Annual Report & Accounts 2014

lancashire
HOLDINGS LIMITED

Adapting to *advance*

Economies wax and wane. Markets ebb and flow. Opportunities emerge and evolve. It's the nature of our business: we adapt to advance.

The challenges of changing markets are not unique to Lancashire, but our strategies and strengths are. Our business is based upon managing the insurance cycle and adapting to our environment, so that today's challenges become tomorrow's progress.

The market has undoubtedly been challenging this year, but thanks to our foresight in 2013, when we broadened the operating base by acquiring Cathedral and setting up a permanent third-party capital management business in Kinesis, we enabled ourselves to adapt to our environment.

Despite the softening market of 2014, our Group is progressing well and has again enabled us to compete effectively in a challenging environment.

In this report

Highlights

RETURN ON EQUITY KPI

13.9%

(2013: 18.9%)

COMBINED RATIO KPI

68.7%

(2013: 70.2%)

PROFIT AFTER TAX

$229.3m

(2013: $222.5m)

DIVIDEND YIELD

17.8%

(2013: 12.3%)

TOTAL INVESTMENT RETURN KPI

1.0%

(2013: 0.3%)

TOTAL SHAREHOLDER RETURN KPI

-24.2%

(2013: 21.3%)

Visit our corporate website for more information:
http://www.lancashiregroup.com

A STRONG INVESTMENT PROPOSITION

Despite changes in market conditions, Lancashire has a consistent record of out-performance, delivering sustainable returns. Our stated goal is to provide an attractive risk-adjusted return to shareholders over the long term. We do this by maintaining an unswerving focus on underwriting and managing our capital to fit the opportunities in the market.

LANCASHIRE

Two operating companies covering the London and Bermuda markets with strong core business portfolios, recognised leadership capability and the ability to deploy capacity nimbly in a changing market across four classes.

A: Aviation: 8.5%
B: Marine: 10.9%
C: Property: 42.2%
D: Energy: 38.4%

Page 24
Read about Lancashire

CATHEDRAL

Two Syndicates in Lloyd's with mature portfolios of short-tail business in the same classes as Lancashire, but separate niches, allowing further diversification of the business and client base. Access to Lloyd's unique capital structure and world-wide licenses.

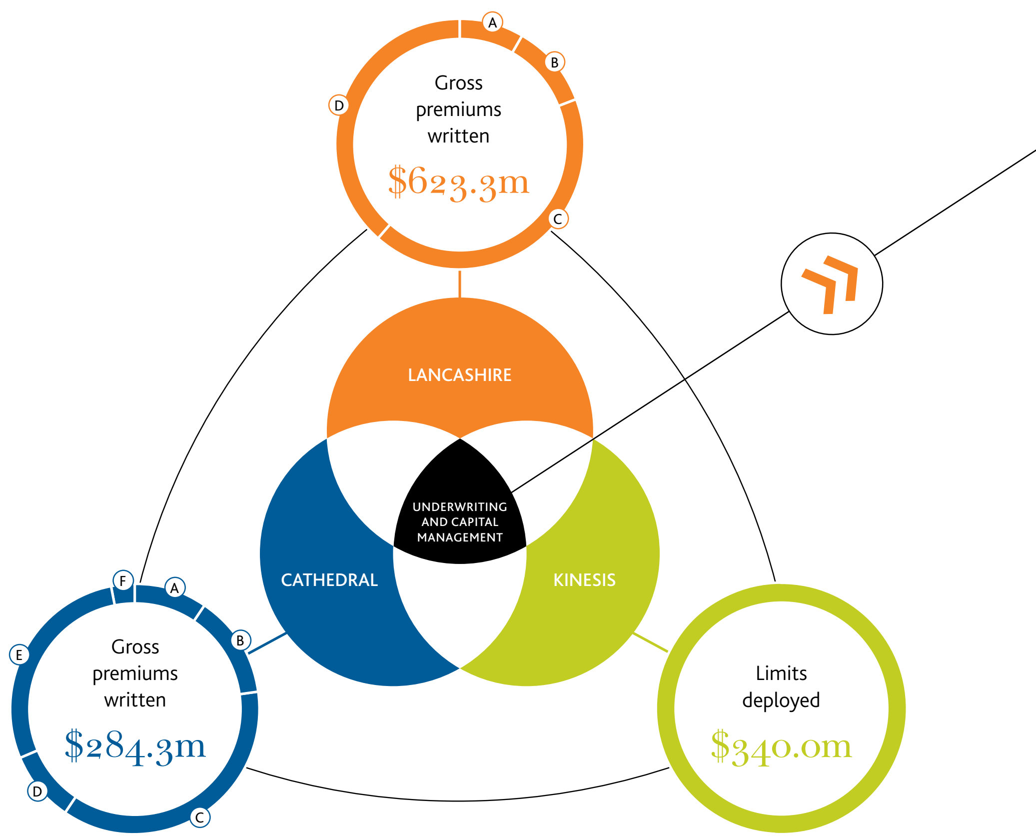
A: Aviation: 9.7%
B: Marine: 13.2%
C: Property Re: 36.7%
D: Energy: 9.1%
E. Property D&F: 28.4%
F. Other: 2.9%

Page 31
Read about Cathedral

KINESIS

A third-party capital and underwriting manager in Bermuda, leveraging Lancashire's expertise and track record to offer unique multi-class products to clients and investors, with scope to develop more products as the market evolves.

Page 32
Read about Kinesis



OPERATING HIGHLIGHTS

- The established portfolios of Lancashire Bermuda and London, and Syndicate 2010, continued to offer significant capacity and leadership expertise.
- Full year contribution from Cathedral with strong underwriting performance.
- Continued integration of Cathedral and building out of Syndicate 3010 with new terrorism, energy and aviation lines.
- Hiring of new aviation teams for Syndicate 3010.
- Kinesis advanced its operations with an expansion of its strong investor club and a blue-chip client roster.
- Continued development across all entities and the Group for compliance with Solvency II.

LANCASHIRE GROUP

Lancashire has been a top-performing specialty short-tail insurer and reinsurer since its foundation in 2005. It has successfully weathered significant tests such as Hurricane Ike and Storm Sandy, earthquakes in Japan, New Zealand and Chile, floods in Thailand and the UK, and non-elemental losses like Deepwater Horizon and Costa Concordia, as well as the financial markets shock of 2008.

Through all these events, Lancashire has consistently produced leading combined ratios and return on equity through an unremitting focus on profitable underwriting and active capital management.

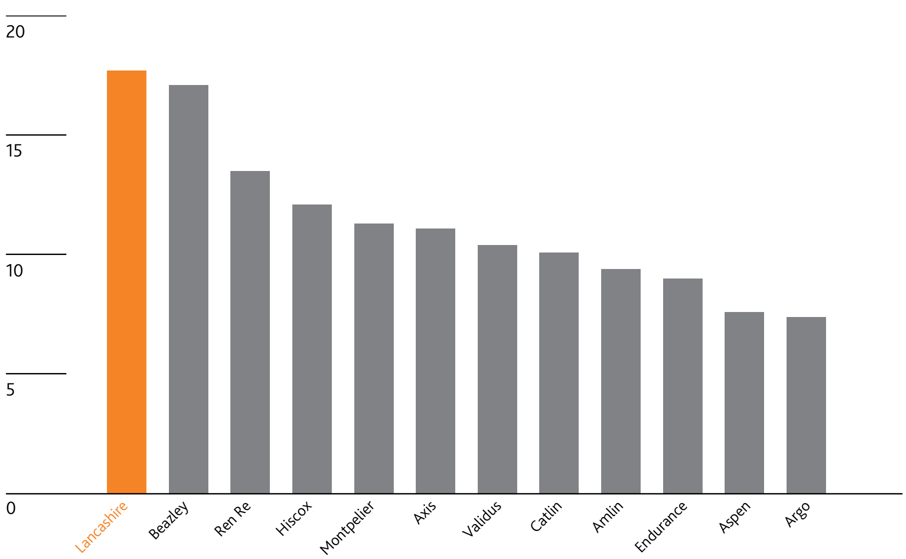
The ability to navigate hard and soft markets has been demonstrated, and our strategy has proved to be fit for purpose across all phases of the market cycle.

Performance incentives for management and staff are aligned to shareholders' interests, so Lancashire will continue to focus on maintaining profitability and optimising capital usage.

Lancashire's commitment: to focus on the drivers of profitability in the business, and to ensure that the Company provides a secure and stable counterparty for clients and brokers, whilst generating strong returns for shareholders.

FIVE YEAR COMPOUND ANNUAL ROE

17.7%



(1) Peer group as defined by the Board of Directors.

(2) RoE calculated as the internal rate of return of the change in FCBVS in the period plus dividends accrued. For Amlin, Argo, Beazley, Catlin, Hiscox and Ren Re basic book value per share is used as FCBVS is not reported by these companies. Compound annual returns for LHL and sector are from 1 January 2010 through 31 December 2014. Data source: Company records.

Lancashire's commitment: to focus on the optimum capital levels in each of its three business units to ensure the best returns for the shareholders, whilst providing meaningful capacity to clients and brokers across the cycle.

FINANCIAL HIGHLIGHTS

- Combined ratio of 68.7 per cent, yet again one of the leading combined ratios in the peer group, reflecting solid underwriting and expense control.
- Loss ratio for 2014 of 31.7 per cent, another strong performance in a year with a number of medium-sized risk and catastrophe losses.
- Gross premiums written of $907.6 million with a contribution of $284.3 million from Cathedral in its first full year as part of the Group.
- Kinesis deployment of $340.0 million of limits with capital raised on three occasions during the year.
- Investment return of 1.0 per cent reflecting emphasis on limiting risk in volatile markets.

ADAPTING TO ADVANCE

"This has been a year of evolutionary change for our Board and management team. We enter 2015 with a business which is fit to deliver our strategic priorities."

Q&A

with Non-Executive Chairman, Martin Thomas

Q | WHAT HAVE BEEN THE STRATEGIC CHALLENGES DURING 2014 AND HOW HAS THE BUSINESS ADAPTED TO THEM?

A | The Group faced the challenge of a year which was marked both by change and continuity. During April the Board had oversight of the most significant change in the management team since Lancashire's foundation in 2005. In April, the prime founder of our business, Richard Brindle, decided to retire from Lancashire. Most shareholders have been with us long enough to appreciate the high level of success the Company enjoyed under his leadership. Fortunately, he left the business in robustly good shape and with a body of staff whose skills and experience allowed for a seamless transition. Alex Maloney was appointed the Group Chief Executive Officer with effect from 30 April 2014. Alex has been with the Group since its earliest days when he joined to lead and shape its Energy underwriting strategy – one of the Group's most profitable lines of business. Since 2010, Alex has been a member of the Board and the Group's Chief Underwriting Officer. He has a detailed knowledge of the Group's business and has demonstrated a practical, hands-on approach to management and cultivated a quiet authority in his leadership of the senior management team and as a member of our Board. The appointment of Alex also saw the promotion of two other members of the management team. Paul Gregory has assumed the role of Group Chief Underwriting Officer and Hayley Johnston has become the Chief Underwriting Officer at LUK. It is a tribute to the bench strength of our team, and the work which had been put in place to ensure that a longer term strategic succession plan was implemented, that the transition to the new management team was completed so smoothly. It has given me great pleasure across the last year to see Alex grow into his new role with such assurance and discretion. He has proven himself to be the right man at the right time.

John Bishop, Neil McConachie and Ralf Oelssner also stepped down from the Board at the 2014 AGM. I would like to thank John, Neil and Richard for their contributions to the success of Lancashire over many years. It is with sadness that we mark the death of Ralf, shortly after his departure from our Board.

Q | HOW HAS THE BOARD EVOLVED DURING THE YEAR?

A | There comes a time in any organisation where "the old order changeth, yielding place to new": in my introduction to last year's Annual Report I talked about the "generational change in Board membership" to be implemented during 2014. We have been as good as our word. Both William Spiegel and Bob Spass stepped down from the Board with effect from 1 January 2015, each having completed nine years' service from the date of their first election. They have stepped down from the Board in keeping with governance good practice. William and Bob leave us with our thanks for their many years of insightful wisdom, leadership and service on our Board and its Committees. Their departure marks the passing of the baton from the original founders of our business to a new generation, and I am delighted to welcome Peter Clarke and Tom Milligan (see biographies on pages 47 and 48) to our Board who, together with our other Board members, bring an appropriate range and depth of knowledge and skills to provide support, challenge and strategic insights for the business.

Q | HAVE THE 2014 RESULTS MET EXPECTATIONS?

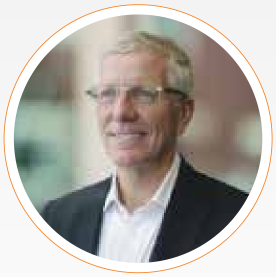
A | Insurance is a cyclical business and surplus underwriting capacity has meant that results for all our peers in the sector have been subdued. Lancashire delivered a solid performance during 2014, when the strategic priorities were to maintain a core book of business and to focus on the fundamentals of good underwriting. RoE for 2014, was 13.9 per cent. 2014 was the first full year for the inclusion of the Cathedral platform and the Group's move into Lloyd's has expanded the premium base for the Group as a whole and has performed in line with expectations. The combined ratio of 68.7 per cent is an excellent result, although slightly above our recent five year average. This is in part a reflection of the softer market in pricing and coverage terms and Cathedral's higher attritional loss ratio. Another bright spot for 2014 was the rapid establishment and recognition of the Kinesis underwriting platform. Kinesis has now completed its first full year cycle and has made progress in establishing relations with both investors and reinsured clients which we expect will help position it well to expand if and when improved underwriting conditions should arrive.

Q | HAS THE GROUP'S CAPITAL MANAGEMENT STRATEGY CHANGED IN 2014?

A | As a business Lancashire has always tailored its capital requirements to its underwriting and business strategy and effective capital management remains at the heart of that strategy. At what is considered to be a low point in the insurance cycle, the Board was pleased to declare ordinary and special dividends in respect of 2014 amounting in total to $1.85 per common share (see page 79 for further details). This equated to a return of $381.2 million, more than the Group's profit after tax for the year of $229.3 million.

Once again I would like to thank our shareholders for affording the Company flexibility in its capital management capabilities. At the AGM held on 30 April 2014 we asked for and received shareholder support to issue up to 15 per cent of shares on a non pre-emptive basis. In an insurance market that rewards the fastest to react, following a market moving loss event, those who can deploy capital quickly, so as to play a leading role in establishing an adjusted pricing regime and meeting brokers' and clients' needs for immediate capacity, will have the advantage. The first movers make the new market. For this reason a nimble capital management strategy remains at the heart of Lancashire's business model and the Company is seeking shareholder support for a similar resolution at the 2015 AGM.

NEW TALENT ADDED TO THE BOARD



We welcome Peter Clarke (left) and Tom Milligan (right) as new members of our Board

Page 47
Read about our Board of Directors

Q | HOW HAS THE GOVERNANCE OF THE BUSINESS EVOLVED DURING 2014?

A | In the 2012 Annual Report I stated that the business placed great importance on good governance, not for its own sake, but because when it is done well it can enhance the effective oversight of the Group and the accomplishment of its strategic objectives. This last year has illustrated the importance of the work carried out by the Board and the management of the Group in ensuring a smooth transition to a new Group CEO and management regime. A fuller account of our governance arrangements and the work of the Board and its Committees can be found at page 44.

Q | WHAT IS THE OUTLOOK FOR 2015?

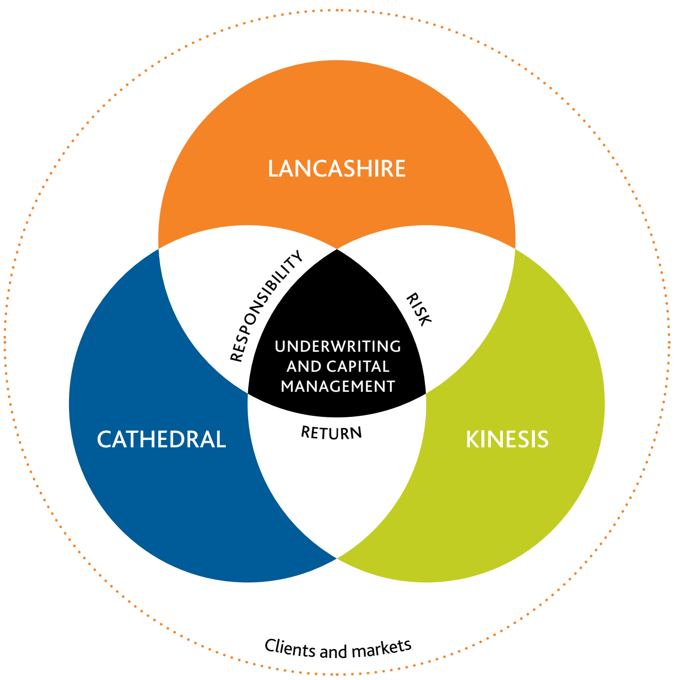
A | 2015 will see the 10th anniversary of the foundation of the Company. Although market conditions are likely to remain challenging the Board expects to see the Group maintain its core book of business across all of our current classes and to see progress in the build-out of Syndicate 3010 and Kinesis.

I would like to thank all employees for the hard work performed in 2014, which has positioned us well to meet the challenges of 2015.

MARTIN THOMAS
NON-EXECUTIVE CHAIRMAN

THREE PLATFORMS, ONE ETHOS

We leverage top-tier underwriting expertise with efficient management of capital and resources across three balance sheet options to provide our clients and brokers with excellent solutions for their insurance and reinsurance needs. We always focus on the risk-adjusted return.



OUR RESPONSIBILITY

We recognise that our responsibility as a company and as individuals reaches wider than our shareholders and our clients. We strive to be a good employer, a good corporate citizen and a responsible preserver of resources. Through our Foundation, we make concrete financial contributions and provide human support to a number of causes in the places we operate and around the world (for further details see pages 38 to 41).

Visit our corporate website for more information: http://www.lancashiregroup.com

Key Strengths

LANCASHIRE

- Strong brand with clients and brokers. Recognised for significant capacity and strong leadership ability in well-defined business sectors
- Proven track record of supplying capacity across the cycle with sector-leading profitable results
- Excellent culture of co-operation with collegiate underwriting, risk selection, multi-disciplinary business review and cross-selling to clients
- Strong record of capital management actions to right-size capital and navigate market cycles
- Experienced and cohesive management team with proven ability

CATHEDRAL

- Strong brand with core clients and brokers recognised for very long-term consistency of relationships and leadership
- Efficient Lloyd's capital model allowing greater premium leverage than for rated companies
- Worldwide licensing maintained by Lloyd's allows Cathedral to write business worldwide with limited regulatory overhead
- Use of world's oldest insurance third-party capital – the Names – who pay underwriting fees, costs and profit commission
- Experienced management team that built the business together over 14 years with a great track record

KINESIS

- Ability to leverage Lancashire data, relationships and reputation with investors and clients
- Experienced management with strong relationships amongst clients, brokers and investors
- Highly specialised multi-class product with strong barriers to entry in terms of data and modeling expertise
- Ability to raise capital very quickly, as demonstrated in 2014, to respond to market dislocation

Goals	Risk	Return
• Maintain key client, broker and reinsurer relationships to ensure continued flow of business and maintenance of capabilities • Continue to improve use of reinsurance and retrocession to uphold risk-adjusted balance in softening markets • Retain "underwriting comes first" culture and discipline without being tempted into innovation or diversification for its own sake	• Continued influx of new capacity from naïve or inexperienced capital and development of broker facilities without proper underwriting controls • Depressed oil price leading to weakening demand for key energy products • Widening terms and conditions being accepted by the markets without adequate pricing or exclusions • Failure to attain Solvency II equivalence by Bermuda to allow smooth continuation of quota share arrangements for the Group	**5 YEAR COMPOUND ROE** 17.7% *Page 24 to 30* To find out more information
• Maintain core portfolios in Syndicate 2010 in climate of increased competition • Develop new lines including energy, terrorism, aviation war and general aviation in Syndicate 3010 and continue to look for new opportunities for bolt on business lines • Leverage Lancashire's balance sheet and cross sell where opportunities arise	• Pressure on signings and participation given relatively small line sizes counterbalanced by strength of broker and client relationships • Expanded burden of regulatory oversight or overlapping regulation from Lloyd's, PRA and FCA	**COMBINED RATIO** 85.1% *Page 31* To find out more information
• Ensure product is correctly calibrated to meet client need in terms of responding to events and capital relief • Deliver returns in line with expectations for modeled ranges given market losses and pricing • Increase investor club members • Increase limits deployed	• Increased competition from traditional and collateralised markets, being displaced from property retrocession, with attempts to replicate the Kinesis product • Waning of investor interest in insurance allocations if interest rates begin to increase and yield returns to capital markets • Client resistance to complex products, given cheap availability of traditional products	**LIMITS DEPLOYED** $340.0m *Page 32* To find out more information

Economies wax & wane

but here at Lancashire, our core strategic focus on underwriting comes first, effectively balancing risk and return and operating nimbly through the cycle, ensuring that we have the right strategy to fit the different micro- and macro-economic conditions.

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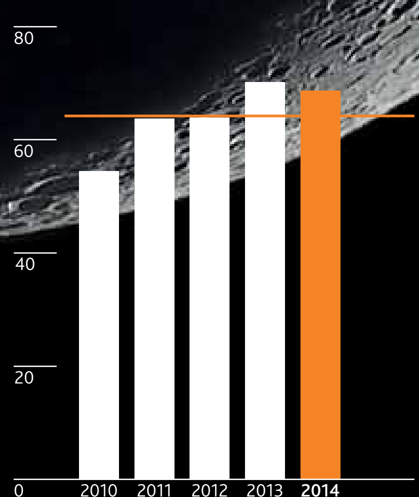
COMBINED RATIO

As a Company that focuses on underwriting and underwriting profitability, the combined ratio is a key performance indicator. Over time, there is a strong correlation between combined ratio and the growth in fully converted book value plus dividends. So combined ratio is a good metric to monitor the underlying health of our portfolio.

68.7%



5 Year average

64.2%

Q&A

with Group Chief Executive Officer, Alex Maloney

WE HAVE NOT CHANGED FUNDAMENTALLY…

we've simply adapted to today's market

In 2013, we laid the foundations to make Lancashire a more durable cross-cycle vehicle; and in 2014, we have executed by adapting our business to a soft market and continuing our capital management discipline.

