchy:

At each valuation date, the Company uses a market approach technique to estimate the fair value of our fixed maturities portfolios, when possible. This market approach includes, but is not limited to, prices obtained from third party pricing services and broker-dealers for identical or comparable securities. The pricing services use market quotations for securities that have quoted prices in active markets. When quoted market prices are unavailable, the pricing services prepare estimates of fair value measurements using observable market inputs such as yield curves, credit risks and spreads, measures of volatility, expected cash flows including prepayment speeds, reported trades and broker/dealer quotes.

A review of fair value hierarchy classifications is conducted on a quarterly basis. Changes in the observability of valuation inputs may result in a reclassification for certain financial assets and liabilities. Reclassifications between Level 1, 2 and 3 of the fair value hierarchy are reported as transfers in and/or out as of the beginning of the quarter in which the reclassifications occur.

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxation

The Company's subsidiaries that are based in Bermuda, the United States of America and the United Kingdom are subject to the tax laws of those jurisdictions and the jurisdictions in which they operate.

Income taxes have been recognized in accordance with current standards on those operations that are subject to income taxes. Deferred tax assets and liabilities result from net operating loss carryforwards and temporary differences between the carrying amounts of existing assets and liabilities recorded in the consolidated financial statements and their respective tax bases. A valuation allowance for a portion or all of deferred tax assets is recorded as a reduction to deferred tax assets if it is more likely than not that such portion or all of such deferred tax assets will not be realized.

3. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

The following table represents the activity in the loss and loss adjustment expenses for the years ended December 31, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Loss and loss adjustment expense reserves beginning of year	\$ <u>26,248,602</u>	\$ <u>17,820,426</u>
Loss and loss expenses incurred related to losses occurring in:		
Current year	10,385,964	13,147,582
Prior year	<u>6,819,760</u>	<u>110,415</u>
Total loss and loss expenses incurred	<u>17,205,724</u>	<u>13,257,997</u>
Losses and loss expenses paid related to losses occurring in:		
Current year	4,430,255	2,180,902
Prior year	<u>10,833,978</u>	<u>2,648,919</u>
Total loss and loss expenses paid	<u>15,264,233</u>	<u>4,829,821</u>
Loss and loss adjustment expense reserves	<u>\$ 28,190,093</u>	<u>\$ 26,248,602</u>

Management believes that the assumptions used establishing its provision for loss and loss adjustment expenses represent a realistic and appropriate basis for estimating those reserves as of December 31, 2015 and 2014. However, these assumptions are subject to change and the Company continually reviews and adjusts its reserve estimates taking into account all currently known information and updated assumptions related to unknown information. While management believes it has made a reasonable estimate of loss expenses occurring up to the balance sheet date, the ultimate costs of claims incurred could exceed the Company's reserves and have a materially adverse effect on its future results of operations and financial condition.

The prior year development during 2015 and 2014 was driven by underwriting of retroactive policies for which all losses incurred and paid are reported as prior year development.

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

3. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES (continued)

Gross loss and loss adjustment expense reserves and reinsurance recoverables

	<u>2015</u>	<u>2014</u>
Gross loss and loss adjustment expenses	\$ 56,139,218	\$ 45,522,278
Reinsurance recoverables	(27,949,125)	(19,273,676)
Net loss and loss adjustment expense reserves	<u>\$ 28,190,093</u>	<u>\$ 26,248,602</u>

4. MARKETABLE SECURITIES

The total fair value of held-for-trading securities and held-to-maturity securities as at December 31, 2015 was \$31,420,503 (2014 - \$28,514,245).

<u>Held for trading</u>	<u>2015</u> <u>Fair value</u>	<u>2014</u> <u>Fair value</u>
Ordinary shares	\$ 2,536,485	\$ 2,275,859
Preferred shares	2,888,228	5,548,730
Treasury funds	489,427	870,049
Property trusts	375,383	312,277
Corporate and Municipal Bonds	<u>145,343</u>	<u>1,603,103</u>
	<u>\$ 6,434,866</u>	<u>\$ 10,610,018</u>

The amortized cost, gross unrealized gains and losses and estimated fair value of held-to-maturity securities as of December 31, 2015 and 2014, are as follows:

	<u>2015</u>			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair Value
Preferred shares	\$ 6,730,870	\$ 645,531	\$ (137,138)	\$ 7,239,263
Floating notes	1,684,036	1,944	(493,659)	1,192,321
Corporate bonds	11,854,238	43,079	(608,032)	11,289,285
Treasury notes	5,305,762	4,306	(45,300)	5,264,768
	<u>\$ 25,574,906</u>	<u>\$ 694,860</u>	<u>\$ (1,284,129)</u>	<u>\$ 24,985,637</u>