COMBINED RATIO

68.7%

LOSS RATIO

31.7%

RETURN ON EQUITY

13.9%

Q | HOW WOULD YOU SUM UP THE MARKET IN 2014?

A | In some ways 2014 has seen significant changes at Lancashire, but if you look at what we've done it has actually been a case of applying our business philosophy to the world in which we find ourselves. From the beginning, Lancashire, as a group, has emphasised the need to be nimble. And what that means is making sure our resources, our structures and our people are fit for all possible market scenarios. We then engage in a constant process of challenging our assumptions and fine-tuning our tactics, but our strategy and our goals remain the same.

The key element driving our market at present is capital. Although we have seen some significant risk losses, we haven't seen any devastating catastrophe losses in the last two years. Without the galvanising effect of capital-eroding losses, many insurers have been building capital through retained earnings. As always, this leads to attempts to build market share or enter new business lines. That is a cyclical change and one that has been well understood, and well managed by Lancashire during its history.

But in addition to this cyclical change we are now seeing a secular change, which is the decision by capital markets to treat insurance risk as an investable asset class like any other. We can debate how much of the allocation by some participants reflects a permanent decision versus a short-term reaction to a prolonged period of low interest rates. But in our judgement, if we're seeing the current levels of capital coming in to a soft market, we expect there to be plenty more capital ready for a post-loss market. At present most of the capital markets' money is being attracted to catastrophe risk, where the use of industry-standard stochastic models like RMS and AIR allows investors to see a scientifically-based projected range of outcomes. Again, we can debate how accurate those modeled outcomes are, but investors are used to this method of assessing a return.

> *"I have a clear vision of how I want Lancashire to develop and continue to advance."*

Q | HOW HAS LANCASHIRE ADAPTED TO CHANGES IN THE MARKET IN 2014?

A | We have to adapt on two levels; at a cyclical level and at a secular level.

At the cyclical level, Lancashire has long shown its ability to maintain discipline in softening markets. And we are reacting nimbly by taking advantage of some attractive catastrophe and risk reinsurance pricing to buy more coverage and reduce our retentions, both at Lancashire UK and Bermuda and at Cathedral. This allows us to focus on the risk-adjusted return for our business, weighing the retained net risk against the retained net premium. But we recognise that more reinsurance cannot always be the answer to declining pricing or broadening terms and conditions. So we are prepared to walk away from business if it is no longer economic. The low attritional component of our loss ratio means that Lancashire is less susceptible to pricing pressures than some of our peers, and our consistently strong combined ratio, including 68.7 per cent in the calendar year 2014, bears this out.

At a secular level, Lancashire is executing on the strategic plans laid in 2013. We recognised the need for Lancashire to develop a broader business base and to get closer to its clients, to maintain its "relevance" in a more competitive market with more options for the insurance and reinsurance buyer. We've done this in several ways, but a good example is the development of more capacity for our energy and terrorism clients through building out these lines of business at Syndicate 3010. By cross-selling from both our rated-paper and Lloyd's capital bases, we are able to offer our clients and brokers significant capacity. Similarly, we have continued to build out our excess energy liability product with key clients to enhance our client offering, whilst remaining within our area of expertise. Within Syndicate 3010, we have added market-leading teams for Aviation War and General Aviation, with encouraging early support. Again, these niche lines broaden our base whilst remaining within classes we already know.

Q | HOW IS THE WIDER GROUP INTEGRATION PROGRESSING?

A | We continue to work on optimising the integration of Cathedral on the underwriting side, with cross-selling and, for example, leveraging the expertise of Mark Wilson of Cathedral as a reinsurance buyer, working for the whole Group. So Cathedral is meeting our expectations, and not just in a financial sense. And at Kinesis we've seen solid development of the client and investor base, as Kinesis has leveraged the Lancashire risk expertise and data to create highly specialised products. The take up, in terms of both investors and limits sold, has met our expectations for 2014; and subject to market conditions, we will build on this in 2015.

On the investment side 2014 has seen continuing short-term volatility in markets, and an expectation that the low interest rate environment may start to turn in 2015. Lancashire has always felt its first task on the asset side is to protect the liquidity required for our clients and to preserve the balance sheet to be able to engage in market opportunities when they arise. As such we focus on trying to stay market neutral in the current environment, and given our heavy weighting to short duration fixed income instruments to match our liabilities, we have increased our allocation to certain risk assets in 2014 to mitigate some of our interest rate risk. We currently have more of a risk-on bias and this is likely to continue for the immediate future.

Q | HOW ARE YOU ADAPTING TO YOUR NEW ROLE AS CEO?

A | I took on the role of Group CEO in 2014 after more than nine years with Lancashire. I'd like to pay tribute to Richard Brindle who handed the reins on to me following the 2014 AGM, and who created a company with a keen understanding of its role and a real depth of management talent. It's a great help to me to have people like Elaine Whelan and Paul Gregory, who have been with Lancashire since the early days, Peter Scales and John Hamblin who started Cathedral and Darren Redhead who is building Kinesis. They all have many years of experience, and know how to weather all phases of the cycle.

I have a clear vision of how I want Lancashire to develop, and continue to advance. This encompasses continued focus on underwriting profitability as the engine of our success, combined with adherence to right-sizing capital on the most efficient balance sheet for the opportunities in front of us. We cannot control the market, no (re)insurer can, but we can ensure that we are the most nimble at reacting to, and preparing for, it.

Paul Gregory,
Group Chief Underwriting Officer
Chief Executive Officer, LUK

Elaine Whelan,
Group Chief Financial Officer
Chief Executive Officer, LICL

Peter Scales,
Chief Executive Officer, Cathedral

Darren Redhead,
Chief Executive Officer, Kinesis

As such I will continue to focus on the combined ratio as a measure both of our underwriting success and our control of overheads, and on the RoE as a yardstick of both our profitability and right-sizing of capital. During my time with Lancashire I have seen us become a key partner to our clients and brokers – to whom we are very thankful – and deliver market leading returns to our shareholders. We have achieved this on the back of great people, great structures and systems and great focus on the fundamentals. We all at Lancashire UK and Bermuda, Cathedral and Kinesis and at the Group level, intend to build on this for the future by continuing to adapt, but not forsaking our principles.

"Lancashire was established with a clear strategy that recognises the cyclical nature of the insurance and reinsurance markets and enshrines underwriting and capital discipline at the heart of our strategic approach to our business."

Q | HOW HAS THE STRATEGY DELIVERED IN 2014?

A | We can see the Lancashire strategy in action right across the Group in 2014. To take a key example, we can look at how Lancashire deploys property reinsurance capacity across the Group. In 2013, Lancashire wrote most of its catastrophe exposures through LICL, writing both property retrocession and property catastrophe excess of loss, and used the Accordion and the Saltire sidecars to distribute risk it had underwritten to third-party capital. In 2014, with the additions of Cathedral and Kinesis, and the availability of additional outwards retrocession, the shape of the Group's property reinsurance portfolio has undergone significant change.

The amount of property retrocession written has been significantly reduced from $80.8 million in 2013 to $18.1 million in 2014. This reflects Lancashire's judgement that as the most commoditised product we sell, and with a secular change from the commitment of third-party capital to this space, that the risk-adjusted return was declining steeply. We have maintained core relationships in property retrocession in LICL, but with much less capital allocated than in previous years. Instead LICL has continued to develop its previously underweight property catastrophe excess of loss book. Cathedral's own property catastrophe excess of loss portfolio of small U.S. regional business, which is very stable due to the buying habits of the clients, now forms 23.3 per cent of the Group's property reinsurance income. In addition, on the non-U.S. side, LICL has been able to cross-sell its larger capacity on higher layers with Cathedral, who have a more mature portfolio of smaller capacity on lower layers.

At the same time Kinesis has leveraged Lancashire's expertise in risk lines and modeling to sell retrocession products to address a real need for multi-class protection, including property, that affords excellent balance sheet relief to clients. So Lancashire's reinsurance profile has adapted to the cycle, protecting and developing a strong core portfolio, by using multiple balance sheets to match the client's needs. As we look forward, we can see additional opportunities to increase the amount of retrocession cover that we buy to protect these exposures, again strategically using the cyclical glut of capacity to optimise risk-adjusted returns.

That additional flexibility on our outwards reinsurance and retrocession purchases has helped in our capital management for 2014 and beyond. Whilst we originally planned on making a single special dividend payment in December 2014 to right-size capital for 2015, we actually made some very capital-efficient changes to our outwards programmes using both reinstatements and quota share capacity. These have allowed us to make a further special distribution with the final dividend for 2014, whilst maintaining our prudent surplus capital position which will allow us to take advantage of any opportunities.

Q | SO DESPITE THE SOFT MARKET THE STRATEGY IS UNCHANGED?

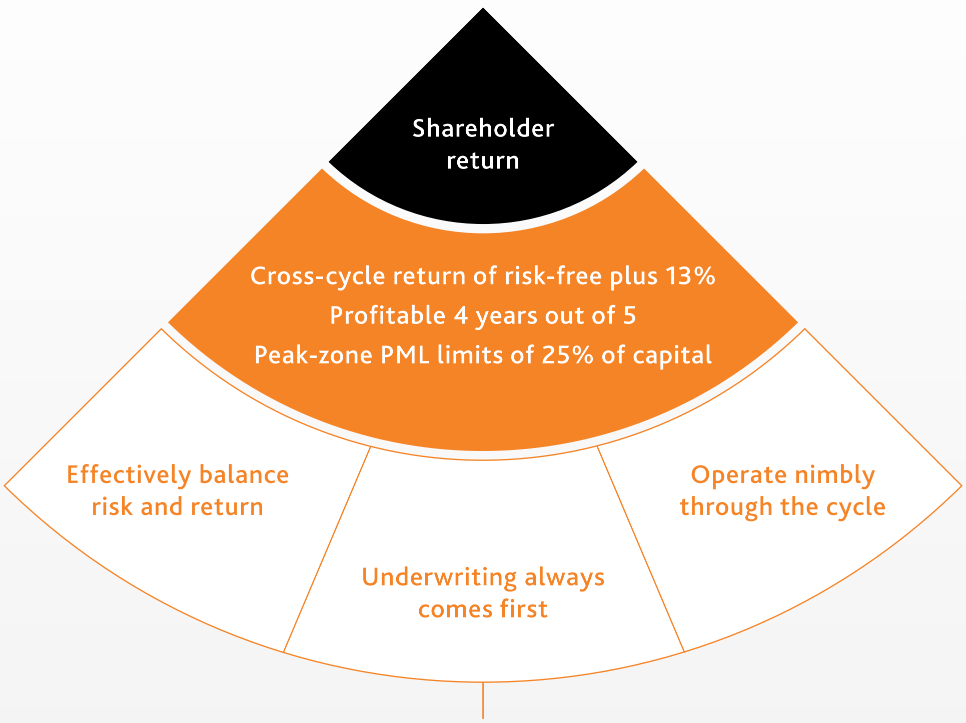
A | The original Lancashire strategy was specifically designed to be durable across the cycle, so there is no need for a strategic change. The whole point of having a lean operating structure, with exposures concentrated in short-tail markets, is to be able to right-size our underwriting and capital to the market in front of us. We added Kinesis and Cathedral to the Lancashire Group to improve our ability to trade across the cycle with both core and opportunistic portfolios.

ALEX MALONEY
CHIEF EXECUTIVE OFFICER

CONSISTENCY IN STRATEGIC DIRECTION

Our strategy

We have three strategic aims that enable us to meet our goal of providing an attractive risk-adjusted return to our shareholders. We put underwriting at the forefront of all we do, we focus on getting the right balance between risk and return and we ensure that we can react nimbly to an ever-changing market. This enables us to serve our clients and brokers with significant capacity across the cycle, not just in the core business we aim to renew every year, but also in times or in areas where capacity is scarce: the opportunistic part of our portfolio. We keep our structure lean and overheads under strict control so that we can refocus our resources quickly. And we test our assumptions and performance constantly through our structure using daily underwriting calls or exception reporting to management, a fortnightly Risk and Return Committee meeting with all disciplines within the Group represented, and a series of supporting underwriting, operational, compliance, investment and finance committees. Around this our risk function and internal audit supply challenge and assurance to management and the Boards through a simple and continuous reporting process.



OUR CULTURE – THE BEDROCK OF OUR STRATEGY

Lancashire encourages a culture of co-operation and respect based on open challenge. This can be seen clearly in the LICL and LUK daily underwriting call where senior and junior underwriters debate the risks they want to write and their fit to the portfolio and market. It also characterises the Group-wide Risk and Return Committee which brings together underwriting, actuarial, finance and investments, operations and risk to challenge the assumptions used in all areas of our planning and measuring the business.

Description

UNDERWRITING ALWAYS COMES FIRST

We employ 33 underwriters across the Group, many of them with decades of experience, and supply them with analytical tools to assess which business best fits our portfolios. We look for new opportunities that will improve our overall returns and ensure that we remain relevant to our brokers and clients.

EFFECTIVELY BALANCE RISK AND RETURN

By bringing together all our disciplines – underwriting, actuarial, modeling, finance, investment, risk and operational – at our fortnightly RRC meetings, we are able to look at how different parts of our operations are working together. We stress test our business plans and gauge where we can be most effective without undue volatility.

OPERATE NIMBLY THROUGH THE CYCLE

As capital continues to surge into the (re)insurance market, the need to be nimble is more important than ever. This means being ready to deploy capital quickly when it is needed, and having the discipline to return it when it is not.

Achievements in 2014

Performance

Associated strategic risks

We have added energy and terrorism lines to our Lloyd's offering in Syndicate 3010, expanding the Group's capacity, licensing and balance sheet options for these classes. We have also added new Aviation classes with two new teams for Syndicate 3010, both with long experience and good track records. We have built out Kinesis deploying $340.0 million of limits with seven investors.

Combined Ratio KPI

68.7%

Still a leading combined ratio, even in difficult markets, evidencing the continued focus on underwriting and portfolio construction.

Gross premiums written

$907.6m

Significant contribution from Cathedral in 2014 as we focused on protecting our core portfolios, but maintained the discipline to decline or re-structure our participation on under-priced or poorly performing business.

The key risk in the current market phase is the loss of relevance to brokers and clients; with so much surplus capacity insurers need to have a unique selling point. For Lancashire that is found in its mixture of capacity, leadership capability, significant reinsurance expenditure and multiple balance sheet options. New business lines and additional reinsurance purchases help us in this respect.

We have had to reduce income in some areas of our business in response to market weakening. But we have been able to find substantial outwards reinsurance opportunities that allow us to mitigate some of the effects of price reductions, and reduce our net exposures until the time is right for us to retain more risk.

Return on Equity KPI

13.9%

A solid result despite a difficult market and the incidence of risk losses, helped by our improved outwards reinsurance programme.

Probable Maximum Loss

$235.2m*

We continued to reduce our exposure to key catastrophe perils as the market has become more competitive, demonstrating our discipline and nimbleness.

* 1 in 100 year Gulf of Mexico Hurricane expected net loss at 1 January 2015.

The key issue is for Lancashire to continue to serve its clients and brokers with significant capacity, whilst ensuring that the portfolio is not unbalanced. This means constantly re-assessing our business mix, and testing key risk assumptions.

Kinesis demonstrated its speed in identifying an opportunity outside its usual bi-annual capital raising and then deploying $37.5 million of limits within one week. In addition, Lancashire renewed its 15 per cent disapplication of pre-emption rights to smooth potential future capital raises.

Percentage of profit returned to shareholders KPI

152.3%

Lancashire continues to exercise the discipline of giving back capital it cannot profitably deploy, but remains open to new opportunities such as those in developing Syndicate 3010.

Page 20
KPIs

Dividend Yield

17.8%

Whilst buying back shares can be a part of right-sizing capital, special dividends allow Lancashire to make substantial capital returns quickly when justified.

Lancashire has developed an expectation among its stakeholders that it will produce a consistent return and pay ordinary and special dividends. Lancashire has to ensure that all stakeholders understand that in hard markets Lancashire will want to retain and even raise capital to take full advantage of underwriting opportunities.

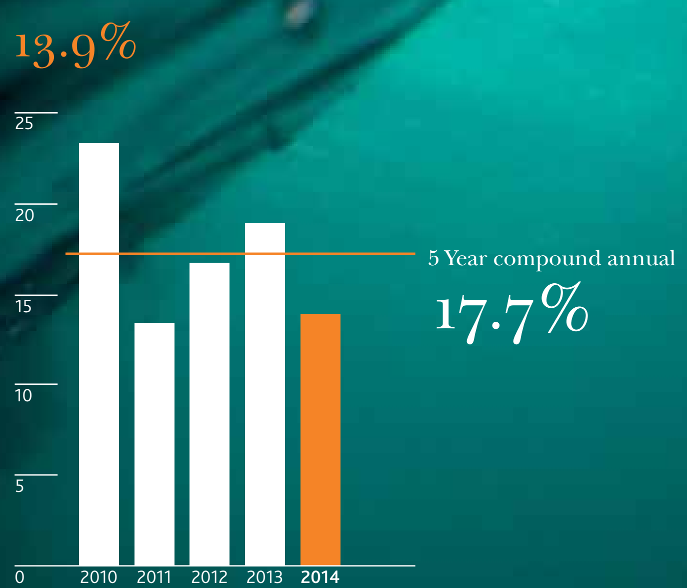
Page 33
Enterprise Risk Management

Markets *ebb & flow*

but here at Lancashire, we remain nimble so as to respond to challenges whilst maintaining a strong balance sheet. Being agile to seize upon opportunities as they arise is a cornerstone of our business.

RETURN ON EQUITY

We set a cross-cycle target for return on equity because we recognise that in a cyclical market the returns we earn can be impacted by available capacity, premium rating and losses amongst other factors. So even though the cycle is currently depressed, we expect to meet our targets over time.



MAINTAINING STRONG FINANCIALS

"Despite a challenging market, Lancashire has remained committed to doing what we've always said we'd do: we have continued to demonstrate both discipline in our underwriting and an unrelenting focus on capital management in order to produce the best risk-adjusted return we can for our shareholders."

Q&A

with Group Chief Financial Officer, Elaine Whelan

Q | HOW WOULD YOU SUM UP 2014 GROUP FINANCIAL PERFORMANCE?

A | In a year where there has been much doom and gloom in discussions around market conditions, it's not all bad. Lancashire produced an RoE of 13.9 per cent and a combined ratio of 68.7 per cent for the year. With our first full year of incorporating Cathedral into our results, they added 1.6 per cent to our RoE, after acquisition adjustments. While there were no major loss events impacting the industry, we did see an increased frequency of attritional losses. To put that in context, our loss ratio for the year was 31.7 per cent. We produced a profit after tax of $229.3 million and comprehensive income of $227.2 million. Our inception-to-date compound annual RoE is 18.9 per cent.

Q | HOW HAS THE SOFT MARKET AFFECTED PREMIUMS AND WHAT HAS CATHEDRAL'S CONTRIBUTION BEEN?

A | Our gross premiums written were $907.6 million, an increase of $227.9 million or 33.5 per cent compared to 2013. The increase in premiums is derived primarily from the new Lloyd's segment following the acquisition of Cathedral in the fourth quarter of 2013. Cathedral contributed $284.3 million of premiums for the year. Otherwise, in the original Lancashire lines of business, we saw a further reduction in property retrocession as terms and conditions and pricing continued to worsen. This was offset to a degree by redeploying capital to the property catastrophe excess of loss book, including some business on a multi-year basis. We also wrote a number of new and renewing multi-year deals in the energy Gulf of Mexico book.

Q | WITH NO MAJOR LOSSES IN 2014 WHAT EFFECT HAS THIS HAD ON LANCASHIRE'S LOSS RATIO?

A | The Group's loss ratio for the year was 31.7 per cent with an accident year ratio of 35.9 per cent. As noted above, there were no major insured loss events this year, although we did see a higher number of smaller losses. The most notable impact was in Lancashire's satellite book and Cathedral's aviation book with a total of $42.4 million reported across a number of losses. Prior year losses developed favourably, albeit modestly so.

Q | HOW HAS THE EVOLVING INVESTMENT MARKET AFFECTED LANCASHIRE?

A | We produced a total return for the year of 1.0 per cent. Investment markets remained challenging – although somewhat less so than in 2013 – with global growth still slow and geopolitical risk heightened. We increased duration during the year, increased our allocation to floating rate securities and added a small hedge fund portfolio. While that helped us generate a better return on our portfolio, the additional asset allocations were primarily with a view to managing our interest rate exposure in anticipation of Federal Reserve rate increases in 2015. The hedge fund portfolio has returned 1.8 per cent since our initial investment in April 2014.

2014 FINANCIAL PERFORMANCE

FINANCIAL HIGHLIGHTS

	2010 $m	2011 $m	2012 $m	2013 $m	**2014 $m**
Gross premiums written	689.1	632.3	724.3	679.7	**907.6**
Net premiums written	649.9	565.1	576.1	557.6	**742.8**
Net premiums earned	614.2	574.5	582.6	568.1	**715.6**
Net insurance losses	165.7	182.3	174.1	188.1	**226.5**
Net underwriting income	342.2	208.8	289.1	254.2	**335.7**
Net investment income	53.4	43.2	32.5	25.4	**28.6**
Net realised gains (losses) and impairments	33.2	8.6	11.8	12.6	**(5.9)**
Net operating profit	306.5	219.0	220.3	184.2	**231.9**
Profit after tax	330.8	212.2	234.9	222.5	**229.3**
Change in net unrealised gains/losses on investments	(2.2)	(10.6)	17.8	(32.5)	**(2.1)**
Comprehensive income	328.6	201.6	252.7	190.0	**227.2**
Dividends	294.2	180.4	201.4	325.6	**321.0**
Diluted earnings per share	$1.86	$1.20	$1.29	$1.17	**$1.16**
Diluted operating earnings per share	$1.73	$1.23	$1.21	$0.97	**$1.17**
Fully converted book value per share	$7.57	$7.62	$7.83	$7.50	**$6.96**
Return on equity	23.3%	13.4%	16.7%	18.9%	**13.9%**
Net loss ratio	27.0%	31.7%	29.9%	33.1%	**31.7%**
Net acquisition cost ratio	17.3%	19.6%	20.5%	22.1%	**21.4%**
Expense ratio	10.1%	12.4%	13.5%	15.0%	**15.6%**
Combined ratio	54.4%	63.7%	63.9%	70.2%	**68.7%**
Accident year loss ratio	42.9%	59.3%	34.6%	36.1%	**35.9%**
Net total return on investments[1]	4.2%	1.8%	3.1%	0.3%	**1.0%**

Note: Dividends included in the financial statement year in which they were recorded.

(1) Net return on investments includes internal foreign exchange hedges.

Q | HOW HAS KCML FINANCIALLY CONTRIBUTED TO 2014 RESULTS?

A | We earned $6.2 million in underwriting fees for the year against an expense base of approximately $4.6 million. We also recorded a $4.7 million share of profits in associates on our 10 per cent equity interest in KHL. During 2014 we received $9.7 million in total profit commissions on previous vehicles and we should receive $5.8 million in profit commission from the Kinesis vehicle in the first quarter of 2015.

Q | WHAT IS THE VALUE OF WARRANTS EXERCISED AND REMAINING AT YEAR END?

A | Warrant exercises during the year reduced RoE by 0.8 per cent. With 18.7 million warrants remaining outstanding at the end of the year, and due to expire on 16 December 2015, we anticipate the imminent exercise of these outstanding instruments.

Q | HOW HAS CAPITAL BEEN MANAGED IN 2014?

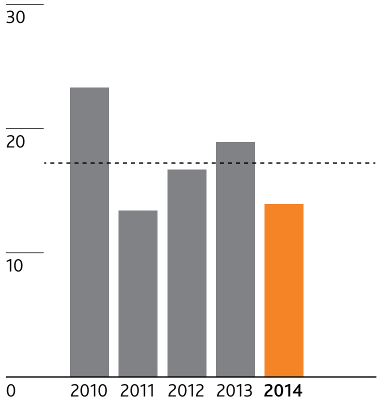
A | During the year we returned $346.0 million of capital, or 152.3 per cent of comprehensive income, by way of dividends and share repurchases paid in the year. Including dividends declared on 11 February 2015, our capital return from inception now stands at $2.3 billion. Our total capital at the end of the year was $1.4 billion. As ever, we will adjust our capital position to match business opportunities and to generate a superior risk-adjusted return for our shareholders.

ELAINE WHELAN
GROUP CHIEF FINANCIAL OFFICER

RETURN ON EQUITY

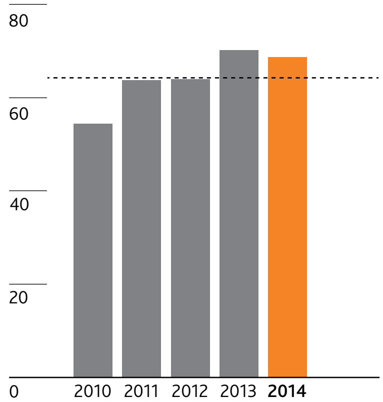
13.9%

$ DR



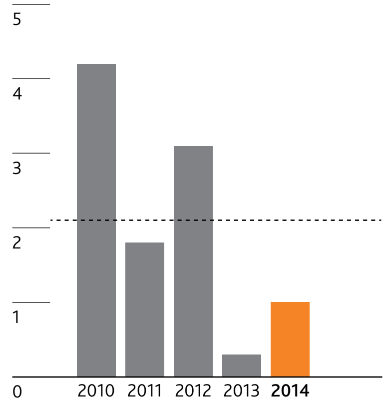
COMBINED RATIO

68.7%



TOTAL INVESTMENT RETURN

1.0%



	Return on Equity	Combined Ratio	Total Investment Return
Aim	The Group's aim is to provide shareholders with a risk-adjusted return on equity of 13 per cent in excess of a risk-free rate over the insurance cycle.	The Group aims to price its business to ensure that the combined ratio in any year is less than 100 per cent.	The Group's primary investment objectives are to preserve capital and provide adequate liquidity to support the Group's payment of claims and other obligations.
Measurement	The return on equity is measured by management as the internal rate of return of the increase in fully converted book value per share in the period, adjusted for dividends.	The combined ratio is the ratio of total costs to total net earned premium and is a measure of an insurance company's operating performance. It is calculated as the sum of the loss ratio, the acquisition cost ratio and the expense ratio.	Total investment return measures investment income and net realised and unrealised gains and losses produced by the Group's managed investment portfolio.
2014 Performance	Our market in 2014 was almost universally in a soft phase. We recognise that whilst we have attained very high RoE in the recent past, at this stage of the cycle we cannot expect to earn such high returns. But we continue to focus on getting the best risk-adjusted return for our shareholders. In 2014 this led us to buy more reinsurance and retrocession protection to reduce our exposures.	Whilst the combined ratio in 2014 was above the five-year average, it was still an excellent result. In the context of a softening market we would expect the loss ratio to increase and have increased our attritional loss ratio to take account of this and Cathedral's more frequency-oriented portfolio.	In 2014 Lancashire continued to monitor risk-on/risk-off volatility and increased the allocation to risk assets as a hedge against the interest rate risk inherent in the significant fixed-income portfolio. However, given the liquidity and duration needs of the portfolio, the composition of the core portfolio is unchanged.
Risk Management	The stated aim is a long-term goal, acknowledging that management expects both higher and lower results in the shorter term. The cyclicality and volatility of the insurance market is expected to be the largest driver of this pattern. We seek to align our variable remuneration to shareholders interest by having an RoE component in this.	The Group's underwriters assess likely losses, using tools such as BLAST and BAM and catastrophe models, and their experience and knowledge of past loss experience, industry trends and current circumstances. This allows them to estimate the premiums sufficient to meet likely losses and expenses. Peer reviews of risks are conducted through the daily underwriting call or peer review, depending on risk impact, enabling the Group to ensure careful risk selection, limits on concentration and appropriate portfolio diversification. The RRC then monitors performance at a portfolio level.	The investment strategy places an emphasis on the preservation of invested assets and provision of sufficient liquidity for the prompt payment of claims, in conjunction with providing a reasonably stable income stream. These objectives are reflected in the Group's investment guidelines and its conservative asset allocation. Management reviews the composition, duration and asset allocation of the investment portfolio on a regular basis in order to respond to changes in interest rates and other market conditions.

TOTAL SHAREHOLDER RETURN

-24.2%

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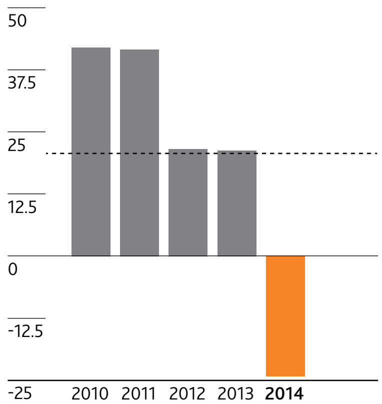


The Group's aim is to provide an attractive risk-adjusted return to shareholders over the insurance cycle. This is a long-term goal, recognising that the cyclicality and volatility of both the insurance market and the financial markets in general will impact management's ability to maximise the share multiple in the immediate term.

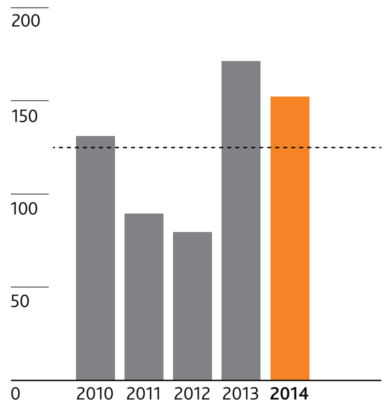
Total shareholder return is measured in terms of the internal rate of return of the increase/decrease in share price in the period, measured in U.S. dollars and adjusted for dividends.

The performance of the share price in 2014 was disappointing, but we continue to communicate regularly and transparently to our investors, and to tell the Lancashire story around the world. The combination of change, including the acquisition of Cathedral and a new CEO, a difficult market, and Lancashire's previous history of out performance meant that it was a challenging year for the share price.

The Lancashire remuneration structure and share scheme ensure that staff are highly motivated and closely aligned to the Group's goals, and therefore with shareholders. Permanent staff are eligible to receive RSS awards for which TSR is an element of the vesting criteria. The participation of employees in the RSS ensures that there is a strong focus on sustainable long-term shareholder value.

PERCENTAGE OF PROFIT RETURNED TO SHAREHOLDERS

152.3%



The Group aims to carry the right level of capital to match attractive underwriting opportunities, utilising an optimal mix of capital tools. Over time, through pro-active and flexible capital management across the cycle, we aim to generate optimum returns for shareholders.

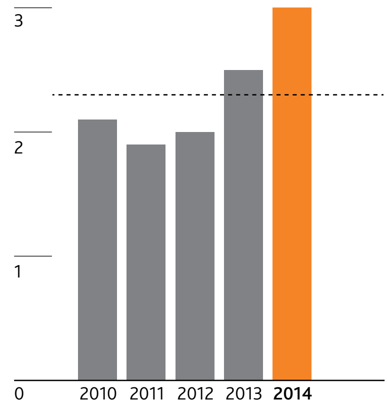
The percentage of profit returned to shareholders equals the total capital returned to shareholders through dividends and share repurchases paid in a given year, divided by the Group's comprehensive income.

In 2014, Lancashire maintained it's A rating. In view of the current market outlook Lancashire took the decision to return surplus capital to shareholders due to the lack of opportunities which met internal hurdles. With significant and long-term new market capital to support our reinsurance needs, we were able to improve the capital efficiency on our outwards purchases.

Risk tolerances are set at a level that aim to prevent the Group incurring losses that would impair its ability to operate. The Group's key capital measure is it's A.M. Best rating, and a minimum rating of A- is considered necessary to attract business.

DONATIONS MADE TO THE LANCASHIRE FOUNDATION

$3.0m



The Lancashire Foundation was established in 2007 with the aim of creating a charitable trust for the benefit of charitable causes in Bermuda, the UK and worldwide.

Money is donated by the Group to the Lancashire Foundation through an annual cash donation and by dividends on Lancashire warrants that were donated to the Foundation on its inception.

Charities supported in 2014 include charities proposed by staff and by clients and brokers. Over 40 charities in total were supported financially in Bermuda, the UK and around the world. All staff had the opportunity to take part in volunteering days.

The Lancashire Foundation is a charity registered in England and Wales (registration number 1149184). The charity's trustees are Group employees and non-executive Board members. The day-to-day operations are administered by a Foundation Donations Committee made up of employees from across the Group which operates within the specific criteria set for the Foundation's charitable giving.

5 Year Average

$ DR

KPI linked to Executive Directors' remuneration. For more information see pages 61 to 78.

STRONG PERFORMANCE IN TOUGH MARKETS

John Hamblin
Active Underwriter,
Cathedral Syndicates 2010 and 3010

Sylvain Perrier
Chief Underwriting Officer, LICL

Bruce Carman, Hayley Johnston, John Spence
Aviation War, AV52 and General Aviation

Simon King
Direct and Facultative Property

Q&A

A roundtable discussion on the state of the market with the Group's underwriters

Q | THERE HAS BEEN A LOT OF DISCUSSION ABOUT NEW CAPACITY IN THE MARKET. HOW DOES THAT AFFECT YOUR LINE OF BUSINESS?

A | J Hamblin: For our part at Syndicate 2010, our core U.S. catastrophe book is made up of some 300 small to mid-size companies who have almost completely shunned the capital markets to date, mostly because of the basis risk which still exists between capital fund offerings and the underlying risks our customer base writes. A combination of the relatively small reinsurance premiums on offer with the conservatism of our customer base has seen less than 2 per cent of deals being completed with new markets to date with no change in their overall buying habits.

A | S Perrier: At LICL, the property reinsurance portfolio has seen a significant decline in retrocession business and this does directly reflect the introduction of new capital with a hunger for the commoditised, model-dependent part of the market. But as John indicates, the traditional market has a superior product in many respects, with features like reinstatements which are very difficult for the capital markets sector to reproduce.

A | J Flude: For much of the remainder of the Group's business it isn't the direct impact of new capital that is being felt, as capital markets cannot satisfactorily rate or underwrite our products in the absence of a model. Rather it is surplus capital and retained earnings in the traditional sector, resulting from benign loss experience and the displacement effect of new capital in catastrophe reinsurance, that is driving competition. But again, we're used to competition and we have a very experienced group of underwriters to navigate all kinds of markets.

Q | SO HOW IMPORTANT ARE RELATIONSHIPS IN A SOFTENING MARKET?

A | J Hamblin: Both Cathedral's U.S. and international books are made up of strong relationships which have lasted decades during which time we've been tested by softer markets than this one. As in most years, we are seeing some organic growth from within our existing client base which will, to some extent, offset lower pricing. But client retention on our book is strong.

A | J Flude: For the Energy and Marine portfolios, we have strong relationships based on our clients' need to have insurance counterparties who understand their exposures and operations in detail. We can provide bespoke coverage for unique exposures such as ultra-deep-water units, and we always aim to adjust claims fairly and quickly,

Simon Thurgood, Mark Wilson
Terror and Property Reinsurance

James Flude, Alasdair Butler
Energy & Cargo

even when they are complex. We've been very pleased by the support those clients have shown by giving orders to both LUK and the new energy capacity in Syndicate 3010.

A | A Butler: In Marine Cargo, Cathedral's emphasis has always been to concentrate on our core accounts. We have been working with many of our clients for up to 25 years, and offer them cover right around the world. These clients are more immune to the fickle rate-chasing that can be seen elsewhere and we consider them to be the foundation on which we can build in more favourable market conditions.

Q | ARE THERE OPPORTUNITIES EVEN IN A SOFT MARKET TO DEVELOP THE BUSINESS?

A | B Carman: There are always opportunities, and the development of the Aviation accounts at Syndicate 3010 in 2014 are a good illustration of this. John Spence and I were able to bring teams with both a track record and experience to Cathedral, and we've already seen the support of brokers and clients.

A | J Spence: Even in General Aviation, which has not been affected by the headline losses, we have been able to lay firm foundations for the account, based on our long experience and relationships in the market.

A | S Thurgood: Lancashire has been able to build out its terrorism and energy lines in Syndicate 3010 as well, often with additional lines on existing Group business thanks to the support of our clients and brokers.

Q | SO HOW CAN YOU UNDERWRITE YOUR WAY THROUGH THIS PHASE OF THE CYCLE?

A | M Wilson: For a start it's important to have the experience to know what to look for. Changes to terms and conditions, like expanding the number of hours in which flood losses can accumulate, can have significant potential impacts on profit margin, depending on the region and attachment point. If you understand these impacts, you can assess whether there is a viable price for the coverage, or whether you need to exclude it.

A | H Johnston: To be fair, the softening of the reinsurance market can actually be a benefit for a Group like ours where around 70 per cent of our income is direct insurance. We're able to buy more and cheaper reinsurance to protect our primary portfolios, and that means we can limit exposure and volatility. As Alex has said, we aim to retain the most risk when markets are hardest, and the least when they are softest, so finding the right balance for the stage of the cycle is key.

A | S King: We can also look at the balance of our business mix. For 2015, the Cathedral D&F portfolio will be about 45 per cent binder business, the small commercial business written through MGAs, which is much less susceptible to violent rate swings. That's the highest that it has ever been. And as Hayley says, we've been able to reduce our retentions by buying more reinsurance at better prices.

SOLID PERFORMANCE

Hayley Johnston
Chief Underwriting Officer, LUK

Sylvain Perrier
Chief Underwriting Officer, LICL

In a difficult year for underwriting, Lancashire still achieved a combined ratio of 68.7 per cent.

BUSINESS ENVIRONMENT AND OUTLOOK

2014 has been a challenging year for the specialty insurance market as we are firmly in the soft phase of the underwriting cycle. But managing the cycle is one of the key skills of the Lancashire Group. As a long-standing leader in the specialty insurance and reinsurance lines, the silver lining of the highly competitive market is the ability for Lancashire to maintain its core inwards portfolio while managing net exposures through greatly improved pricing, and terms and conditions on the outward placements.

The market is not without challenges, but the Lancashire business model was always designed in the knowledge that we have to cater for all phases of the cycle. Solid return on equity and an excellent combined ratio have been achieved in difficult trading conditions and allowed us to maintain our excellent dividend record, based on our continued commitment to focusing first on our underwriting and our capital management. With market-leading underwriters across all three of our business platforms we have defended our core portfolio, built our lines where we had true growth opportunities, reduced exposures where competition made returns unacceptable, and maintained our relevance to brokers and clients. The work we have done over the last couple of years in widening the base of our income, and adding to our underwriting resources, reinforces our ability to trade successfully through all conditions.

RENEWAL PRICE INDEX (RPI)

Lancashire's RPI is an internal methodology that management uses to track trends in premium rates on a portfolio of insurance and reinsurance contracts. The RPI is calculated on a per contract basis and reflects Lancashire's assessment of relative changes in price, terms, conditions and limits on like-for-like renewals only, and is weighted by premium volume. The RPI does not include new business and only covers business written by LICL and LUK, to offer a consistent basis for analysis. The calculation involves a degree of judgement in relation to comparability of contracts and the assessment noted above. To enhance the RPI tool, the management of Lancashire may revise the methodology and assumptions underlying the RPI, so the trends in premium rates reflected in the RPI may not be comparable over time. Consideration is only given to renewals of a comparable nature so it does not reflect every contract in Lancashire's portfolio. The future profitability of the portfolio of contracts within the RPI is dependent upon many factors besides the trends in premium rates.

The following table summarises the RPI figures for the main business classes, excluding the Lloyd's segment, using 2006 as the base year:

RPI

Class	2006	2007	2008	2009	2010	2011	2012	2013	**2014**
Aviation (AV52)	100	80	69	68	62	59	55	49	**44**
Gulf of Mexico offshore energy	100	80	64	137	139	140	140	136	**125**
Worldwide offshore energy	100	80	68	84	88	97	100	97	**91**
Marine	100	88	80	82	80	79	86	89	**91**
Property retrocession and reinsurance	100	97	86	127	121	131	157	152	**132**
Terrorism	100	86	71	66	60	57	55	52	**48**
Combined	100	86	76	83	81	83	84	81	**76**

UNDERWRITING RESULTS

	2014						2013					
	Property $m	**Energy $m**	**Marine $m**	**Aviation $m**	**Lloyd's $m**	**Total $m**	Property $m	Energy $m	Marine $m	Aviation $m	Lloyd's $m	Total $m
Gross premiums written	**263.0**	**239.4**	**67.7**	**53.2**	**284.3**	**907.6**	333.4	209.9	63.0	48.9	24.5	679.7
Net premiums earned	**221.5**	**169.7**	**57.7**	**52.6**	**214.1**	**715.6**	218.8	203.1	61.7	44.7	39.8	568.1
Net loss ratio	**9.8%**	**24.7%**	**47.8%**	**62.5%**	**47.9%**	**31.7%**	13.8%	26.5%	105.3%	44.7%	47.7%	33.1%
Net acquisition cost ratio	**11.8%**	**30.9%**	**30.7%**	**18.3%**	**22.2%**	**21.4%**	13.4%	27.7%	34.8%	22.6%	21.6%	22.1%
Expense ratio	**–**	**–**	**–**	**–**	**–**	**15.6%**	–	–	–	–	–	15.0%
Combined ratio	**21.6%**	**55.6%**	**78.5%**	**80.8%**	**70.1%**	**68.7%**	27.2%	54.2%	140.1%	67.3%	69.3%	70.2%

PREMIUMS

Gross premiums written increased by 33.5 per cent compared to 2013. The increase in premiums is derived primarily from the new Lloyd's segment following the acquisition of Cathedral in the fourth quarter of 2013. The Group's five principal segments, and the key market factors impacting them, are discussed below.

PROPERTY

Property gross premiums written decreased by 21.1 per cent for the year ended 31 December 2014 compared to the year ended 31 December 2013. The decrease is driven primarily by reductions in the property retrocession book at the 1 January 2014 renewals, offset in part by the expansion of our property catastrophe excess of loss book. As property retrocession rates, terms and conditions continued to worsen, we redeployed capital to property catastrophe excess of loss, adding some new business and restructuring some existing programmes for core clients, including writing some business on a multi-year basis. Otherwise we saw a reduction in both the terrorism and political and sovereign risks books due to the impact of timing from long-term contract renewals.

ENERGY

Energy gross premiums written increased by 14.1 per cent for the year ended 31 December 2014 compared to the year ended 31 December 2013. The increase for the year is driven primarily by the Gulf of Mexico book where a number of both new and renewing deals were written on a multi-year basis. Volumes across other energy lines are fairly flat year on year.

MARINE

Marine gross premiums written increased by 7.5 per cent for the year ended 31 December 2014 compared to the year ended 31 December 2013. The increase is largely due to non-annual contract renewals in the marine hull sub-class in the second quarter of 2014.

AVIATION

Aviation gross premiums written increased by 8.8 per cent for the year ended 31 December 2014 compared to the year ended 31 December 2013 driven by increases in the aviation satellite sub-classes, due to new satellite business plus additional satellite launches on contracts written in previous years.

LLOYD'S

2014 reflects the first full year of gross premiums written attributable to the Lloyd's segment since the Cathedral acquisition in the fourth quarter of 2013. Two months of gross premiums written, from the date of acquisition, were included in the fourth quarter of 2013. The Lloyd's segment gross premiums written for the year ended 31 December 2014 were $284.3 million, $3.9 million or 1.4 per cent lower than the year ended 31 December 2013 (including premiums written prior to the acquisition). For the year ended 31 December 2014, while there have been decreases across the existing book of business due to declining rates, these have been offset by the new energy, terrorism and aviation classes being written by Syndicate 3010.

CEDED

Ceded premiums increased by $42.7 million, or 35.0 per cent for the year ended 31 December 2014 compared to the year ended 31 December 2013. The overall increase for the year is predominantly due to the new Lloyd's segment. Cessions to the Accordion sidecar were $47.9 million in 2013. The Accordion quota share contract was commuted in the first quarter of 2014 and, other than standard premium adjustments, no premiums were ceded to the facility this year. This reduction was more than offset by $64.9 million of ceded premiums in relation to the Lloyd's segment. Lancashire also took advantage of lower reinsurance rates to purchase some new non-marine retrocession aggregate cover and to restructure and increase limits for the marine, energy and terror programmes.