	<u>2014</u>			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair Value
Preferred shares	\$ 7,864,435	\$ 561,894	\$ (58,423)	\$ 8,367,906
Floating notes	1,668,413	27,843	(460,656)	1,235,600
Corporate bonds	6,683,519	126,199	(75,945)	6,733,773
Treasury notes	1,563,697	3,848	(597)	1,566,948
	<u>\$ 17,780,064</u>	<u>\$ 719,784</u>	<u>\$ (595,621)</u>	<u>\$ 17,904,227</u>

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

4. MARKETABLE SECURITIES (continued)

The following table represents the fair value hierarchy for the Company's investments measured at fair value as at December 31, 2015:

	2015			Total
	Level 1	Level 2	Level 3	
Ordinary shares	\$ 2,536,485	\$ –	\$ –	\$ 2,536,485
Preferred shares	10,127,491	–	–	10,127,491
Floating notes	–	1,192,321	–	1,192,321
Corporate and municipal bonds	–	11,434,628	–	11,434,628
Treasury funds	5,754,195	–	–	5,754,195
Property trusts	375,383	–	–	375,383
	<u>\$ 18,793,554</u>	<u>\$12,626,949</u>	<u>\$ –</u>	<u>\$ 31,420,503</u>

The following table represents the fair value hierarchy for the Company's investments measured at fair value as at December 31, 2014:

	2014			Total
	Level 1	Level 2	Level 3	
Ordinary shares	\$ 2,275,859	\$ –	\$ –	\$ 2,275,859
Preferred shares	13,916,636	–	–	13,916,636
Floating notes	–	1,235,600	–	1,235,600
Corporate and municipal bonds	–	8,336,876	–	8,336,876
Treasury funds	2,436,997	–	–	2,436,997
Property trusts	312,277	–	–	312,277
	<u>\$ 18,941,769</u>	<u>\$ 9,572,476</u>	<u>\$ –</u>	<u>\$ 28,514,245</u>

The Company did not impair its investment in the held to maturity portfolio in 2015 or 2014. The Company considers impairment as other than temporary if evidence indicating that an investment's cost is recoverable within a reasonable period of time is outweighed by evidence to the contrary. The Company also considers its ability and intent to hold an investment until such recovery of the security's fair value. Recognition of impairment losses for declines in the value of securities attributable to issuer-specific events are based upon all relevant facts and circumstances for each investment. Factors considered by management include, but are not limited to, the impact of issuer-specific events, dividend flow, industry-specific events, current and expected future market and economic conditions, the nature of the investment, the severity and duration of the impairment and the volatility of the security's market price.

The amortized cost and estimated fair value amounts for preferred shares and corporate bonds held at December 31, 2015 and December 31, 2014 are shown by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

There were no securities transferred between Level 1, Level 2 or Level 3 during the years ended December 31, 2015 and 2014.

CITADEL REINSURANCE COMPANY LIMITED

Notes to Consolidated Financial Statements

December 31, 2015 and 2014
(Expressed in United States Dollars)

4. MARKETABLE SECURITIES (continued)

The maturity distribution for fixed maturities held as of December 31, 2015 was:

	Amortized <u>cost</u>	Estimated <u>fair value</u>
Due within one year	\$ 1,049,743	\$ 1,044,390
Due after one year through five years	6,647,877	6,421,278
Due after five years	<u>16,193,250</u>	<u>16,327,649</u>
	<u>\$ 23,890,870</u>	<u>\$ 23,793,317</u>

The maturity distribution for fixed maturities held as of December 31, 2014 was:

	Amortized <u>cost</u>	Estimated <u>fair value</u>
Due within one year	\$ 1,495,290	\$ 1,523,820
Due after one year through five years	2,801,734	2,820,299
Due after five years	<u>11,814,627</u>	<u>12,324,508</u>
	<u>\$ 16,111,651</u>	<u>\$ 16,668,627</u>

Excluded from the above table are floating rate note securities with a fair value of \$1,192,320 as of December 31, 2015 (2014 - \$1,143,727). The interest rates are reset quarterly, based on a margin over the Australian 90 day bank bill benchmark rate. Most of these securities have passed early redemption dates and can be redeemed at any time by the issuer of the securities. In such cases, this would be taken as the maturity date.

5. LETTERS OF CREDIT

The Company has pledged cash and cash equivalents of \$21,512 (2014 - \$77,294) to banks to fund fees for letters of credits and has pledged deposits reported within Deposit assets of \$8,523,049 (2014 - \$24,489,007) to banks as security for letters of credit totalling \$8,523,049 (2014 - \$24,685,224) in respect of the Company's obligations under non-risk transfer programs reported on a deposit asset and liability basis.

6. DEPOSIT ASSETS

Deposit assets represent cash, fixed deposits, marketable securities and accrued interest held to meet the Company's future obligations on non-risk transfer business.