EARNED

Net premiums earned as a proportion of net premiums written were 96.3 per cent for the year ended 31 December 2014, compared to 101.9 per cent for the year ended 31 December 2013. The decreased percentage in premiums earned for the year ended 31 December 2014 compared to the same period in 2013 reflects the impact of increased multi-year premiums written in the property catastrophe and energy Gulf of Mexico classes in 2014.

LOSSES

The Group's net loss ratio was 31.7 per cent for the year ended 31 December 2014 compared to 33.1 per cent for 2013. For the year ended 31 December 2014, there were relatively low reported losses across all lines, although there was some negative development on prior accident year mid-sized marine and energy claims. In 2013, attritional losses were exceptionally low, offset by prior year adverse development on the Costa Concordia marine loss of $37.9 million, after reinsurance and reinstatement premiums.

Prior year favourable development was $34.4 million for the year ended 31 December 2014, compared to $15.9 million for the same period in 2013, which included the adverse development on Costa Concordia above. Both years otherwise experienced releases due to lower than expected reported losses.

The 2014 accident year loss ratio, including the impact of foreign exchange revaluations, was 35.9 per cent compared to 36.1 per cent for the year ended 31 December 2013. The 2014 accident year loss ratio for the year ended 31 December 2014 did not include any significant large losses. The corresponding period of 2013 also included low levels of current accident year losses.

The following tables show the impact of prior year development and large losses on the Group's loss ratio:

FOR THE YEAR ENDED 31 DECEMBER 2014

	Losses $m	**Loss ratio %**
At 31 December 2014	**226.5**	**31.7**
Absent prior year development	**260.9**	**36.5**
Adjusted losses and ratio	**260.9**	**36.5**

Note: Adjusted loss ratio excludes large losses and prior year development. The table does not sum to a total due to the impact of reinstatement premiums.

FOR THE YEAR ENDED 31 DECEMBER 2013

	Losses $m	Loss ratio %
At 31 December 2013	188.1	33.1
Absent Europe hail and flood	167.2	29.4
Absent Costa Concordia	154.6	27.0
Absent remaining prior year development	237.5	41.8
Adjusted losses and ratio	183.1	32.0

Note: Adjusted loss ratio excludes large losses and prior year development. The table does not sum to a total due to the impact of reinstatement premiums.

The table below provides further detail of the prior year's loss development by class, excluding the impact of foreign exchange revaluations:

LOSS DEVELOPMENT BY CLASS

	2010 $m	2011 $m	2012 $m	2013 $m	**2014 $m**
Property	28.8	63.5	(36.0)	13.2	**19.8**
Energy	47.6	57.3	37.4	18.4	**5.4**
Marine	17.7	28.6	25.9	(23.4)	**(9.7)**
Aviation	6.0	5.9	0.1	(1.4)	**0.9**
Lloyd's	n/a	n/a	n/a	9.1	**18.0**
Total	100.1	155.3	27.4	15.9	**34.4**

Note: Positive numbers denote favourable development.

ACCIDENT YEAR LOSS RATIOS

	2010	2011	2012	2013	**2014**
Accident year loss ratio	28.1%	56.5%	31.2%	32.7%	**35.9%**
Initial accident year loss ratio	42.9%	59.3%	34.6%	36.1%	**n/a**
Change in loss ratio post-accident year	14.8%	2.8%	3.4%	3.4%	**n/a**

Note: Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2014.

Excluding the impact of foreign exchange revaluations, previous accident years' ultimate losses developed as follows during 2014 and 2013:

ULTIMATE LOSS DEVELOPMENT BY ACCIDENT YEAR

	2013 $m	2014 $m
2006 and prior accident years	(0.7)	**1.8**
2007 accident year	(0.9)	**(0.3)**
2008 accident year	(4.1)	**3.6**
2009 accident year	2.0	**4.3**
2010 accident year	1.4	**5.7**
2011 accident year	(4.1)	**(6.1)**
2012 accident year	22.3	**11.1**
2013 accident year	n/a	**14.3**
Total	15.9	**34.4**

Note: Positive numbers denote favourable development.

The ratio of IBNR to total net loss reserves was 31.6 per cent at 31 December 2014 compared to 31.8 per cent at 31 December 2013.

ACQUISITION COSTS

The accident acquisition cost ratio was 21.4 per cent compared to 22.1 per cent for the 12 months to 31 December 2013. The decrease was largely due to profit commission received on Accordion (see page 32).

INVESTMENTS, LIQUIDITY AND CASH FLOW

Since inception, the primary objectives for our investment portfolio have been capital preservation and liquidity. Those objectives remain unchanged, and are more important than ever in today's volatile and reactive markets. As market volatility continues, we position our portfolio to limit downside risk in market shocks. In 2014, our focus has been on managing our interest rate risk, the largest risk to our predominantly fixed income portfolio. We continue to maintain a short duration fixed income portfolio and have been using our risk budget to add products to our portfolio to help mitigate a rise in rates. We produced a total investment return of 1.0 per cent (2013 – 0.3 per cent) for the year. Our average annual total investment return since inception is 3.3 per cent, and we have made a positive investment return in every year since inception, including 2008.

Our portfolio mix illustrates our philosophy, as shown in the table on page 112. With the composition regulated by the Group's investment guidelines we have three investment portfolio categories: 'core', 'core plus' and 'surplus'. The core portfolio contains at least enough funds required to meet near-term obligations and cash flow needs following an extreme event. Assets in excess of those required to be held in the core portfolio may be held in any of the three portfolio categories, which are discussed further on page 111. As at 31 December 2014 and 2013 the managed portfolio was as follows:

	2013 %	2014 %
Fixed income securities	84.4	**81.9**
Cash and cash equivalents	14.7	**10.6**
Equity securities	0.7	**0.7**
Hedge funds	–	**6.8**
Other investments	0.2	**–**
Total	100.0	**100.0**

MANAGED INVESTMENT PORTFOLIO ALLOCATIONS

	2010 %	2011 %	2012 %	2013 %	2014 %
Cash	21.9	13.2	11.1	14.7	**10.6**
Short-term investments	0.5	4.0	5.4	9.8	**1.4**
Fixed income funds	–	–	–	1.1	**0.7**
Government debt	22.4	27.2	18.8	14.6	**21.4**
Agency debt	1.6	4.2	6.2	4.1	**0.8**
Agency MBS, CMBS	15.3	13.2	19.2	10.9	**7.7**
Non-agency RMBS, ABS, CMBS	2.9	5.8	5.3	8.4	**11.0**
FDIC corporate bonds	4.3	2.5	–	–	**–**
Corporate bonds	31.1	29.9	32.2	29.7	**31.7**
Bank loans	–	–	1.8	4.5	**5.8**
Fixed income – at FVTPL	–	–	–	1.3	**1.4**
Equity securities	–	–	–	0.7	**0.7**
Hedge Funds – at FVTPL	–	–	–	–	**6.8**
Other investments	–	–	–	0.2	**–**
Total	100.0	100.0	100.0	100.0	**100.0**

The corporate bond allocation represented 31.7 per cent of managed invested assets at 31 December 2014 compared to 29.7 per cent at 31 December 2013. At 31 December 2014 the Group's allocation to bank loans represented 5.8 per cent of the portfolio compared to 4.5 per cent at 31 December 2013. The Group's portfolio at 31 December 2014 also included a 6.8 per cent allocation to a diversified portfolio of low volatility hedge funds. There was no allocation to hedge funds at 31 December 2013.

The composition, duration and asset allocation of the investment portfolio are reviewed on a regular basis in order to respond to changes in interest rates and other market conditions. If certain asset classes are anticipated to produce a higher return within management's risk tolerance an adjustment in asset allocation may be made. Conversely, if the risk profile is expected to move outside of tolerance levels, adjustments may be made to reduce the risk in the portfolio. We try to be nimble in our investment strategy while putting our objective of capital preservation first and foremost. We believe in the application of common sense, and do not place much reliance on 'black box' approaches to investment selection.

Investments are, however, inherently unpredictable and there are risks associated with any investment strategy decisions. Recent history has been tumultuous and we remain ever watchful. We will continue to monitor the economic environment closely.

INVESTMENT PERFORMANCE

Net investment income excluding realised and unrealised gains and losses, was $28.6 million for the year ended 31 December 2014, an increase of 12.6 per cent compared to 2013. The increase for the year ended 31 December 2014 compared to 2013 is mainly due to the increased size of the investment portfolio resulting from the acquisition of Cathedral during 2013.

Total investment return, including net investment income, net realised gains and losses, impairments and net change in unrealised gains and losses was $22.0 million for the year ended 31 December 2014 compared to $6.9 million for 2013. For the year ended 31 December 2014, returns were generated primarily by a reduction in treasury yields, which offset the slight widening of investment grade credit spreads. This was in contrast to 2013 which saw a significant increase in treasury yields, offset somewhat by notable investment grade credit spread narrowing. In addition, in 2013, our EMD portfolio was detrimentally impacted by rising treasury yields and wider EMD credit spreads which led to negative performance in this asset class.

LIQUIDITY

Lancashire is a short-tail insurance and reinsurance group. As such, the investment portfolio must be liquid, short duration, and highly credit-worthy. As noted earlier, Lancashire's investment strategy places an emphasis on the preservation of invested assets and provision of sufficient liquidity for the prompt payment of claims in conjunction with providing a reasonably stable income stream.

Liquid securities will be maintained at an adequate level to more than meet expenses, including unanticipated claims payments. Only once safety, liquidity, and investment income requirements are satisfied, may additional growth in the investment portfolio be pursued. Given the current global outlook and incessant volatility in the markets, this is unlikely to occur in the near future.

CASH FLOW

Lancashire's cash inflows are primarily derived from net premiums received, from losses recovered from reinsurers, from net investment income, including dividends and other returns from associates, and any capital raising activities performed in a given year including the issuance of debt. Excess funds are invested in the investment portfolio, which consists of high-quality, highly liquid fixed income securities of short duration. Other cash inflows result from the sale and redemption of investments.

The principal outflows for the Group are the settlement of claims, the payment of reinsurance cover, payment of general and administrative expenses, the servicing of debt, the purchase of investment products, the distribution of dividends and the repurchasing of shares.

In 2014, operating cash flow was again strong, driven by the Group's robust underwriting performance. A net positive cash inflow arose from operations during the year of $212.5 million (2013 – $167.7 million). We have generated positive operating cash flows in each year of operation since inception.

KEY INVESTMENT PORTFOLIO STATISTICS

	2010	2011	2012	2013	**2014**
Duration	2.2 years	1.8 years	1.8 years	1.0 years	**1.5 years**
Credit quality	AA	AA–	AA–	AA-	**AA-**
Market yield	1.9%	1.5%	1.1%	1.2%	**1.5%**
Book yield	2.4%	1.9%	1.8%	1.4%	**1.5%**

ASSOCIATES

The $5.9 million share of profit of associates for the year ended 31 December 2014, mostly reflects Lancashire's 10 per cent equity interest in KHL. The share of profit of associates was $9.2 million for the year ended 31 December 2013 and related to the Accordion and Saltire vehicles. Kinesis and third-party capital are discussed on page 32.

OTHER OPERATING EXPENSES

	2013 $m	**2014 $m**
Employee salaries and benefits	37.3	**36.0**
Employment taxes on equity compensation	4.2	**(2.0)**
Other operating expenses	36.2	**36.8**
Total Lancashire, excluding Lloyd's segment	77.7	**70.8**
Lloyd's segment	7.3	**40.5**
Total	85.0	**111.3**

Excluding the Lloyd's segment, employee remuneration costs were $1.3 million lower for the year ended 31 December 2014 compared to the same period in 2013 largely due to the retirement of the Company's previous CEO earlier in the year. The year ended 31 December 2014 included reversals of employee national insurance accruals in relation to equity compensation exercises driven by both the timing of exercises and fluctuations in the share price.

The Lloyd's segment for the year ended 31 December 2014 includes $20.1 million of employee remuneration costs and $12.0 million of other operating expenses and $8.4 million relating to the amortisation of intangible assets arising on acquisition. For comparison, for the full year 2013, including the period pre-acquisition, the Lloyd's segment included $17.2 million, $14.1 million and $4.7 million respectively.

Equity based compensation was $23.3 million for the year ended 31 December 2014 and $16.7 million for the year ended 31 December 2013. Included in the 2014 charge is $4.4 million for awards made to Cathedral employees.

CAPITAL MANAGEMENT

Lancashire has built a reputation for being one of the best known and most active proponents of capital management in the industry. Capital management is our most important area of focus after underwriting and it is our firm belief that pro-active and flexible capital management is crucial in helping to generate a superior risk-adjusted return over time. With our focus on maximising shareholder return we will return capital where this offers the best returns for our shareholders. Including dividends declared in February 2015, we have returned 101.9 per cent of comprehensive income generated via dividends or share repurchases since inception.

The Group actively reviews the level and composition of capital on an ongoing basis. Internal methods have been developed to review the profitability of classes of business and their estimated capital requirements plus the capital requirements of the combination of a wide range of other risk categories. The key aim of the capital management process is to maintain a strong balance sheet, whilst:

- maintaining sufficient capital for underwriting opportunities and to meet obligations to policyholders;
- maximising the risk-adjusted return to shareholders within predetermined risk tolerances;
- maintaining adequate financial strength ratings; and
- meeting internal, regulatory and rating agency requirements.

The subsidiary operating entities also conduct capital requirement assessments under internal measures and in compliance with local regulatory requirements.

Capital raising can include debt or equity, and returns of capital may be made through dividends, share repurchases, a redemption of debt or any combination thereof. All capital actions require approval by the Board of Directors. The retention of earnings generated also leads to an increase in capital.

The composition of capital is driven by management's appetite for leverage, amongst other factors, including the cost and availability of different types of capital.

Maintaining a strong balance sheet will be the overriding factor in all capital management decisions.

CAPITAL

At 31 December 2014, total capital available to the Group was $1.683 billion, comprising shareholders' equity of $1.357 billion and $326 million of long-term debt. Tangible capital was $1.530 billion. Leverage was 19.4 per cent on total capital and 21.4 per cent on total tangible capital. Total capital and total tangible capital at 31 December 2013 was $1.792 billion and $1.615 billion respectively.

DIVIDENDS

During 2014, the Lancashire Board declared an interim dividend of $0.05, special dividends of $0.20 and $1.20, and a final dividend in respect of 2013 of $0.10 per common share. With the final dividend in respect of 2014 of $0.10 per common share plus the additional special dividend of $0.50 per share, total capital returns since inception amount to $2.3 billion, or 234.6 per cent of initial capital raised. The final dividend of $0.10 per common share and special dividend of $0.50 per share have been declared and will be paid on 15 April 2015 to the shareholders of record on 20 March 2015.

NON PRE-EMPTIVE ISSUE OF SHARES

As part of Lancashire's flexible approach to capital management the Board has in recent years requested and received from shareholders authority to issue up to 15 per cent of its shares on a non pre-emptive basis. Lancashire believes that this ability to raise capital quickly is important in securing first mover advantage in the catastrophe insurance and reinsurance business which it underwrites. The Board proposes to put a similar request for authority to shareholders in a resolution at the 2015 AGM to be held on 29 April 2015.

REPURCHASE PROGRAMME

During 2014, under the current Repurchase Programme ratified at the AGM on 30 April 2014, the Group commenced the repurchase of its own shares. The total shares repurchased during the year ended 31 December 2014 was $25.0 million compared to $nil in the year ended 31 December 2013.

WARRANTS

The outstanding warrants to purchase the Company's common shares were issued on 16 December 2005 and expire on 16 December 2015. We saw a higher volume of warrants exercised during 2014, relative to the prior year, and would expect this trend to continue until expiry. Warrants exercised during the year are shown below.

LETTERS OF CREDIT

Lancashire has standard LOC facilities which in total amount to $400.0 million, with a $75.0 million loan sub-limit available for general corporate purposes. Syndicate 2010 and Syndicate 3010 each have a catastrophe facility in place to assist in paying claims and gross funding of catastrophes. These facilities amount to a combined $100.0 million with a total of $60.0 million available by way of LOCs.

There was no outstanding debt under the above facilities at any reporting date. There are no off-balance sheet forms of capital.

WARRANTS

	Number of Management Team Performance warrants	Number of Management Team Ordinary warrants	Number of Founder warrants	Number of Lancashire Foundation warrants	Number of ordinary warrants	Total Number of warrants
Outstanding and exercisable as at 31 December 2013	859,445	6,184,399	19,074,787	648,143	2,350,000	29,116,774
Exercised during the year	(741,965)	(5,625,217)	(4,042,108)	–	–	(10,409,290)
Outstanding and exercisable as at 31 December 2014	**117,480**	**559,182**	**15,032,679**	**648,143**	**2,350,000**	**18,707,484**

CATHEDRAL

"Cathedral has demonstrated the ability to adapt to the market, and to attract new talent and develop new product lines, even in a very difficult market."

Peter Scales,
Chief Executive Officer, Cathedral

2014 reflects the first full-year of contribution from Cathedral to the Lancashire Group's results, following the completion of the acquisition in November 2013. The trading conditions were tough, but this was as expected. There was competition on all fronts, but Cathedral's long-standing client and broker relationships served to mitigate the worst effects of this.

Syndicate 2010, for which Lancashire owns 57.8 per cent of the capacity, had a good year with the emphasis on protecting the core portfolio. The reinsurance and primary lines saw pricing pressure across the board, but in general our signings, the proportion of the business that we subscribe to that we actually get, remained strong. The Aviation Reinsurance account suffered a number of losses including two Malaysian Airlines aircraft and the violence in Tripoli airport. This led to an all too brief up tick of the market, but was quickly overwhelmed by continued overcapacity. Cathedral has renewed the majority of its core book and reduced exposures where appropriate. For the Direct and Facultative Property line, the Binding Authorities segment remained generally stable with small increases in the first half of 2014 balanced with small reductions in the second half. The Open Market segment, however, did see continued rate pressure, which we expect to build. Our Property Reinsurance book came under some rating pressure, but the terms and conditions held up better than was feared at one point and we have been able to deliver a book largely where we expected it to be.

Syndicate 3010 continued its build out to four new lines in 2014, which has seen us increase our stamp from £30.0 million to £60.0 million during the year with a further increase to £100.0 million for 2015. The core Cargo portfolio is now supported by new Energy and Terrorism accounts written by the LUK teams in conjunction with the existing Lancashire portfolios and benefiting from their relationship and expertise, and by two new aviation portfolios.

Cathedral was fortunate to secure the services of two teams of underwriters specialising in Direct Aviation Hull and Liabilities with an emphasis on General Aviation and Rotorwing, and Aviation War including three consortia which the team leads on behalf of a number of Syndicates in Lloyd's.

Cathedral has demonstrated the ability to trade through a difficult market, to attract new talent and develop new product lines. As a significant buyer of reinsurance, the silver lining to the soft market cloud has been the ability to buy a greater depth of cover, reduce retentions and make savings to mitigate the effect of reductions on inwards business, as was the case for 2014.

Key financial information for Cathedral is as follows:

	For the period 7 November 2013 to 31 December 2013 $m	Full year 2013[1] $m	**2014 $m**
Gross premiums written	24.5	288.2	**284.3**
Net premiums written	22.8	222.3	**219.4**
Net premiums earned	39.8	224.6	**214.1**
Net insurance losses	19.0	90.3	**102.5**
Net underwriting profit	12.2	82.3	**64.1**
Other income	2.9	8.9	**10.2**
Profit after tax	6.4	33.0	**25.7**
Comprehensive income	6.7	33.3	**25.4**
Net loss ratio	47.7%	40.2%	**47.9%**
Net acquisition cost ratio	21.6%	23.2%	**22.2%**
Expense ratio[2]	15.8%	13.9%	**15.0%**
Combined ratio[2]	85.1%	77.3%	**85.1%**

(1) Full 2013 year financial information is presented for informational purposes only.

(2) In accordance with standard Lloyd's practice the expense ratio in CCL's financial statements is presented net of fees, commissions and other non-investment income. On this basis the combined ratio for 2014 is 81.5 per cent compared to 78.7 per cent for the full year 2013 and 77.8 per cent for the period 7 November 2013 to 31 December 2013.

KINESIS AND THIRD-PARTY CAPITAL

"Kinesis bound its first deals in 2014, representing a further development of Lancashire's strategy to build partnerships with capital market participants."

Darren Redhead,
Chief Executive Officer, Kinesis

Following the success of the Accordion and Saltire sidecars, Kinesis was launched in 2013 and represents a further development of Lancashire's strategy to build partnerships with capital market participants. It gives the Group the opportunity to leverage its underwriting expertise, whilst affording flexibility in the management and deployment of its own capital. In early 2014, Kinesis underwrote its first tranche of multi-class reinsurance agreements with further business written during the year. All contracts are fully collateralised with combined aggregate limits of $252.5 million, including net premiums written of $56.2 million. Two further offerings were completed during 2014, where an additional $87.5 million of limits were written for $21.6 million of net written premiums.

Lancashire's subsidiary KCML receives underwriting fees on all net premiums written by Kinesis Re, generating a stable stream of fee income, in addition to potential profit commissions. LHL also holds a 10 per cent equity stake in KHL, which is treated as an associate for accounting purposes. Lancashire's share of KHL's results is reflected as an equity pick up in the consolidated financial statements.

During the year ended 31 December 2014, Accordion and Saltire were placed in members' voluntary liquidation. A final profit commission of $6.7 million was paid by Accordion following a commutation of our quota share agreement and this was recorded in net insurance acquisition cost. The Saltire vehicle ran loss free in 2013. During the first half of 2014 the Group received a payment of $3.0 million of profit commission from the Saltire vehicle.

Financial information for the year ended 31 December is as follows:

	Kinesis		Accordion		Saltire		Total	
For the year ended 31 December	**2014 $m**	2013 $m	**2014 $m**	2013 $m	**2014 $m**	2013 $m	**2014 $m**	2013 $m
Profit commission	**–**	–	**6.7**	–	**3.0**	–	**9.7**	–
Underwriting fees	**6.2**	–	**–**	1.8	**–**	1.2	**6.2**	3.0
Equity pick up	**4.7**	–	**1.1**	6.6	**0.1**	2.6	**5.9**	9.2

Note: LHL owns 92.7% of KCML at 31 December 2014.

ENTERPRISE RISK MANAGEMENT

"The fundamental principle of the Group's approach to ERM is that risk management should be embedded in the processes and procedures that we use to run our business every day."

Charles Mathias,
Chief Risk Officer

The fundamental principle of the Group's approach to ERM is that risk management should be embedded in the processes and procedures that we use to run our business every day. This has not changed. However in 2014 we have had a busy year, preparing for the advent of Solvency II and ensuring that, whilst we recognise the different operating models and environments of our different platforms, we have a clear view of our risks and their management right across the Group.

ERM DEVELOPMENTS

With Solvency II now slated to apply from 1 January 2016, and the first supervisory reporting to the PRA due in mid-2015 there has been a lot of activity in 2014. Currently the Group Supervisor is the BMA, but both LUK and Cathedral (via Lloyd's) are subject to the supervision of the PRA and FCA in the UK. Bermuda is in the process of being assessed for Solvency II equivalence and is in the first wave of countries for consideration. The PRA has confirmed that it will be the Group Supervisor under the provisions of Solvency II.

At the Group level Lancashire created an ORSA Working Group. The concept of the ORSA is one that is gaining currency in many jurisdictions including the U.S. We believe that Lancashire has a good story to tell as we continually review our levels of risk and capital through established procedures such as the daily underwriting call, underwriting exception reports, weekly LICL and LUK PML updates and the fortnightly RRC meetings, as well as quarterly at the entity and Group Boards. The ORSA Working Group consists of the CRO and two Non-Executive Directors from the LHL Board who will rotate every two years. The ORSA Working Group allows Non-Executive Directors to make a more detailed review of the ORSA process and procedure, to raise challenges throughout the ORSA development and to contribute directly to the point-in-time report given to our regulators.

In 2014 the Group has:

- Developed and approved ERM and ORSA policies and procedures that were reviewed and agreed by the Board.
- Performed and documented a Risk Taxonomy Review to validate the completeness of the risk registers and the relation of risk assessment to Internal Audit activity.
- Performed and documented a Risk Appetite review leading to a Risk Appetite Process document to test and provide an overview of how we set and measure risk appetites.
- Integrated the CUL exposures to the Group exposure monitoring suite to allow stochastic modeling of Group PMLs and aggregation of overlapping RDS events.
- Submitted a Group ORSA point-in-time report to the PRA including an assessment of the appropriateness of the Standard Formula using a best efforts approach prior to finalisation of the guidelines.

Cathedral has maintained its 'Green' rating by Lloyd's in relation to the Lloyd's Solvency II regime. This has included submissions and procedural and process documentation for the internal model, submission of an ORSA and overall compliance with the Lloyd's risk framework.

KCML has instituted its own risk register, with input from the CRO, which reflects its unique role within the Group as an underwriting manager. It has also been the subject of review by Internal Audit.

ERM STRUCTURE

Capital Optimisation

Continuous monitoring of current and projected solvency against a suite of rating agency, regulatory and internal tolerances using proprietary and external models.

Active capital optimisation across the cycle, maintaining appropriate buffers and contingency arrangements.

…maintaining the focus and flexibility to optimise capital in line with underwriting opportunity… (not the other way around)

Risk Optimisation

Timely and appropriate integration of strategic and business planning, stress and scenario testing and capital and risk management to maximise shareholder returns across the cycle whilst maintaining exposures within appetite.

…targeting RoE of 13 per cent over the risk free rate across the cycle whilst exposing a maximum of 25 per cent of capital to a single peak zone return period loss in any one period…

ORSA & ERM

People

Collegiate underwriting approach across entities supported by the UMCC, daily exception reports, fortnightly management RRC covering the entire ERM and ORSA scope with core risk themes embedded in the work of key management and Board committees rather than being stand-alone.

…fostering and rewarding a culture of risk challenge, questioning and understanding throughout all our business – a 'way of working' not a 'function'…

Process

Clear Group and Entity Risk Appetites spanning the entirety of the Risk Universe.

Significant investment in risk modeling and analytics tools and associated processes enabling virtually continuous monitoring and management of key risk metrics and their associated capital implications.

…clearly defined risk appetite and tolerances with effective processes for the identification, selection, assessment and optimisation of intrinsic and operational risk…

RRC

The Risk and Return Committee, now under the Chairmanship of the Group CEO, is the key management tool for monitoring and challenging the assessment of risk on a continual basis. The RRC agenda has seen a number of amendments in 2014 as part of a programme to ensure that we clearly embed the ownership of core ORSA elements in the RRC, and to schedule appropriate review activities across the business cycle. In particular, this has led to a more formal review of business planning, stress testing and reinsurance purchasing.

BLAST

We continue to challenge the assumptions used in BLAST and make changes where appropriate. In 2014, we have for example revised our assumptions about the frequency and severity of major energy losses, based on recent experience. We also developed BLAST to provide a more forward-looking assessment of underwriting risk through the use of synthetic portfolios for inwards property catastrophe reinsurance and retrocession business (i.e. the business that has most impact on our catastrophe exposures). The Kinesis catastrophe exposures were included alongside those of Cathedral, LICL and LUK.

EMERGING RISK

As ever, the Group tried in 2014 to foresee potential areas of new risk, or developments in existing risk that could threaten the Group. The continued emergence of new capital into the reinsurance arena and the subsequent displacement of traditional capacity into primary insurance may stretch the definition of an 'emerging' risk but it is an area that we monitor carefully. The Group CEO and CUO are uniquely well placed to see the trends through participation in the LICL and LUK daily UMCC. We also monitor cyber risk carefully, both in our operating exposure; where through our lack of retail clients and limited holding of our own employees personal data we present a low risk profile; and our insurance risk where we have conducted a careful review of our energy and marine hull accounts to determine what exposures there could be under our policies, and the robustness of policy exclusions where they are applied. We were satisfied that our exposure to cyber risk in these lines was limited and did not pose a threat to the business. The general geopolitical instability is also something we constantly monitor for implications for our Political Risk and trade-related lines such as Cargo and Sovereign obligors. The steep decline in the oil price is also bound to have an affect on our energy business, and we certainly expect the energy construction portfolio to be strongly impacted. There is little we can do to mitigate this, although parts of our Gulf of Mexico wind portfolio are sold on a multi-year basis, which is of some assistance.

RISK UNIVERSE

We performed a detailed study and provided a paper to the ORSA Working Group in 2014 that looked at the taxonomy of risk – how we identify and classify risks, and what this means in terms of our management and mitigation strategy. We classify risks in three broad classes;

- Intrinsic Risk: 'Risk that stems from the inherent randomness and uncertainty that exists in the universe in which we operate and that is therefore fundamental to how we manage our business'. This is the risk we accept as inherent in the core functions of our business; so we recognise that by insuring against fortuitous events we can suffer losses, and by investing premiums and other assets we can see the value of those investments fall. We cannot avoid these risks so we focus on the correlated operational risks and seek to mitigate them. So for example, we know that by insuring against the risk of earthquake we are exposed to the risk that losses exceed our plan. We model our portfolio using stochastic modeling to review actual and planned exposures to ensure they remain within tolerances. The correlated risks are that we might fail to design or maintain effective tolerances and limits, and fail to maintain exposures within such limits; or that we fail to keep accurate and timely records of our exposures. We then devise systems and processes to mitigate these risks, such as PML reconciliations, and RDS sign-offs.
- Operational Risk: 'The potential for specific losses arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events'. Risks that are operational in causation can be split in to two sub-categories in terms of how they crystallise:
  - Independent: risks that have the potential to crystallise independently from intrinsic risk. For example, losses arising through the imposition of fines as a result of a regulatory breach, so unrelated to our core functions.
  - Correlated: risks that relate to the failure to effectively operate the processes designed to manage intrinsic risk, and therefore have the potential to amplify its impact beyond that modeled. For example, increased reinsurer default losses arising through the use of non-approved counterparties.
- Other Risk: This is the more nebulous category of risks such as reputational risk, or communication risk which cannot necessarily be mitigated by holding capital since they may not have direct balance sheet implications. These are included within the risk register and assessed and mitigated through scenario and stress testing.

RISK UNIVERSE

Type		Category	Description
Intrinsic	Core	Underwriting Market (Investment)	Intrinsic risks representing the potential to generate a return as well as a loss. In these areas, the Group promotes informed risk taking that considers the risk and return equation in all major decisions, with the intention of maximising risk adjusted return on equity.
Intrinsic	Non-Core	Reserving (Re)Insurance Counterparty Liquidity	Intrinsic risks to which we are inevitably exposed as a result of conducting our day-to-day business operations yet offer no direct potential for return. They are quantified in so far as practicable for the purposes of capital and risk management and avoided or minimised insofar as is economically justifiable.
Operational		Operational	These are risks arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events. They have the potential either to magnify the adverse impacts of intrinsic risks or crystallise separately in their own right.
Other		Strategic Group Emerging	These are risks for which quantitative assessment is difficult but for which a structured approach is still required to ensure that their potential impact is considered and mitigated in so far as is practicable.

PRINCIPAL RISKS

As described under our review of the Risk Universe, our classification of risks as Intrinsic Core and Non-Core, Operational and Other, helps us to focus on our management and mitigation of those risks. Within BLAST insurance risk accounts for over 80 per cent of the allocated risk capital, so this is clearly the principal area where we stringently apply controls and reviews. For example, we place lots of controls around monitoring risk levels across the business. However we understand that even risks that do not generate a capital charge under an economic capital model can pose serious threats to the execution of the business plan and strategy, and therefore need to be monitored and tested. For example, we spend a lot of time looking at the implications of emerging capital and the evolution of the market cycle.

INTRINSIC RISK: CORE

TYPE	MITIGATION
Underwriting: Losses in our classes are hard to predict as to the specifics of timing and quantum of occurrence. Additionally, we write lines of business that are subject to accumulations, including accumulations of individual risks in a single event such as several property catastrophe excess of loss programmes being affected by a windstorm or earthquake, and accumulations between business lines such as a 9/11 type event impacting both the terrorism and AV52 portfolios. Losses can also exceed expectations in terms of both frequency and severity. So although we model losses, for example using the RMS and AIR stochastic models, we know that these projections can and will be wrong in many instances.	Modeling: We apply loads to, and stress test, stochastic models and develop alternative views of losses using exposure damage ratios. Risk and Return Committee: The Committee considers accumulations, clashes and paramaterisation of losses and models. Capital: We set our internal capital requirements at a level that allows for buffers above accumulations of extreme events.
Investment: We need to hold sufficient assets in readiness to pay claims, and the markets and products in which we invest can suffer volatility and losses. As a short-tail insurer, we are able to hold the majority of assets in low duration securities such as fixed income bonds. However, this creates an additional source of risk in the current environment, where there is a considerable risk from changes to interest rates as quantitative easing programmes may begin to taper or be increased. We model our investment portfolios and use various stressed scenarios to see what kinds of losses we could expect under a range of outcomes.	Investment strategy: Our strategy is that investment income is not expected to be a significant driver of our returns. Our primary focus remains on underwriting as the engine of profits. In 2014, we sought to hedge our interest rate risk through an increased risk asset allocation. Investment Risk and Return Committee: The IRRC forms an integral part of our risk management framework, meeting at least twice a quarter and reporting to the Board quarterly. External advisers: Lancashire's Board and management recognise that the Company's principal expertise lies in underwriting, so we use the services of internationally recognised investment managers who are experts in their fields.

INTRINSIC RISK: NON-CORE

TYPE	MITIGATION
Reserving: Because we do not know the amount of losses we are going to incur at the outset of a contract, we have to make estimates of the reserves we need to hold to pay claims. If these reserves are inadequate and claims exceed them, the change may have an impact on earnings, or indeed capital. We use independent external reviews of our reserves which look at the overall levels of expected losses, as well as individual large events, including benchmarking analyses.	Short-tail business: Lancashire's focus is on short-tail lines of business where losses are usually known within, or shortly after, the policy period with a reasonable degree of certainty. Experience data: We have access to a lot of data, both our own and from the industry as a whole, about losses and loss trends. Actuarial and statistical data is used to set estimates of future losses, and these are reviewed by underwriters, claims staff and actuaries to ensure that they reflect the actual experience of the business. External review: Insurers typically conduct an independent, external review of their loss reserves. Lancashire retains the services of one of the leading industry experts, and our appetite is defined so as to set reserves within a range of reasonable estimates based on both internal and external review.

INTRINSIC RISK: NON-CORE CONTINUED

TYPE

Reinsurance and intermediary counterparty: Almost all our risks are brought to us by brokers, who act as an intermediary between us and the client and handle the transaction of payments of claims and premiums on our behalf. This exposes us to the risk of the mishandling by, or failure of, the broker concerned. In order to make our portfolio as efficient as possible, we buy reinsurance to protect against severity, frequency and accumulation of losses. Again, this exposes us to the risk that our counterparties may have the inability or unwillingness to pay us in the event of a loss.

MITIGATION

Counterparty credit limits: We use counterparty limits and seek to deal with reputable reinsurers, and use collateral agreements where appropriate. The operating entities of the Group that contract for reinsurance separately, maintain and report their own counterparty credit limits at the entity level. System checks prevent the use of unauthorised intermediaries and we have terms of business agreements with all of them that seek to limit our exposure. All reinsurers must conform to minimum rating standards or collateral arrangements where appropriate.

TYPE

Liquidity: In order to satisfy claims payments we need to ensure that sufficient of our assets are held in readily realisable form. This includes holding cash accounts for the expected level of attritional losses, as well as ensuring we can meet claims payment requirements in extreme events.

MITIGATION

Portfolio management: The Group maintains liquidity significantly in excess of the Board agreed tolerances through its focus on maintaining a portfolio that is highly liquid, of overall short duration and highly creditworthy. We monitor this through the use of stress tests, and mitigate it through the quality of the investments themselves.

OPERATIONAL

TYPE

These are risks arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events. They have the potential either to magnify the adverse impacts of intrinsic risks or crystallise separately in their own right. This can encompass IT availability where failure of an IT system such as our underwriting system could impact our ability to maintain accurate and up-to-date records of our exposure, which if correlated with an insurance loss could cause us to breach insurance risk tolerances. It could also encompass IT integrity, where an unauthorised intruder could alter data in our systems, or introduce a bug that would corrupt the system.

MITIGATION

Capacity: We mitigate the availability risk by adding redundancy to the capacity we need and using backups of data including off-site storage and we test these systems regularly.

Testing and access: We mitigate the integrity risk by using independent external penetration tests, and by restricting access to key systems to only those people who need to use them.

OTHER

TYPE

These are risks for which quantitative assessment is difficult but for which a structured approach is still required to ensure that their potential impact is considered and mitigated insofar as practicable. They include categories such as Strategic, Group and Emerging risks. A key area in 2014 has been Strategic Risk as we have seen continued emergence of capital eating away at pricing, and broadening of terms and conditions as the cycle reaches a low point.

MITIGATION

Qualitative approach: These risks require a qualitative approach, engaging staff in appropriate discussions about sources of risk, and then thinking about possible outcomes. The Group Executive Committee and the RRC consider these issues, and the CRO reports to the Board include standing items on Emerging Risk.

Revision of Attritional Loss Ratio: Lancashire has responded to the influx of new capital and the downturn in the market cycle by revising the expected attritional loss ratios to account for the changes to pricing and coverage, and using Kinesis to participate in a niche product for the collateralised market.

BALANCING RISK, RETURN AND RESPONSIBILITY

WHY CORPORATE RESPONSIBILITY IS IMPORTANT TO LANCASHIRE

Just as the Group seeks to balance risk and reward in the insurance market we are aware of the need to balance the responsibilities we owe to our stakeholders such as shareholders, regulators, staff and clients with our responsibilities to the broader society in which we operate. The insurance business by its nature seeks to provide support to those afflicted by the unexpected, but we recognise that many people and businesses around the world cannot afford, or do not have access to, the right kind of insurance. So we use our talents and resources, our people, time and money to support those who are in distress or at a disadvantage. We do this through our Foundation which supports a number of excellent charities, through giving our staff charity sabbatical weeks after an initial period of employment. We also do it by trying to be a responsible employer and a good corporate citizen in the societies in which we operate.

In terms of governance, the LHL Board sets the Group Corporate Responsibility policy and reviews reports on the activities of the Foundation (and is represented directly by a Non-Executive Director as one of the Trustees), the execution of the HR function, and the environmental impact of the business. The day-to-day activities of the Foundation are delegated to a Donations Committee comprised entirely of staff members, which monitors and reports on the activities of the charities to which donations are made.

OUR APPROACH

Corporate responsibility is an integral part of Lancashire's approach to its business. We try to limit the negative impact of our carbon footprint through mitigation strategies and offsets, and we also try to improve the world around us in positive ways such as the donations of the Foundation and the staff charity days to work on local improvement projects. As well as the direct benefits, we believe that Lancashire reaps indirect benefits in terms of its attraction as an ethical and compassionate employer, and the positive team-building benefits of the activities undertaken.

COMMUNITY

There is a growing sense in the insurance market of an insurance community that can combine a commitment to excellence in providing a crucial support for trade and business with a determination to influence local and global societies for the better. We remain strongly committed to engaging with our local communities in Bermuda and London and continue to support local initiatives and activities across the network, through partnerships with schools, local government and local businesses.

OUR APPROACH

We support our communities through the Foundation making donations to locally based charities and through our staff charity day release programmes and charity leave. We also help to run fundraising for the London Summer in the City Appeal to provide activities and care in the school holidays, and working groups to help improve our industry. We make our people available for market forums, and hold staff raffles to aid in our fundraising efforts.

OUR FOCUS AREAS

We focus on victims of disasters and those who are disadvantaged whether through lack of opportunity, lack of resources or just a need for a helping hand. As our business is in part based on insuring against natural disasters we know very well how disruptive they can be, so our biggest Foundation donation is to Médecins Sans Frontières (MSF), who provide immediate aid in crisis situations (both natural and man-made) right across the globe.

The Foundation has made significant financial commitments to charities that support families in crisis (Family Centre) and children with autism (Tomorrow's Voices) in Bermuda, and charities supporting ex-offenders throughout the UK (St Giles Trust), and a poverty relief programme in the Philippines (ICM). But we also support them in other ways, for instance renovating premises for Tomorrow's Voices, mentoring staff members for St Giles Trust and sending volunteers on week-long service missions to ICM.

We also make donations to charities suggested by staff and indeed by clients and brokers. In 2014, we supported Medical Detection Dogs, Find a Better Way, Action on Addiction and Ace Africa, all at the suggestion of our business partners, helping to build the sense of an insurance community in Bermuda and London.

COMMUNITY

$14.0m

donated through the Lancashire Foundation since inception.

ENVIRONMENT

100%

of CO_2 emissions offset.

MARKETPLACE

6,500

kids helped by the summer appeal co-ordinated by Lancashire in 2014.

WORKPLACE

100%

of employees are eligible for RSS awards.

EMPLOYEE ENGAGEMENT

We recognise that the energy and talents of the people of Lancashire can make a difference in a number of ways, and that our charitable partnerships offer a valuable way to channel these generous instincts. We provide day release programmes for staff to give back to the communities in which they live and around the world. In addition, staff are entitled to a week's charity leave on completion of three years' permanent employment with the Group, which they can spend with a charity of their choice or with an existing Foundation-supported entity.

INTERNATIONAL CARE MINISTRIES ('ICM')

Teamwork is important at Lancashire, so for the last five years we've sent a team of six volunteers each year to work with ICM in the Philippines on a building project to improve the quality of life of the poorest of the poor. In 2014, a team of eight built toilets for slum dwellers, assisted in various lessons at kindergartens and hosted health and livelihood sessions to participants of a major transformation project run by the charity. The experience of working together in an environment that is both physically and emotionally tough is one that all the participants have cited as something that improves their relationships with colleagues across the Group.

"Lancashire have been a faithful partner to the poorest of the poor in the Philippines. Coming alongside ICM for the past 5 years with both financial sponsorship and volunteer service, your commitment to improving lives in the Philippines is an admirable and much needed investment.

At ICM, we focus on efficiency and effectiveness, and we are proud to say that Lancashire's funding has been stewarded to create the maximum impact in the Philippines. Providing education to at risk children, delivering anti-malnutrition food, and developing strong leaders with effective training teams, Lancashire's generosity has turned despair into hope for thousands of people, and provided them a better future.

Thank you for your generosity, commitment and support. Your gifts to ICM, both as volunteers and sponsors, inspire and encourage us to go further. We are so grateful to have a company of such high calibre standing alongside us in the fight against poverty. On behalf of the thousands of lives you have touched, thank you."

DAVID SUTHERLAND,
CHAIRMAN OF THE BOARD, ICM

ENVIRONMENT

As a business based in London and Bermuda, with clients and brokers around the globe, the Lancashire Group incurs the bulk of its carbon footprint in the form of airline travel, which we offset through an organised programme. In 2014, Cathedral and Lancashire UK moved into a new building at 20 Fenchurch Street, which complies with all the latest standards for energy use and recycling.

OUR APPROACH

The figures in this report calculate 12 months from 1 January 2014 to 31 December 2014. Lancashire has elected to use the number of full-time employees (FTE) as its intensity metric and has determined an intensity ratio of 12.9 tCO_2e per FTE.

Types of Emissions	Activity	tCO_2e
Direct (Scope 1)	Gas (kWh)	40.3
	Refrigerant	13.0
Indirect energy (Scope 2)	Electricity (kWh)	751.6
Indirect other (Scope 3)	Business travel (km)	1,270.9
	Additional Upstream Activities	334.3
	Other	67.4
TOTAL EMISSIONS (tCO_2e)		2,477.5
Intensity metric:		
Staff number – 192 FTE		
TOTAL EMISSIONS (tCO_2e)		
Intensity ratio per FTE		12.9

OUR FOCUS AREAS

Using an operational control approach, Lancashire assessed its boundaries to identify all of the activities and facilities for which it is responsible and reported on all of the material Green House Gas (GHG) emissions including Scope 1, 2 and 3. Calculations performed follow the ISO-14064-1:2006 standard and give absolute and intensity factors for the Group's emissions.