	<u>2015</u>		<u>2014</u>	
	<u>Carrying value</u>	<u>Fair value</u>	<u>Carrying value</u>	<u>Fair value</u>
Cash	\$ 20,488,141	\$ 20,488,141	\$ 15,989,763	\$ 15,989,763
Fixed deposits	8,523,049	8,532,170	24,489,007	24,538,481
Marketable securities	10,092,566	10,092,566	10,079,563	10,079,563
Accrued interest	<u>356,153</u>	<u>356,153</u>	<u>142,838</u>	<u>142,838</u>
	<u>\$ 39,459,909</u>	<u>\$ 39,469,030</u>	<u>\$ 50,701,171</u>	<u>\$ 50,750,645</u>

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6. DEPOSIT ASSETS (continued)

The total deposit asset balance of \$39,459,909 (2014 - \$50,701,171) is fully comprised of amounts due within one year. The estimated fair value at December 31, 2015 of \$39,469,030 (2014 - \$50,750,645) represents management's best estimate using all available information to the report date.

7. GOODWILL

During the year ended December 31, 2011, the Company recorded \$1,633,739 of goodwill on the determination of the final purchase price of the acquisition of American Millennium Insurance Company. The Company has determined no impairment of this goodwill exists as of December 31, 2015 and 2014. During the year ended December 31, 2011, the Company recorded \$10,217 goodwill on the determination of the final purchase price of the acquisition of First Brokers, LLC. This company is no longer trading and the Company determined that the goodwill should be written down to \$Nil as at December 31, 2014.

8. UNEARNED PREMIUM

	<u>2015</u>	<u>2014</u>
Gross unearned premiums provision	\$ 31,457,173	\$ 17,225,869
Prepaid reinsurance premiums provision	(23,643,166)	(11,170,574)
Deferred policy acquisition costs	(4,076,411)	(3,827,256)
Deferred ceding commission income	<u>5,005,661</u>	<u>3,520,391</u>
Net unearned premium provision	<u>\$ 8,743,257</u>	<u>\$ 5,748,430</u>

9. DEPOSIT LIABILITIES

Deposit liabilities represent loss reserves due to insureds and letter of credit fees due to banks on the Company's non-risk transfer business. The total balance of \$39,265,761 (2014 - \$51,884,723) is fully comprised of amounts due in less than one year.

Included in the deposit liabilities are amounts totalling \$Nil (2014 - \$38,221,982) which are effectively recorded at their estimated net present value using discount rate of 0% (2014 - rates between 0.60% and 1.02%) which reflect the anticipated payout patterns of the losses at their ultimate expected value.

The Company's exposure under these contracts is limited to the value of the Deposit assets at any point in time.

10. SHARE CAPITAL

Share capital is comprised of the following authorized, issued and fully paid shares of the par value \$1 each:

	<u>2015</u>	<u>2014</u>
Common shares (20,000,000 shares in 2015 and 2014)	\$ <u>20,000,000</u>	\$ <u>20,000,000</u>

No dividends were declared or paid during 2015 (2014 - \$Nil).

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11. RELATED PARTY TRANSACTIONS

Included in accounts payable and accruals are advances made by affiliated companies totaling \$95,425 (2014 - \$110,655).

Included in accounts receivable and accrued interest are advances made to the parent company and affiliates totaling \$2,567,485 (2014 - \$2,132,793). The advances are non-interest bearing and repayable on demand.

12. CONTINGENCIES AND COMMITMENTS

The Company is liable on reinsurance ceded to the extent that the companies to which the business is ceded do not meet their contractual obligations. In the opinion of management, no loss to the Company is expected to arise in the future as a result of reinsurance ceded.

The investment portfolio is managed following prudent standards of diversification across counterparties, issuers, asset classes and geographical regions. Investment guidelines are designed to limit the holdings of a single issue and issuer, control non-US dollar currency exposure and minimize sovereign risk. At December 31, 2015, 76% (2014 - 79%) of the fixed and floating income portfolio at carrying value was rated investment grade.

The Company's investment guidelines permit short selling, whereby the Company sells borrowed securities which must, at some date, be repurchased and returned to the lender. The risk associated with this practice is that, if the market value of the securities sold short increases, the Company may realize losses upon repurchase at prices which may exceed that liability presented in the consolidated balance sheet. Further, in unusual circumstances, the Company may be unable to repurchase securities to close the short position, except at prices above those previously quoted in the market. There were no short positions open at year end, and all short positions have been covered.

13. TAXATION

The Company is incorporated in Bermuda, and under current Bermuda law, is not required to pay any taxes in Bermuda on either income or capital gains. The Company has received an undertaking from the Minister of Finance in Bermuda that in the event of such taxes being imposed the Company will be exempted from taxation until the year 2035. The Company is subject to withholding tax on investment income from foreign securities.