Results show that GHG emissions in the year were 2,477.5 tonnes of CO_2e, comprised of direct emissions (Scope 1) amounting to 53.3 tonnes of CO_2e, and indirect emissions (Scope 2) amounting to 751.6 tonnes of CO_2e. The source of other indirect emissions (Scope 3) comprised 1,672.6 tonnes of CO_2e. Lancashire has purchased carbon credits to reduce its gross GHG emissions by 2,477.5 tonnes, off-setting its total carbon emissions and remaining carbon neutral.

In terms of emissions intensity, tCO_2e per FTE has increased by 13.2 per cent. This is due to the acquisition of Cathedral in 2013 and a subsequent increase in the number of FTEs. As actual data for Cathedral was unavailable in 2013, an extrapolation method was used based on industry standards; however a full set of actual data has been used in 2014's calculation, which has also contributed to the increase in Group emissions. In addition, Well-to-Tank (WTT) and Transmission and Distribution (T&D) emissions that were not reported in 2013, have been included in 2014's calculation, and account for more than 13 per cent of total Group emissions.

MARKETPLACE

We continue to help the development of our marketplace by making employees available to sit on market committees, boards and working groups. In 2014, they have given talks at industry conferences, investor days and symposia, and as part of market education programmes. We continue to work closely with colleagues in the market on the Summer in the City fundraising. As noted above, we also donate to many of the causes supported by our industry peers through the Foundation.

OUR APPROACH

We believe the most important thing we can do is to make the talents of our people available, and we do this happily. We also engage actively with our regulators in Bermuda and London, and the Cathedral team are active within the Lloyd's market structure. With our clients we are happy to welcome them to our offices, but we also travel to see them and their businesses right around the world.

INTERNSHIP PROGRAMME

Following a meeting with the Bermuda Minister for Home Affairs, the Company and the Lancashire Foundation jointly sponsor two two-year internship positions for Bermuda resident college graduates, to be spent working and learning in the Group's London office. The two-year term is a major commitment demonstrating the Group's determination to give back to Bermuda and the first two interns have been working in the London office during 2014.

"The Lancashire Foundation Graduate Development Programme has given me great insight into the underwriting process. The daily underwriting call allows for exposure to all classes of business written at Lancashire, enabling me to gain an understanding of various lines of business, beyond those that I have had the opportunity to be involved with on a daily basis. The Lancashire culture is one into which it has been incredibly easy to fit. Everyone is exceptionally approachable, willing to help and answer any questions; this setting has allowed me to learn about different aspects of the business beyond underwriting. The Lancashire Foundation Graduate Development Programme is a great jump start to my career and so far has given me a solid foundation in the London insurance market. I am really looking forward to the rest of my time at Lancashire."

JAIME FERRARI-MCCOMB
INTERN

"The Lancashire Foundation Graduate Development Programme has been a great experience for me. In my role I have been exposed to various classes of business. This has expanded my knowledge on different types of insurance, and I've learned more about the dynamic London market. Through various research tasks I've become more aware of current events around the world, and I am constantly learning new things. In my team I'm encouraged to ask questions, lines of communication are open, and teamwork is essential. During my time at the Bermuda office, I gained more knowledge about the reinsurance sector as well as more insight into the property catastrophe class of business. It was a very good learning experience to work with the team in Bermuda, particularly throughout the renewal period. The Lancashire Foundation Graduate Development Programme has had a very positive impact on me personally and professionally, and I am excited to see what the future holds!"

NICHOLAS BUTTERFIELD
INTERN

Visit our corporate website for more information: http://www.lancashiregroup.com

OUR FOCUS AREAS

Regulators: we recognise the need to engage closely with our regulators at the BMA, PRA, FCA and at Lloyd's and seek to be transparent in all our dealings with them.

Clients: we strive to offer clear, fairly-priced and useful products that meet our clients' needs across our three capital bases.

Brokers: we are fully committed to being a 'broker market' and prize our broker relationships very highly right across the Group.

Investors: we continue to work hard at investor relations and have an active programme of engagement with investors around the globe.

WORKPLACE

We continue to strive to attract excellent employees who drive our appetite to outperform. Every company says it, but we truly believe that the talents of our people and our unique culture set us apart from our competitors. We strive to attract and retain the very best employees in the insurance industry.

Recruiting the right people for the Group will always be a high priority for the business. It is critical that the aspirations and values of new recruits are a good match to both the role and the values of the Company.

OUR FOCUS AREAS

Our focus in 2014 has been to maintain the success of our employees through ongoing training and coaching – provided both internally and externally. We have continued to deliver the Management Development Programme and we measure our employees' success through attainment of personal performance metrics as well as performance within the Group's values framework.

DIVERSITY

We are committed to being an equal opportunities employer. The Lancashire Group is currently represented by employees from 16 different nations. There is a 65/35 per cent split of males to females (see page 58) that work in the Group. New staff receive equal opportunities training during their induction, and refresher training sessions for all staff are planned for 2015. We promote the value of having a diverse workforce. We have recently supported the 'Ban the Box' campaign, an initiative from Business in the Community to give ex-offenders better employment opportunities by calling for the removal of tick boxes from employment application forms that ask about criminal convictions.

Page 58
See our diversity figures

MÉDECINS SANS FRONTIÈRES

"2014 has been a remarkable year for MSF, as our staff continue to face an almost unprecedented level of humanitarian need. At the start of the year, MSF teams were responding to emergencies in South Sudan, Central African Republic and the Philippines. Whilst the devastation wrought by Typhoon Haiyan required a much shorter response, the violence prevalent in South Sudan and Central African Republic has been widespread. There has been little immunity granted to those working to provide healthcare to affected people – in South Sudan MSF hospitals have been bombed, looted and destroyed; in Central African Republic hospitals sheltering those wounded and sick were targeted, and in April, MSF lost three of our own staff in such an attack.

Other concurrent emergencies were even more challenging to respond to. The targeting of aid workers in Syria, including our own staff, resulted in the closure of MSF health facilities in the north-west of the country. Despite the mass violence and huge needs in Syria, MSF teams are constrained to working on the periphery of the country, providing medical care for those who make it to Jordan or Lebanon, and supporting national medical staff inside the country with supplies and equipment. In Myanmar, MSF activities in Rakhine State were suspended in February by the government, depriving a Muslim minority group, the Rohingya, many of whom live in squalid camps with restricted movement and without vital healthcare.

Then Ebola happened. An outbreak, not a war or communal violence, not a natural disaster, and not the actions of a government. During my years with MSF, I've read many testimonies from our staff working in crisis situations, however I've never been transported to the horrors of a situation quite so vividly as to the horrors of West Africa in the grip of the biggest Ebola outbreak the world has ever seen. A disease that preys on the compassion of those who care for those that are sick. Yet somehow in between all of the horror, our staff have also managed to transport me to those that have survived.

The work we do is possible because of your support. MSF puts a priority on private funds, raised from donors like Lancashire Insurance. Without this, MSF would not be able to work in situations that are not in the public eye, nor would we have been able to be the first responder to Ebola, or mounted large emergency responses in remote parts of South Sudan and Central African Republic.

Knowing that we have the continued support of Lancashire Insurance is so important to our teams, both in the office and in the field. I want to extend my personal thanks to you for that support, for entrusting MSF with your donation and enabling us to do our vital work. Thank you."

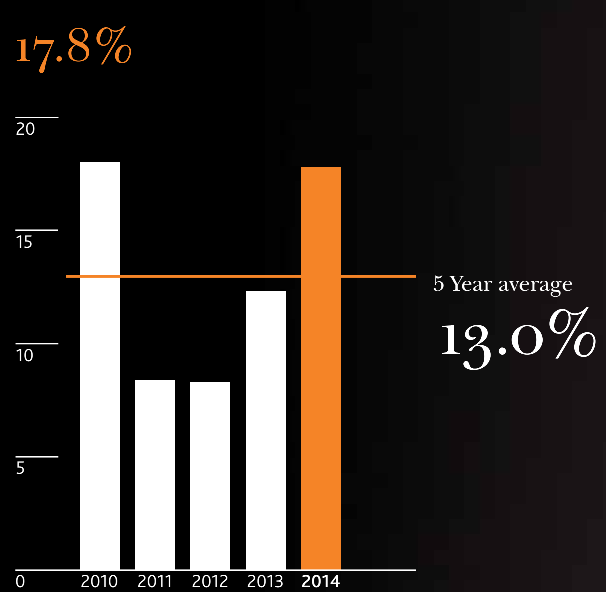
VICKIE HAWKINS
EXECUTIVE DIRECTOR – MSF UK

Opportunities *emerge &*

while here at Lancashire, we keep ourselves one step ahead of the curve, so that we are ready to maximise the right opportunities as they emerge into the market.

DIVIDEND YIELD

Lancashire's dividend yield demonstrates the active capital management that underpins our business model. Although we will buy back shares when the valuation makes sense, if we want to right-size capital quickly, the special dividend has become the key tool to enable us to do this.



evolve

EFFECTIVELY MANAGING CHANGE

"A combination of independence and diversity of talents and perspectives equips the Board to meet the challenges of our business."

Martin Thomas,
Non-Executive Chairman

In my opening statement I gave a broad overview of the challenges addressed by the Board during 2014 in ensuring that our business has the right management and strategic goals. The following section contains a more detailed account of the work carried out by the Board and its Committees in exercising effective oversight, taking decisions and providing support and constructive challenge to the business.

Q | HOW DOES THE BOARD SET AND MONITOR THE GOVERNANCE OBJECTIVES FOR THE GROUP?

A | Lancashire seeks to achieve the highest standards of corporate governance. By virtue of its premium listing on the LSE, Lancashire measures its corporate governance compliance against the requirements of the UK Corporate Governance Code published by the UK Financial Reporting Council (FRC). The FCA requires each company with a premium listing to 'comply or explain' against the Code (i.e. to disclose how it has complied with Code provisions or, if the Code provisions have not been complied with, provide an explanation for the non-compliance). The Code was further revised during 2014 for financial years beginning on or after 1 October 2014, but Lancashire and the Board have decided to comply with these new requirements in this year's Annual Report. The Company monitors its compliance with the Code, and in this corporate governance section and throughout this Annual Report for the 2014 financial year, areas of corporate governance compliance and non-compliance are explained by reference to the Code, as revised. The Company also monitors its compliance with applicable corporate governance requirements under Bermuda law and regulations. I am pleased to be able to report that there are no areas of material non-compliance with the Code.

Q | IS THE BOARD EFFECTIVE?

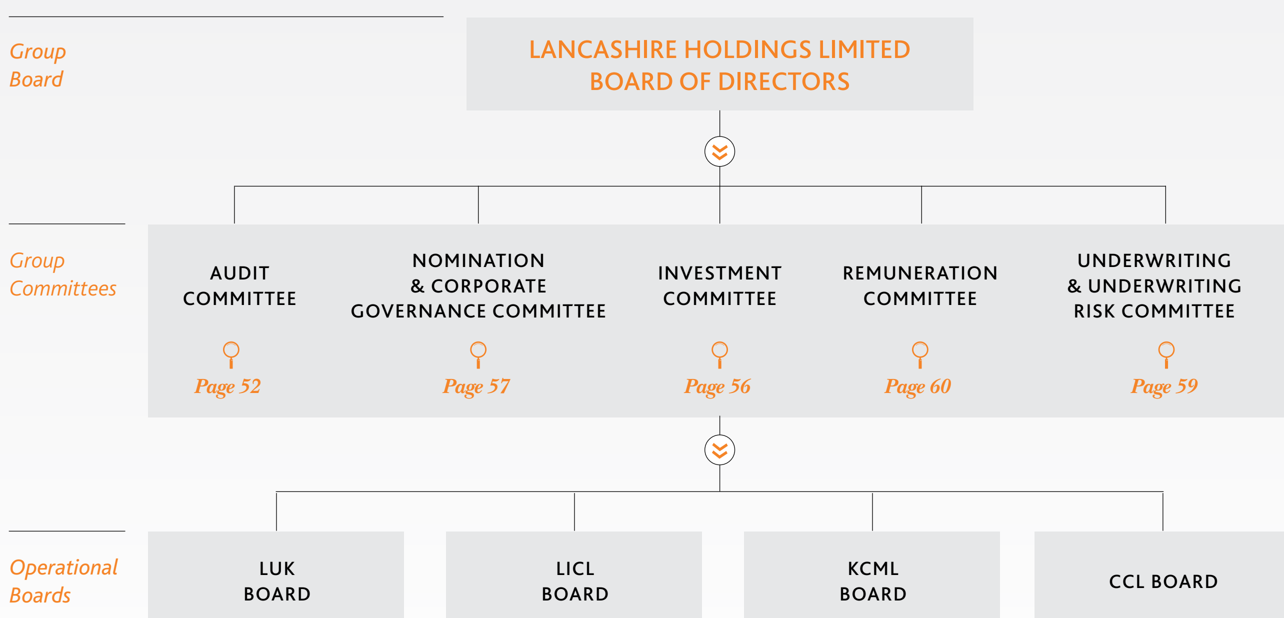
A | In my opening remarks I highlighted those changes that we have implemented to the Board and management team during this last year. The transition in management required time and attention from all the Non-Executive members of our Board, and I am grateful to all our Directors for the diligence with which they discharged their duties during the year. A Board is not always a comfortable place, but when it holds the necessary diversity of skills and experience it can operate as a forum to provide the strategic leadership and direction required by a business, particularly during times of transition. Having risen to these challenges earlier during the year, the Board took the opportunity to consider in more detail its own operation, composition and governance in a process facilitated by KPMG. That process has helped our Board to learn useful lessons and to focus on the requirement to maintain a Board whose members are independent in judgement and character and whose diversity of talent and perspectives equips the Board as a whole to meet challenges of the business. It has also helped inform our search for new talent and insight and I am delighted to be able to welcome Peter Clarke and Tom Milligan to our Board, who between them bring a wealth of experience in the areas of insurance, underwriting and investments as well as senior management and the operation of listed companies.

The 2014 performance appraisal of the Board and its Committees was facilitated by Chris Head, our Company Secretary, (see page 50 for further details). A summary report was discussed by the full Board and I am pleased to report the conclusion that the Board and each of its Committees are considered to have a balance of skills and perspectives that serve the Company effectively. The process also identified a number of areas for procedural improvements, training and learning. Following the recent period of rebuilding and refreshment, I believe Lancashire's Board is appropriately constituted to deliver the benefits of experience from a diverse range of perspectives and backgrounds. All the current Directors are recommended to shareholders for re-election at the 2015 AGM and I anticipate that 2015 will be a year of relative stability and continuity on the Board.

In closing I would like to record the thanks and appreciation of everyone at Lancashire to Ralf Oelssner, who sadly died in May 2014, shortly after having stepped down from the Boards of LHL and LUK. Ralf was a true gentleman who served our business over many years with a close attention to detail and a particular talent for contributing to the debate only at those moments when his insight was most valuable.

MARTIN THOMAS
CHAIRMAN

OUR GOVERNANCE STRUCTURE



OUR TEAM

MARTIN THOMAS (AGE 51),
NON-EXECUTIVE CHAIRMAN

ALEX MALONEY (AGE 41),
CHIEF EXECUTIVE OFFICER

ELAINE WHELAN (AGE 40),
CHIEF FINANCIAL OFFICER

PETER CLARKE (AGE 55),
NON-EXECUTIVE DIRECTOR

EMMA DUNCAN (AGE 55),
NON-EXECUTIVE DIRECTOR

SIMON FRASER (AGE 51),
SENIOR INDEPENDENT
NON-EXECUTIVE DIRECTOR

SAMANTHA HOE-RICHARDSON (AGE 44),
NON-EXECUTIVE DIRECTOR

TOM MILLIGAN (AGE 45),
NON-EXECUTIVE DIRECTOR

CHRISTOPHER HEAD (AGE 48),
COMPANY SECRETARY

MARTIN THOMAS (AGE 51),
NON-EXECUTIVE CHAIRMAN

Martin Thomas is a partner and board member of Altima Partners, LLP, the hedge fund manager, and a Director of two farming businesses, El Tejar Limited and Spearhead International Limited. Prior to this, he was an official of the Bank of England, most recently on secondment to the EU Commission where he worked in the Financial Services Policy and Financial Markets Directorate of the Internal Market and Services Directorate General. Before Mr Thomas joined the Commission, he established the Financial Markets Law Committee at the Bank of England. Prior to that, he was Deputy Chief Executive of the Financial Law Panel and prior to that, senior counsel to the European Central Bank in Frankfurt. He started his career in private practice, specialising in corporate and commercial litigation at Travers Smith and in the law and regulation of financial services at Clifford Chance.

ALEX MALONEY (AGE 41),
CHIEF EXECUTIVE OFFICER

Alex Maloney joined Lancashire in December 2005 and was appointed Group Chief Executive Officer in April 2014. On joining, Mr Maloney was responsible for establishing and building the energy underwriting team and account and, in May 2009, was appointed Group Chief Underwriting Officer. Since November 2010 Mr Maloney has served as a member of the Board and was appointed Chief Executive Officer of Lancashire Insurance Company (UK) Limited in 2012. Mr Maloney also serves as a Director of Cathedral Underwriting Limited and has been closely involved in the development of the Group's Lloyd's strategy. Mr Maloney has over 20 years of underwriting experience and has also worked in the New York and Bermuda markets.

ELAINE WHELAN (AGE 40),
CHIEF FINANCIAL OFFICER

Elaine Whelan joined Lancashire in March 2006 and leads both the Group finance function and the Bermuda insurance subsidiary, reporting to the Group Chief Executive Officer. Ms Whelan was previously Chief Accounting Officer of Zurich Insurance Company, Bermuda Branch. Prior to joining Zurich, Ms Whelan was an Audit Manager at PricewaterhouseCoopers, Bermuda, where she managed a portfolio of predominately (re)insurance and captive insurance clients.

PETER CLARKE (AGE 55),
NON-EXECUTIVE DIRECTOR

Peter Clarke was Group Chief Executive of Man Group plc between April 2007 and February 2013. In 1993 Mr Clarke joined Man Group plc, a leading global provider of alternative investment products and solutions as well as one of the world's largest futures brokers. He was appointed to the board in 1997 and served in a variety of roles before becoming the Group Finance Director in 2000. During this period he was responsible for investing in and developing one of the leading providers of third-party capital insurance and reinsurance products. In November 2005, he was given the additional title of Group Deputy CEO. Mr Clarke is currently the Chairman of the National Teaching Awards Trust and a Non-Executive Director of both AXA Investment Management S.A. and Lombard Odier Investment Management. Mr Clarke took a first in Law at Queens' College, Cambridge and is a qualified solicitor, having practised at Slaughter and May, and has experience in the investment banking industry, working at Morgan Grenfell and Citibank.

EMMA DUNCAN (AGE 55),
NON-EXECUTIVE DIRECTOR

Emma Duncan is the Deputy Editor of The Economist. She has also held several other posts on the magazine, including Britain Editor and Asia Editor. She has covered the media business, the Middle East, home affairs, agriculture, commodities and the transport industry and has served as Delhi correspondent, covering India, Pakistan, Bangladesh and Sri Lanka. She has written special reports for the magazine on Saudia Arabia and the Gulf states, India, Pakistan and the food industry. Ms Duncan appears regularly on television and radio programmes. She has written widely on a freelance basis, for publications such as The Times, The Sunday Times, The Daily Telegraph, Vogue and Cosmopolitan. She has an honours degree in politics, philosophy and economics from Oxford University and started her career as a researcher and reporter at Independent Television News.

SIMON FRASER (AGE 51),
SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR

Simon Fraser was Head of Corporate Broking at Merrill Lynch and subsequently Bank of America Merrill Lynch until his retirement in 2011. He began his career in the City in 1986 with BZW and joined Merrill Lynch in 1997. He led initial public offerings, rights issues, placings, demergers and mergers and acquisitions transactions during his career and advised many UK companies on stock market and London Stock Exchange issues. Mr Fraser has an MA degree in modern history from St Andrews University. He is also a Non-Executive Director of Derwent London plc where he chairs the Remuneration Committee and sits on the Audit and Nominations Committees.

SAMANTHA HOE-RICHARDSON (AGE 44),
NON-EXECUTIVE DIRECTOR

Samantha Hoe-Richardson is Head of Environment for Anglo American plc, one of the world's leading mining and natural resources companies. Ms Hoe-Richardson is responsible for improving sustainable development performance across the breadth of Anglo American's business units in areas such as water and climate change. She is also a director of Anglo American Zimele Green Fund (Pty) Ltd, which supports entrepreneurs in South Africa. Prior to her role with Anglo American, Ms Hoe-Richardson worked in investment banking and audit and she holds a masters degree in nuclear and electrical engineering from the University of Cambridge. She also has a chartered accountancy qualification.

TOM MILLIGAN (AGE 45),
NON-EXECUTIVE DIRECTOR

Tom Milligan was Co-Chief Executive Officer of Ariel Re Holdings Ltd., until his retirement in 2015. He began his career in the City in 1991 with Guy Carpenter & Co. and worked in both London and Bermuda as an insurance intermediary and underwriter. In 2005, Mr Milligan joined Goldman Sachs Group Inc. to start and manage the GS Reinsurance Group's non-life activities. As a Managing Director of Goldman Sachs, Mr Milligan served as Chief Underwriting Officer of Arrow Capital Re in Bermuda, before starting GS-owned Lloyd's Syndicate 1910 in 2008 and serving as Active Underwriter until 2012. In 2012, Mr Milligan led GS' purchase of Ariel Re and served as Co-CEO from April 2012 until July 2014. During 2013, Mr Milligan played a leading role in the spin-off of GS Reinsurance Group into Global Atlantic Financial Group (GAFG), before managing the sale of the Ariel businesses from GAFG to BTG Pactual in 2014. Mr Milligan graduated from Durham University in 1991.

CHRISTOPHER HEAD (AGE 48),
COMPANY SECRETARY

Christopher Head joined Lancashire in September 2010. Mr Head is Company Secretary of Lancashire Holdings Limited and advises on issues of corporate governance and generally on legal affairs for the Group. Prior to joining Lancashire, Mr Head was in-house counsel with the Imagine Insurance Group, advising specifically on policy wording and the structuring of reinsurance transactions. He transferred to Max at Lloyd's in 2008 as Lloyd's and London Counsel. Between 1998 and 2006 Mr Head was Legal Counsel at KWELM Management Services Limited, where he managed an intensive programme of reinsurance arbitration and litigation for insolvent members of the HS Weavers underwriting pool. Mr Head is a qualified solicitor having trained at Barlow Lyde and Gilbert where he worked in the Reinsurance and International Risk Team. Mr Head has a History degree and legal qualification from Cambridge University, where he was a choral scholar in the choirs of King's College and Trinity College.

BOARD COMMITTEES

THE DIRECTORS

Appointments to the Board are made on merit, against objective criteria and with due regard for the benefits of diversity on the Board, including gender. The Board considers all of the Non-Executive Directors to be independent within the meaning of the Code.

Peter Clarke, Emma Duncan, Samantha Hoe-Richardson and Tom Milligan are independent, as each is independent in character and judgement and has no relationship or circumstance likely to affect his or her independence. Prior to his appointment in 2013, the Board noted special circumstances relevant to determination of the independence of Simon Fraser which required consideration under the Code. Having taken into account Simon Fraser's employment at Merrill Lynch, in which capacity he had acted as lead corporate broker to the Company, and from which he had retired in December 2011, the Board determined that Simon Fraser is independent in character and judgement. This matter was previously disclosed and discussed in the Company's 2013 Annual Report. Simon Fraser became the Senior Independent Director on 30 April 2014 succeeding Ralf Oelssner upon his retirement from the Board. Martin Thomas was independent upon his appointment as Chairman on 1 May 2007. At the Board meeting held on 11 February 2015, further to a recommendation by the Nomination and Corporate Governance Committee, the Board affirmed its judgement that five of the eight members of the Board are independent Non-Executive Directors. Therefore, in the Board's judgement, the Board composition complies with the Code requirement that at least half the Board, excluding the Chairman, should comprise Non-Executive Directors determined by the Board to be independent.

In accordance with the provisions of the Code, all Directors are subject to annual election by shareholders. Shareholders are asked to note that Martin Thomas will have served as both a Non-Executive Director and Chairman of the Board for more than six years. Notwithstanding this period of service, the Board is of the view that Mr. Thomas continues to offer valuable service to the Company. The Board proposes to recommend the re-election of all the Directors at the 2015 AGM.

INFORMATION AND TRAINING

On appointment, the Directors receive written information regarding their responsibilities as Directors and information about the Group. An induction process is tailored for each new Director in the light of his or her existing skill set and knowledge of the Company, and includes meeting with senior management and visiting the Company's operations. Information and advice regarding the Company's official list and legal and regulatory obligations and on the Company's compliance with the requirements of the Code is also provided on a regular basis.

An analysis of the Company's compliance with the Code is collated and summarised in quarterly reports together with a more general summary of corporate governance developments, which are prepared by the Company's Legal and Compliance department for consideration by the Nomination and Corporate Governance Committee. The Directors have access to the Company Secretary who is responsible for advising the Board on all legal and governance matters. The Directors also have access to independent professional advice as required. Regular sessions are held between the Board and management as part of the Company's quarterly Board meetings, during which in-depth presentations covering areas of the Group's business are made. During these presentations the Directors have the opportunity to consider, challenge and help shape the Company's commercial strategy.

BOARD PERFORMANCE EVALUATION

A formal performance evaluation of the Board, its Committees and individual Directors is undertaken on an annual basis and the process is initiated by the Nomination and Corporate Governance Committee. The aim of this work is to assess the effectiveness of the Board and its Committees in terms of performance, composition, supporting processes and management of the Group, as well as to review each Director's performance, training and development needs. The 2012 performance evaluation was facilitated by external consultants, whilst in 2013 and 2014 the evaluation was conducted internally.

During 2014, it was decided that the evaluation process would be led by the Company Secretary, who conducted a series of meetings with each of the Directors to appraise and discuss their individual performances and to ascertain their views on the effectiveness of the Board and its Committees, the contribution of each of the individual Directors, and the management of the Company. The process was informed by the governance review which had been facilitated by KPMG earlier during 2014. On completion of the interviews, the Company Secretary reported to the Nomination and Corporate Governance Committee and the Board.

In summary, the 2014 evaluation discussions found that the Board operates effectively and has a good blend of insurance, financial and regulatory expertise. All Non-Executive Directors are committed to the continued success of the Company and to making the Board and its Committees work effectively. Attendance at Board meetings was found to be good. The CEO and the CFO, the Company's Executive Directors, were also found to be operating effectively.

Appropriate infrastructure, processes and governance mechanisms are in place to support the effective performance of the Board and its Committees. The Board is considered to manage risk effectively. The number of Directors on the Board is considered to be appropriate and the Board Committees are considered to have an appropriate balance of skills and to function effectively. The Board will continue to review its procedures, training requirements, effectiveness and development in 2015.

The Chairman's performance appraisal was convened by the Senior Independent Director, who consulted with the Non-Executive Directors with input from the Executive Directors during July 2014. The Chairman's performance was found to be effective.

At the end of the year, the Chairman met the CEO, and the CEO met the CFO, to conduct a performance appraisal in respect of 2014 and to set targets for 2015.

	Board	Audit Committee	Investment Committee	Nomination and Corporate Governance Committee	Remuneration Committee	Underwriting and Underwriting Risk Committee
Non-Executive Directors						
John Bishop[1]	4/4	2/2	–	–	–	2/2
Peter Clarke[2]	3/3	1/2	1/2	–	0/0	–
Emma Duncan[3]	8/8	–	0/0	3/3	6/6	–
Simon Fraser[4]	8/8	4/4	–	–	6/6	–
Samantha Hoe-Richardson[5]	8/8	4/4	–	3/3	–	–
Neil McConachie[6]	3/4	–	2/2	–	–	–
Ralf Oelssner[7]	0/4	0/2	–	1/5	0/4	0/2
Robert Spass[8]	8/8	–	3/4	–	–	–
William Spiegel[9]	7/8	–	3/4	4/5	5/6	–
Martin Thomas	8/8	–	–	8/8	–	–
Executive Directors						
Richard Brindle[10]	1/1	–	–	–	–	1/2
Alex Maloney	7/7	–	–	–	–	4/4
Elaine Whelan	6/6	–	4/4	–	–	–

(1) John Bishop retired from the Board, and as a member of the Audit and Underwriting and Underwriting Risk Committees, on 30 April 2014.

(2) Peter Clarke was appointed to the Board and as a member of the Audit and Investment Committees on 9 June 2014, and was appointed as a member of the Remuneration Committee on 4 November 2014.

(3) Emma Duncan was appointed as a member of the Nomination and Corporate Governance Committee on 5 June 2014 and as a member of the Investment Committee on 4 November 2014.

(4) Simon Fraser was appointed Chair of the Remuneration Committee on 30 April 2014.

(5) Samantha Hoe-Richardson was appointed Chair of the Audit Committee on 30 April 2014 and as a member of the Nomination and Corporate Governance Committee on 5 June 2014.

(6) Neil McConachie retired from the Board and as a member of the Investment Committee on 30 April 2014.

(7) Ralf Oelssner suffered from ill health for much of 2014 and was unable to attend the majority of meetings held prior to his retirement from the Board on 30 April 2014. He also retired as a member of the Audit, Nomination and Corporate Governance, Remuneration and Underwriting and Underwriting Risk Committees on 30 April 2014. Mr Oelssner sadly passed away shortly after his retirement.

(8) Robert Spass retired from the Board and the Investment Committee on 31 December 2014.

(9) William Spiegel retired from the Nomination and Corporate Governance Committee on 5 June 2014 and from the Board and Investment and Remuneration Committees on 31 December 2014.

(10) Richard Brindle retired from the Board, and as a member of the Underwriting and Underwriting Risk Committee, on 30 April 2014.

RELATIONS WITH SHAREHOLDERS

During 2014, the Group's Head of Investor Relations, usually accompanied by one or more of the CEO, the CUO, the CFO, the CRO, the Chairman or a senior member of the underwriting team, made presentations to major shareholders, analysts and the investor community. Formal reports of these meetings were provided to the Board on at least a quarterly basis.

Conference calls with shareholders and analysts hosted by senior management are held quarterly following the announcement of the Group's financial results. The CEO, CUO and CFO are generally available to answer questions at these presentations.

Shareholders are invited to request meetings with the Chairman, the Senior Independent Director and/or the other Non-Executive Directors by contacting the Head of Investor Relations. All of the Directors are expected to be available to meet with shareholders at the Company's 2015 AGM.

The Company commissions regular independent shareholder analysis reports together with independent research on feedback from shareholders and analysts following the Company's results announcements. This research, together with the analysts' notes, is made available to all Directors.

ENTERPRISE RISK MANAGEMENT

The Board is responsible for setting the Group's risk appetite and preferences, defining its risk tolerances, and monitoring and ensuring compliance with risk tolerances. During 2014, the Board carried out a robust assessment of the principal risks affecting the Group's business model, future performance, solvency and liquidity.

Further discussion of the risks affecting Lancashire and the policies in place to manage them can be found in the risk disclosures section on pages 100 to 126.

Each of the Committees is responsible for various elements of risk. The CRO reports directly to the Group and subsidiary Boards and facilitates and aids the identification, evaluation, quantification and control of risks at a Group and subsidiary level. The CRO provides regular reports to the Group and subsidiary Boards covering, amongst other things, actual risk levels against tolerances, emerging risks and any lessons learned from risk events. The Board considers that a supportive ERM culture, established at the Board and embedded throughout the business, is of key importance. Facilitating and embedding of ERM and helping the Group to improve its ERM practices is a major responsibility assigned to the CRO. The Group's risk management is informed by FRC's Internal Control: Revised Guidance for Directors on the Combined Code. The CRO's remuneration is subject to annual review by the Remuneration Committee.

COMMITTEES

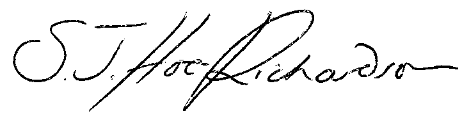
The Board has established Audit, Nomination and Corporate Governance, Remuneration, Investment and Underwriting and Underwriting Risk Committees. Each of the Committees has written Terms of Reference, which are reviewed regularly and are available on the Company's website (www.lancashiregroup.com). All the Committee Terms of Reference were reviewed and revised by the Board during 2014 with particular reference to the good practice guidance published by the ICSA. The Committees are generally scheduled to meet quarterly although additional meetings are scheduled as business requirements dictate.

The composition of the Committees as at 31 December 2014 was as set out in the table appearing on page 45. A report from each of the Committees is set out from page 52 through to page 60.

Samantha Hoe-Richardson –
Chairman of the Audit Committee

AUDIT COMMITTEE

"The Audit Committee works closely with management and the Company's internal and external auditors to give the Board and our broader stakeholders assurance on the quality and integrity of the Company's financial statements, reports and financial controls."



Following the AGM on 30 April 2014, I was delighted to take up the position of Audit Committee Chairman, a role that I assume from John Bishop who had ably chaired the Audit Committee since 2010. I would like to thank John Bishop and Ralf Oelssner, who served on the Audit Committee until their retirement from the Board at the 2014 AGM, as well as the current Audit Committee members and all those staff who contribute to the Audit Committee's work.

COMMITTEE MEMBERSHIP

The Audit Committee comprises three independent Non-Executive Directors and is chaired by Samantha Hoe-Richardson, a qualified accountant, whom the Board considers to have recent and relevant financial experience (see Ms Hoe-Richardson's biography on page 48). The internal and external auditors have the right of direct access to the Audit Committee. The Audit Committee's detailed Terms of Reference are available on the Company's website.

	Meetings attended
Samantha Hoe-Richardson (Chairman)	4/4
Simon Fraser	4/4
Peter Clarke (appointed effective 9 June 2014)	1/2
Former members	
John Bishop	2/2
Ralf Oelssner	0/2

Notes:

(1) John Bishop and Ralf Oelssner retired from the Committee on 30 April 2014 (see notes 1 and 7 on page 50).

PRIORITIES FOR 2015

The Committee's priorities for 2015 are to ensure the continued effectiveness of the Company's control environment and ensure that the Company is able to meet the requirements of the new Solvency II regime in 2016.

FINANCIAL REPORTING

COMMITTEE RESPONSIBILITY	COMMITTEE ACTIVITIES
Monitors the integrity of the Company's financial statements and any other formal announcement relating to the Company's financial performance. Reports to the Board on significant financial reporting issues and judgements contained in the financial statements.	At each quarterly meeting the Committee reviews the Company's financial statements for the purposes of recommending their approval by the Board. The Committee also monitors the activities of the Company's Disclosure Committee and reviews the Company's quarterly financial press releases, which it recommends to the Board for approval. The Committee receives quarterly reports from management on: • developments in accounting and financial reporting requirements, • any new and/or significant accounting treatments/transactions in the quarter, and • loss reserving (see page 143 for further details). An annual paper is also presented that details the areas of judgement or estimation in the financial statements (see accounting policies page 94 for detail of these areas). The Committee also considers quarterly reports on the financial statements from the external auditors, including an interim review report and a year-end audit results report. These are discussed with the external auditors at the Committee's meetings. Of the areas of judgement or estimation considered by the Committee in 2014, those that were considered significant are loss reserving and the valuation of intangible assets. These are explained in further detail in the box below. In accordance with auditing guidance, the external auditors' report includes revenue recognition and the estimation of premium revenues as an area of risk. The Audit Committee considered this and concluded that for Lancashire revenue recognition is straightforward and low risk. While some premiums are subject to estimation, revenues are unlikely to be materially different from initial estimates, particularly on a consolidated Group basis.
Reviews the content of the Annual Report and Accounts and advises the Board on whether, taken as a whole, it is fair, balanced and understandable.	The Chairman of the Committee reviews early drafts of the Annual Report and Accounts to keep appraised of its key themes and messages and to raise any issues early in the process. The Committee reviewed the 2014 Annual Report and Accounts at the February 2015 Audit Committee meeting and advised the Board that the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

SIGNIFICANT AREAS OF JUDGEMENT OR ESTIMATION

LOSS RESERVING

As detailed on pages 143 to 146 of the consolidated financial statements, the estimation of ultimate loss reserves is a complex actuarial process that incorporates a significant amount of judgement. The Committee considers the adequacy of the Company's loss reserves at each Audit Committee meeting, for which purpose it receives quarterly reports from the Company's Reserving Actuary. Both the Reserving Actuary and Ernst & Young LLP (EY) present a comparison of Lancashire's reserves to their own best estimate at the Q2 and Q4 Audit Committee meetings. EY also conducts a high level review of the Company's loss reserves as part of their Q1 and Q3 review procedures. During 2014, the Committee focused its discussions around the Company's loss reserves on: the range of reasonable actuarial estimates and the divergence of the Company's estimates to the external actuarial estimates; current and prior year loss development including 'back-testing' of the Company's prior year reserves; and reserving for each insurance operating subsidiary. Having reviewed and challenged these areas, the Committee concurred with management's valuation of the Company's loss reserves and the relevant disclosures around loss reserving in the Company's consolidated financial statements.

INTANGIBLE ASSET VALUATION

The Company has two indefinite life intangible assets following the acquisition of Cathedral – goodwill and syndicate participation rights. Intangible assets with indefinite useful lives are subject to an impairment review at least annually or sooner if there is an indication of impairment. Some of the key inputs in the impairment review are based on management judgement and/or estimation (see page 96 of the consolidated financial statements for further details). These inputs are reviewed by the Audit Committee annually and are considered reasonable. The Audit Committee also considers the Company's internal stress tests and what stress scenarios would have to occur to indicate an impairment of its intangible assets. As a result of these considerations the Audit Committee agreed that there was no indication of an impairment of the Company's intangible assets and that the valuation of these assets was reasonable.

SOLVENCY II

COMMITTEE RESPONSIBILITY

Monitors developments in the Solvency II regime and the progress made within the Group in readiness for its implementation.

COMMITTEE ACTIVITIES

A quarterly report is provided to the Audit Committee by the CRO detailing the Company's current progress towards meeting its Solvency II requirements. The Group remains on track to meet the requirements of the new regime on implementation in 2016.

INTERNAL AUDIT

COMMITTEE RESPONSIBILITY

Monitors and reviews the effectiveness of the Group's Internal Audit function in the context of the Group's overall risk management system.

COMMITTEE ACTIVITIES

The Group's Internal Audit function reports directly to the Committee. Each year the Head of Internal Audit presents an audit plan to the Committee for consideration and approval. The key objective of Internal Audit is to audit on at least an annual basis those areas of the Group's business that are deemed to pose the greatest risk to the achievement of the Group's business objectives, and to audit all other areas of the Group's operations at least once every three years. The findings of each internal audit are reported to the Committee at the quarterly meetings. The Committee has a responsibility to ensure the timely implementation of agreed management actions and to review the status of these at its meetings.

During 2014, the Committee reviewed and approved an updated Internal Audit Charter. This can be viewed on the Company's website. An external assessment of the effectiveness of the Internal Audit function was commissioned by the Committee and was conducted by Deloitte LLP (Deloitte), with a report issued to the Committee. The Committee discussed the report and its findings with Deloitte and the Head of Internal Audit and noted that no significant issues were raised. The Committee concluded that the Internal Audit function is operating effectively and efficiently in the context of the Group's overall risk management system and is adequately resourced.

EXTERNAL AUDIT

COMMITTEE RESPONSIBILITY

Oversees the relationship with the Group's external auditors and is responsible for assessing annually their independence and objectivity, taking into account the relevant professional and regulatory requirements, specifically including:

- An annual assessment of the qualifications, expertise and resources of the external auditors and the effectiveness of the external audit process.

COMMITTEE ACTIVITIES

The Committee reviews reports from the external auditors at each quarterly Committee meeting including the annual audit plan and an ongoing assessment of the effective performance of the audit compared to the plan. The Committee Chairman conducts informal meetings with the auditors and the CFO prior to, during and after the quarterly audits. The Committee meets in executive session with the external auditors and with management at least twice per annum.

During 2014, a detailed assessment of the effectiveness of the external audit process was performed by the Committee Chairman by means of the completion of a detailed questionnaire. This included input from the Company's senior management and the external auditors. The review enabled the Audit Committee to determine that the external audit process was effective and to note some minor development areas for future audits. Also during 2014, a review of EY's 2013 audit of the Company was completed by the FRC with no significant issues noted. The results of this review were discussed by the Committee and minor improvements to the external audit process were agreed for future years.

EXTERNAL AUDIT CONTINUED

• The implementation of a policy on the supply of non-audit services to ensure that the provision of non-audit services by the external auditors does not impair their independence and objectivity.	The Committee has approved and adopted a non-audit services policy that is reviewed on an annual basis and was last updated in October 2014. The policy, which stipulates rules around approvals required for various types of non-audit services, can be found on the Company's website. During 2014, EY provided non-audit services in relation to taxation services, capital management projects, Cathedral group restructuring and services pursuant to the KCML shareholder and subscription agreement. Fees for non-audit services provided in 2014 totalled $0.3 million representing 15.0 per cent of total fees paid to EY. The Committee gave careful consideration to the nature of the non-audit services provided and the level of fees charged, and has determined that they would not affect the independence and objectivity of EY as auditors.
• Making a recommendation to the Board, to be put to shareholders for approval at the AGM, in relation to the appointment, re-appointment and removal of the Company's external auditors.	The Committee has recommended to the Board the re-appointment of EY to perform the 2015 external audit. EY has been the Group's external auditors since 2005 and Angus Millar has been the lead audit partner since 2012. When making its recommendation to the Board, the Committee considered and had regard to EY's length of tenure and any non-audit services provided during the year, and continued to be satisfied with EY's performance, independence and objectivity, level of fees charged, compliance with ethical standards and audit partner rotation policy. During 2014, the Board approved a recommendation by the Committee that the external audit contract is put out to tender during 2016, which will be during the fifth year for the current EY lead audit partner. A recommendation will be made to shareholders at the 2017 AGM.

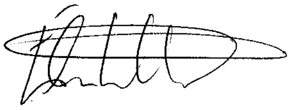
INTERNAL CONTROLS AND RISK MANAGEMENT SYSTEMS

COMMITTEE RESPONSIBILITY	COMMITTEE ACTIVITIES
Reviews the adequacy and effectiveness of the Group's internal financial controls and internal control and financial risk management systems (including financial, operational and compliance controls).	The Board has ultimate responsibility for maintaining a robust framework of internal controls and risk management and for overseeing and ensuring the effectiveness of the Group's risk management and internal control systems and has delegated the monitoring and review of this framework to the Committee. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss. The Committee receives an annual paper detailing the effectiveness of the Company's internal controls, which is reviewed and discussed by the Committee. This paper covers all material controls including financial, operating and compliance controls. In 2014, the Committee was satisfied that the Company's internal control framework was operating effectively.
Reviews for adequacy and security of the Company's 'whistleblowing' arrangements, procedures for detecting fraud and systems and controls for the prevention of bribery and money laundering.	During 2014, the Committee reviewed and recommended the adoption by the Board of updated policies and procedures for anti-money laundering, bribery and financial crime, conflicts of interest and whistleblowing. The Committee regularly reviews the Company's procedures for detecting fraud. The Committee also keeps under review the adequacy and effectiveness of the Company's legal and compliance function.

Elaine Whelan –
Chairman of the Investment Committee

INVESTMENT COMMITTEE

"The focus of the Committee continues to be on capital preservation and liquidity to support and complement the Group's underwriting operations."



COMMITTEE MEMBERSHIP

The Investment Committee comprises two Non-Executive Directors and one Executive Director (the CFO) together with the Head of Investments and Treasury (who is not a Director).

	Meetings attended
Elaine Whelan (Chairman)	4/4
Peter Clarke	1/2
Emma Duncan	0/0
Denise O'Donoghue	4/4
Former members	
Neil McConachie[1]	2/2
Robert Spass[2]	3/4
William Spiegel[3]	3/4

Notes:

(1) Neil McConachie retired from the Committee on 30 April 2014.

(2) Robert Spass retired from the Committee on 31 December 2014 (see note 8 on page 50).

(3) William Spiegel retired from the Committee on 31 December 2014 (see note 9 on page 50).