The Company's subsidiaries that are based in the United States and the United Kingdom are subject to the tax laws of those jurisdictions and the jurisdictions in which they operate.

At December 31, 2015, the Company had recorded a net tax receivable of \$40,006 within Accounts receivable and accrued interest (2014 – net tax provision of \$137,721 within Accounts payable and accruals). The Company has not recorded any interest or penalties during the years ended December 31, 2015 and 2014.

The components of income tax (credit) expense were as follows:

	<u>2015</u>	<u>2014</u>
Current tax	\$ 107,852	\$ 241,402
Deferred tax	<u>(952,477)</u>	<u>(1,167,546)</u>
	<u>\$ (844,625)</u>	<u>\$ (926,144)</u>

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13. TAXATION (continued)

Deferred income taxes reflect net operating loss carry forwards and the tax impact of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and those for income tax purposes. The significant components of the net deferred tax assets and liabilities as of December 31, 2015 and 2014 are as follows:

Total deferred tax assets net of valuation allowance

	<u>2015</u>	<u>2014</u>
Outstanding losses and loss expenses	\$ 113,045	\$ 96,751
Unearned premiums	958,232	166,343
Net operating loss carry forwards	1,207,060	1,558,807
Other	85,736	26,132
Unrealised losses (gains)	53,189	(22,378)
Total deferred tax assets	<u>2,417,262</u>	<u>1,825,655</u>
Valuation allowance	(75,640)	(576,625)
Total deferred tax assets net of valuation allowance	<u>\$ 2,341,622</u>	<u>\$ 1,249,030</u>

As of December 31, 2015, the Company has a net deferred tax asset of \$1,207,060 (2014 - \$1,558,807) generated by net operating loss carry forwards ("NOLs") of approximately \$3,550,179 (2014 - \$6,342,000) relating to NOLs in the United States expiring through to the year 2034. The assets are recognized at the relevant federal tax rates.

In light of the continued improvement in the profitability of the operations in the United States, the Company has recognized a deferred tax asset in 2015 in respect of post-acquisition NOLs. Although realization is not assured, management believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize the net balance of deferred tax assets carried forward. The total deferred tax assets net of valuation allowance are included within Accounts receivable and accrued interest.

14. NON-CONTROLLING INTEREST

In connection with the Company's co-investments in Great Falls Insurance Company, Great Falls Holding Company has issued ordinary shares to a non-controlling interest. These shares represent a 18.79% (2014 -26.65%) ownership interest in Great Falls Holding Company and the carrying value of that interest is presented in Equity.

15. STATUTORY REQUIREMENTS

Under the Bermuda Insurance Act 1978 ("The Act"), the Company is required to prepare Statutory Financial Statements and to file a Statutory Financial Return. Each year the Company is required to file with the Bermuda Monetary Authority (the "Authority") a capital and solvency return within four months of its relevant financial year end (unless specifically extended).

The prescribed form of capital and solvency return comprises the Company's Bermuda Solvency Capital Requirement ("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.

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15. STATUTORY REQUIREMENTS (continued)

As a Class 3A insurer, the Company is required to maintain available statutory capital and surplus in an amount that is equal to or exceeds the target capital levels based on enhanced capital requirements ("ECR") calculated using the BSCR model. The BSCR model is a risk-based capital model introduced by the Authority that measures risk and determines ECR and a target capital level (defined as 120% of the ECR) based on the Company's statutory financial statements. In circumstances where the Authority concludes that the Company's risk profile deviates significantly from the assumptions underlying the ECR or the Company's assessment of its management policies and practices, it may issue an order requiring that the Company adjust its ECR.

The Insurance Act mandates certain actions and filings with the Authority if the Company fails to meet and maintain its ECR or solvency margin, including the filing of a written report detailing the circumstances giving rise to the failure and the manner and time within which the insurer intends to rectify the failure. The Company is prohibited from declaring or paying a dividend if its statutory capital and surplus is less than its ECR, or if it is in breach of its solvency margin or minimum liquidity ratio, or if the declaration or payment of such dividend would cause such breach.

The Act also requires the Company to meet certain minimum capital and surplus requirements. To satisfy these requirements, the Company was required to maintain a minimum level of statutory capital and surplus of \$3,216,412 at December 31, 2015 (2014 - \$3,085,656). The Company's statutory capital and surplus was \$17,540,740 at December 31, 2015 (2014 - \$22,092,172).

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. At December 31, 2015 the Company is required to maintain relevant assets of at least \$52,259,084. At that date relevant assets are \$71,937,920 and the minimum liquidity ratio is therefore met.

All Statutory requirements were met at December 31, 2015 and 2014.

16. SUBSEQUENT EVENTS

Subsequent events have been evaluated through June 14, 2016, which is the date the financial statements were available to be issued.