PRINCIPAL RESPONSIBILITIES OF THE COMMITTEE

- Recommend investment strategies, guidelines and policies for the Board of the Company and operating entities to approve annually.
- Recommend and set risk asset definitions and risk tolerance levels for management to operate within.
- Recommend the appointment of investment managers to manage the Group's investments.
- Monitor the performance of the investment strategies against pre-defined benchmarks.
- Establish and monitor compliance with investment operating guidelines relating to custody of investments and internal controls.

HOW THE COMMITTEE DISCHARGED ITS RESPONSIBILITIES DURING 2014

During 2014, the Investment Committee recommended the development of a hedge fund portfolio and the appointment of hedge fund managers. The Committee also conducted a review of the Group portfolio investment managers and recommended a reduction in the number of generalist fixed income managers.

The Committee undertook a strategic asset allocation study that resulted in recommended changes to the Group asset allocations. The Committee also recommended amendments to the definition of risk assets, although no changes were proposed to the maximum risk asset allocation.

The Committee considered regular reports on investment performance, asset allocation and compliance with pre-defined guidelines and tolerances.

During Q4 2014, the Investment Committee recommended to the Board the adoption of the 2015 investment strategy.

PRIORITIES FOR 2015

The Investment Committee will continue to focus upon the appropriate balance of risk and return in the implementation of the Group's investment strategy, preserving capital and managing its interest rate risk.

Martin Thomas –
Chairman of the Nomination and
Corporate Governance Committee

NOMINATION AND CORPORATE GOVERNANCE COMMITTEE

"A particular focus of the Committee during 2014 has been to ensure that, during a period of transition for the management team and the Board, the business is refreshed with individuals who bring skills, experience and a diversity of perspectives and backgrounds."

COMMITTEE MEMBERSHIP

A majority of the members of the Nomination and Corporate Governance Committee are independent Non-Executive Directors. The Committee Chairman is Martin Thomas who is the Chairman of the Board.

	Meetings attended
Martin Thomas (Chairman)	8/8
Emma Duncan	3/3
Samantha Hoe-Richardson	3/3
Former members	
Ralf Oelssner[1]	1/5
William Spiegel[2]	4/5

Notes:

(1) Ralf Oelssner retired from the Committee on 30 April 2014 (see note 7 on page 50).

(2) William Spiegel retired from the Committee on 5 June 2014 (see note 9 on page 50).

PRINCIPAL RESPONSIBILITIES OF THE COMMITTEE

- Review the structure, size and composition (including the skills, knowledge, experience and diversity) of the Board.
- Consider succession planning for Directors and other senior executives.
- Nominate candidates to fill Board vacancies.
- Make recommendations to the Board concerning Non-Executive Director independence, membership of Committees, suitable candidates for the role of Senior Independent Director and the re-election of Directors by shareholders.
- Review the Company's corporate governance arrangements and compliance.

HOW THE COMMITTEE DISCHARGED ITS RESPONSIBILITIES DURING 2014

BOARD COMPOSITION

The Committee reviewed the composition of the Board, with particular focus on the Non-Executive Directors, to ensure that the balance of skills, experience and diversity continued to be appropriate for the Group's business to meet the strategic objectives. The Committee also considered whether any additional skills and experience would be needed, either to complement those already on the Board, or to plan for filling vacancies due to the retirement of Directors.

The Committee recommended changes to the composition of the Board Committees during the year. It also recommended Simon Fraser for the role of Senior Independent Director upon the retirement of Ralf Oelssner at the 2014 AGM.

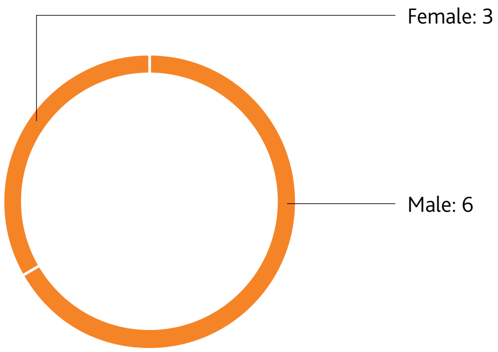
SUCCESSION PLANNING

The Committee reviewed the Company's succession plan for Executive Directors and other senior executives, taking into account the Company's risk environment and strategic objectives as well as the anticipated demands of the business. The Committee also recommended the appointment of Paul Gregory as Group Chief Underwriting Officer following the promotion of Alex Maloney to Group Chief Executive Officer.

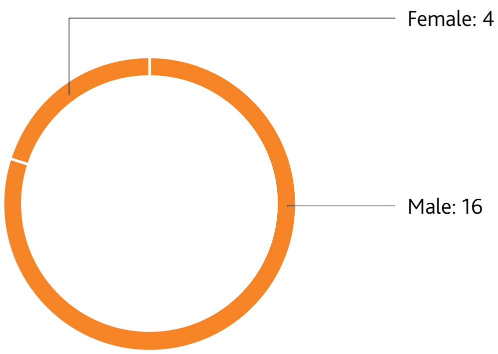
APPOINTMENT OF DIRECTORS

Peter Clarke and Tom Milligan were considered by the Committee and recommended to the Board for appointment as new Non-Executive Directors. In each case, the recruitment process was initiated by the Committee and, as part of that process, the Company engaged Odgers Berndtson (an executive search firm with no other connection to the Lancashire Group), who identified a number of potential candidates. Both Directors have received a tailored induction programme led by the Company Secretary.

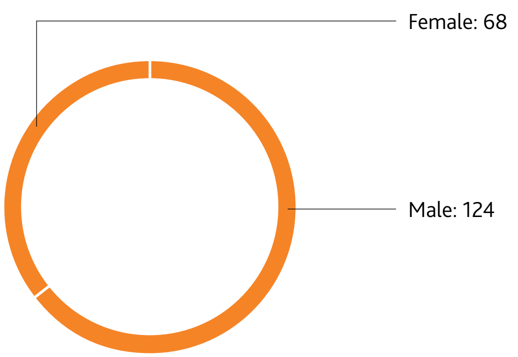
LHL BOARD MEMBERS



GROUP MANAGEMENT EXCLUDING LHL NON-EXECUTIVE BOARD DIRECTORS



OVERALL LANCASHIRE GROUP EMPLOYEES



* As at 31 December 2014.

CORPORATE GOVERNANCE

The Committee keeps under review the Company's corporate governance, particularly compliance with the Code, and is responsible for making recommendations to the Board concerning the process for conducting and facilitating the annual performance evaluation of the Board, its Committees and its individual Directors – see page 50.

During 2014, the Committee recommended the adoption by the Board of revised Terms of Reference for the Audit Committee, the Nomination and Corporate Governance Committee and the Remuneration Committee. It also recommended the approval by the Board of an amended Schedule of Reserved Matters and an updated protocol for the division of responsibilities and roles of the Chairman and Group CEO and the responsibilities and reporting lines of the CEOs of Group subsidiaries.

The Committee recommended approval by the Board of an updated statement on the representation of women on the Board, on executive committees and in senior management. This is published on the Company's website. In the context of the Davies Report, the Committee recognises the benefits that a broad diversity of skills, experience and gender, amongst other factors, brings to enhance Board performance but considers that quotas are not the best option for achieving diversity.

The Committee considered statistics relevant to the gender composition of the Board, Group management excluding Non-Executive Directors, and overall Lancashire Group employees. These statistics are shown opposite.

THE LANCASHIRE FOUNDATION

Flowing from the review of the Committee's Terms of Reference, the Committee assumed responsibility for monitoring and making recommendations to the Board in relation to the Company's charitable giving policy and the operation of, and reporting requirements for, the Lancashire Foundation.

PRIORITIES FOR 2015

The priority for the Nomination and Corporate Governance Committee for 2015 will be a continued focus on succession planning and to support management in the development of talent planning within the business, to ensure that the Board benefits from the skills and expertise of a diverse and independent team of Non-Executive Directors.

Alex Maloney –
Chairman of the Underwriting and Underwriting Risk Committee

UNDERWRITING AND UNDERWRITING RISK COMMITTEE

"The Committee is an important forum for discussing and setting the right underwriting risk appetites. It also monitors the Company's underwriting performance against the risk tolerances."

COMMITTEE MEMBERSHIP

The Underwriting and Underwriting Risk Committee comprises one Executive Director (the Group CEO) together with the Group CUO, the CUO of LICL, the CUO and Reinsurance Manager of LUK and the Head of Capital Modeling (who are not Directors).

	Meetings attended
Alex Maloney (Chairman)	4/4
Paul Gregory	4/4
Hayley Johnston	1/1
Sylvain Perrier	4/4
Ben Readdy	4/4
Former members	
John Bishop[1]	2/2
Richard Brindle[1]	1/2
Ralf Oelssner[1]	0/2

Note:

(1) John Bishop, Richard Brindle and Ralf Oelssner all retired from the Committee on 30 April 2014 (see notes 1, 7 and 10 on page 50).

PRINCIPAL RESPONSIBILITIES OF THE COMMITTEE

- Formulate Group underwriting strategy.
- Oversee the development of, and adherence to, underwriting guidelines by operating company CUOs.
- Review underwriting performance.
- Review significant changes in underwriting rules and policies.
- Establish, review and maintain strict underwriting criteria and limits.
- Monitor underwriting risk and its consistency with Lancashire's risk profile and risk appetite.

HOW THE COMMITTEE DISCHARGED ITS RESPONSIBILITIES DURING 2014

Underwriting risk is one of the key risks faced by the Company, and the Committee is actively engaged in the development of strategy and underwriting risk tolerances, which are approved by the Board. The Committee also monitors underwriting performance on a quarterly basis. In what has been a challenging ratings environment, Lancashire continues to prioritise good risk selection first and foremost, and the portfolio mix since inception has been relatively stable. The soft market has presented opportunities for the business to increase its reinsurance purchasing thereby de-risking the portfolio. The strategic underwriting priority for the business is to service the needs of clients and their brokers and thereby build a core book of business capable of sustaining a relevant and viable operation over the insurance cycle. During 2014, the Cathedral platform has afforded opportunities for new lines of business within the Lloyd's market through the build out of Syndicate 3010. The Committee has also received regular reports on the progress made in the development of the Kinesis platform during 2014. The Committee receives quarterly reports of significant claims to the business.

During 2014, the Committee meetings were open to attendance by all the Board members and provided a useful forum for the discussion of underwriting performance, risk tolerances and strategic initiatives. The Committee and Board place great importance on the management of the Company's capital so as to match capital to the underwriting requirements of the business.

A more detailed analysis of the Lancashire underwriting performance appears in the Business Review section of this Annual Report at pages 24 to 32.

PRIORITIES FOR 2015

For the coming year the Underwriting and Underwriting Risk Committee will continue to monitor the development of a forward-looking and disciplined underwriting strategy appropriate for the Group's three underwriting platforms, within a framework of appropriate risk tolerances.

REMUNERATION COMMITTEE

"The Committee seeks to align the interests of the Company's owners with those of its senior executives. Our remuneration policy affords financial rewards which are closely linked to performance."

Simon Fraser – Chairman of the Remuneration Committee

COMMITTEE MEMBERSHIP

The Remuneration Committee comprises three independent Non-Executive Directors.

	Meetings attended
Simon Fraser (Chairman)	6/6
Peter Clarke	0/0
Emma Duncan	6/6
Former members	
Ralf Oelssner[1]	0/4
William Spiegel[2]	5/6

Notes:

(1) Ralf Oelssner retired from the Committee on 30 April 2014 (see note 7 on page 50).

(2) William Spiegel retired from the Committee on 31 December 2014 (see note 9 on page 50).

PRINCIPAL RESPONSIBILITIES OF THE COMMITTEE

- Set the remuneration policy for the Company's Chairman, the Executive Directors, Company Secretary and other designated senior executives, to deliver long-term benefits to the Company.
- Determine the total individual remuneration package, including pension arrangements, of the Company's Chairman, the Executive Directors and other designated senior executives.
- Agree personal objectives for each Executive Director and the related performance and pay-out metrics for the performance element of the annual bonus.
- Determine each year whether awards will be made under the Company's restricted share scheme and, if so, the overall amount of such awards, the individual awards to Executive Directors and other designated senior executives, and the performance targets to be used.
- Ensure that contractual terms on termination, and any payments made, are fair to the individual and the Company.
- Oversee any major changes in employee benefit structures throughout the Group.

HOW THE COMMITTEE DISCHARGED ITS RESPONSIBILITIES DURING 2014

During 2014, the Committee approved the terms of the retirement arrangements for Richard Brindle, the former Group CEO. The Committee also approved the remuneration packages for Alex Maloney as the new Group CEO and for Paul Gregory as the new Group CUO.

The Committee considered the salary and bonus awards for 2014 for Executive Directors and other designated senior executives. The Committee also approved the grant of awards under the Company's restricted share scheme.

The Committee approved revised share ownership guidelines for senior and key executives.

The Committee also reviewed the policy for Executive Director remuneration which was approved by shareholders at the 2014 AGM. The Committee considers the policy fit for purpose and does not propose any amendments for the 2015 AGM.

The Directors' Remuneration Policy and the Annual Report on Remuneration for which the Committee is responsible can be found on pages 61 to 78.

The Committee's Terms of Reference were amended on 4 November 2014 to include provisions for the Committee's oversight and approval of performance objectives for Executive Directors and the related metrics for the performance element of the annual bonus.

PRIORITIES FOR 2015

During the coming year the Remuneration Committee, working with management, will undertake a review of incentivisation packages throughout the Group to ensure that remuneration is structured appropriately to promote the long-term success of the Company. This is expected to involve a degree of standardisation across the Group as Catherdral is integrated fully. The RSS structure for Executive Directors will also be reviewed to ensure that the performance metrics continue to align the interests of the Company, its investors and management.

ANNUAL STATEMENT

Dear Shareholder,

I am pleased to present my first Directors' Remuneration Report to shareholders following my appointment to chair the Remuneration Committee on 30 April 2014.

As a company incorporated in Bermuda, Lancashire is not bound by UK law or regulation in the area of Directors' remuneration to the same extent that it applies to UK incorporated companies. However, by virtue of the Company's premium listing on the London Stock Exchange and reflecting the Committee's approach to good governance, shareholders were given the opportunity to approve our remuneration policy at the 2014 AGM and we were grateful for the support of over 90 per cent of our shareholders. We are not proposing any changes to our remuneration policy but for convenience we have reproduced the policy on pages 62 to 65.

REMUNERATION AND STRATEGY

Lancashire's goal continues to be to reward its employees fairly and responsibly, by providing an appropriate balance between fixed and variable remuneration, linked to the achievement of suitably challenging Group and individual performance measures.

There is a strong link between the remuneration policy and the business strategy. As highlighted at the front of this Annual Report, our strategy focuses on the effective operation of the business necessary to maximise long-term and sustainable RoE and the delivery of superior total shareholder returns. Our remuneration policy is closely aligned to this strategy.

PERFORMANCE OUTCOME FOR 2014

The Lancashire Group has delivered solid results in a challenging market for 2014 (see the performance review of this report on pages 70 to 74).

Against a background of challenging market conditions there was a significant reduction between 2013 and 2014 in the total remuneration for our CEO and CFO (see the comparison table for single figure remuneration on page 69). This resulted in part from a lower RoE than was achieved in 2013 and a disappointing total shareholder return of -24.2 per cent for the year (see page 21 for further details).

The annual bonus was focused on both absolute RoE and relative RoE and also on individual objectives. Executive Directors' performance targets set at the beginning of 2014 for financial performance were stretching, and reflecting the Company's 2014 performance were achieved at about target level (and at or below 53 per cent of maximum bonus). Executive Directors' 2014 bonuses are expected to pay between 100 per cent and 106 per cent of target. Due to the large number of warrants outstanding, and the potentially volatile impact on the annual bonus performance metrics and the fact that the warrants are no longer owned by employees, the Committee decided at the beginning of the year that for the annual bonus performance targets for both the absolute and relative elements there should be an adjustment for the impact of warrant exercises. Accordingly the warrant adjusted RoE used for purposes of the absolute RoE metric is 14.7 per cent which represents an uplift of 0.8 per cent on the 2014 actual RoE of 13.9 per cent. For full details of Executive Directors' bonuses and the associated performance delivered see page 71.

In relation to long-term incentives, the 2012 Performance RSS awards were half based on absolute RoE targets and half on relative TSR against other peers over the three year period to 31 December 2014. Our TSR performance (in USD) over this period ranked the Company below the median of the designated peer group of 11 companies, resulting in no vesting for the TSR component. This, in part, was a reflection of the out-performance of the Company's share price relative to its peer group comparator companies in 2011, with a high base point resulting in a weaker TSR performance by comparison to peers during the relevant three year period.

Our average RoE performance over this period was 16.5 per cent against a threshold target of the 13 week Treasury bill rate plus 6 per cent, resulting in 100 per cent of the RoE component of the 2012 Performance RSS award vesting, a total vesting of 50 per cent of awards. This compared to the 100 per cent vesting of the 2011 RSS Performance awards, which we reported last year.

The total remuneration received by our current directors in 2014 was significantly lower than what was received in 2013 and this demonstrates the Committee's key principles of setting challenging performance criteria and having a significant proportion of the overall package linked to Company performance. The like for like employee costs at Lancashire (excluding the costs of the Lloyd's segment, but including the cost of the retirement package for Richard Brindle) were $1.3 million lower in 2014 (see page 29 for further detail).

Overall, in light of the annual and three-year performance delivered, the Committee is satisfied that there has been a robust link between performance and reward.

CHANGES TO THE EXECUTIVE BOARD

As detailed in the Nomination and Corporate Governance Committee report, at the 2014 AGM, there was a change in Chief Executive as Richard Brindle retired and Alex Maloney was promoted from his previous role as the Group's Chief Underwriting Officer.

As specified in his contract, Richard Brindle received payments comprising salary, benefits and pension in lieu of his notice period, and a pro-rata bonus for the period he was employed in 2014. In consideration of his decision to retire and his significant contribution to the foundation and management of Lancashire since its incorporation in 2005, the Committee decided to treat him as a good leaver under the rules of the annual bonus and Restricted Share Scheme. Full details of his termination payments are set out in the Annual Report on Remuneration on page 72.

APPLICATION OF REMUNERATION POLICY FOR 2015

Since my appointment, the Remuneration Committee has reviewed the policy approved by shareholders and considers it to remain fit for purpose. That said we have taken on board shareholder comments expressed at the last AGM and have made a number of changes in the way we will operate our policy for 2015.

- The policy includes a share ownership guideline requiring the CEO to build and maintain a holding of two times his salary and for other Directors to have shares worth one times salary. The Committee has revisited the share ownership guideline and tightened up the definition of ownership. Going forward, only wholly-owned shares or vested entitlements to shares will count whereas previously unvested deferred bonus awards were included. This will strengthen the alignment between management and shareholders.

- The Committee is cognisant of the need to set remuneration at a level which is sufficiently attractive to incentivise the best talent in a very competitive industry but at the same time to ensure that reward is not excessive by market and shareholder standards. In this regard, it should be noted that we have set the new Chief Executive's pay at a level which is significantly lower than his predecessor. See page 77 for further details.
- The minimum and maximum absolute RoE targets (adjusted for warrant exercises) attached to our annual bonus plan have been left unchanged despite the increased likelihood of a softer market in 2015. The target pay-out has been reduced from 12 per cent to 11 per cent to reflect the market outlook.

The final section of this report is the Annual Report on Remuneration which provides detailed disclosure on how the policy will be implemented for 2015 and how Directors have been paid in relation to 2014.

The disclosures provide shareholders with the information necessary to form a judgement as to the link between Company performance and how the Executive Directors are paid. This Annual Statement together with the Annual Report on Remuneration will be subject to an advisory vote and I hope that you will be able to support the resolution at the forthcoming AGM.

The Committee is committed to maintaining an open and constructive dialogue with our shareholders on remuneration matters and I welcome any feedback you may have. The Committee has committed to a full review of Group compensation for 2016 to include all Group Companies.

SIMON FRASER
CHAIRMAN OF THE REMUNERATION COMMITTEE

DIRECTORS' REMUNERATION POLICY SECTION

This part of the Directors' Remuneration Report sets out the Remuneration Policy for the Company. The policy has been developed taking into account the principles of the Code and the views of our major shareholders. The policy was voted into effect from the date of the 2014 AGM and is currently intended to operate until the AGM in 2017.

Although not required by the regulations, the substantive terms of the Remuneration Policy are reproduced below for ease of reference. However, any details that were specific to 2014 or earlier years (including, for example, the disclosure of the illustrative remuneration scenarios) have been updated where applicable. The policy table has been updated to incorporate the change to the share ownership guideline as set out in the Annual Statement. The full Policy Report approved by the Company's shareholders at last year's AGM can be accessed in the 2013 Annual Report on the Company's website.

GOVERNANCE AND APPROACH

The Company's Remuneration Policy is geared towards providing a level of remuneration which attracts, retains and motivates Executive Directors of the highest calibre to further the Company's interests and to optimise long-term shareholder value creation, within appropriate risk parameters. The Remuneration Policy also seeks to ensure that Executive Directors are provided with appropriate incentives to drive individual performance and to reward them fairly for their contribution to the successful performance of the Company.

The Remuneration Committee and the Board have considered whether any element of the current Remuneration Policy could conceivably encourage Executive Directors to take inappropriate risks and have concluded that this is not the case, given the following:

- there is an appropriate balance between fixed and variable pay, and therefore Executive Directors are not required to earn performance related pay to maintain their day-to-day living expenses;
- there is a blend of short-term and long-term performance metrics with an appropriate mix of performance conditions, meaning that there is no undue focus on any one particular metric;
- there is a high level of share ownership amongst Executive Directors, meaning that there is a strong focus on sustainable long-term shareholder value; and
- the Company has the power to claw back bonuses (including the deferred element of the annual bonus) and long-term incentive payments made to Executive Directors in the event of material misstatements in the Company's financial statements, error in the calculation of any performance condition, or the Executive Director ceasing to be a Director and/or employee due to gross misconduct.

HOW THE VIEWS OF SHAREHOLDERS ARE TAKEN INTO ACCOUNT

The Committee Chairman and, where appropriate, the Company Chairman, will consult with major investors and representative bodies on any significant remuneration proposal relating to Executive Directors. Views of shareholders at the AGM and feedback received at other times will be considered by the Committee.

HOW THE VIEWS OF EMPLOYEES ARE TAKEN INTO ACCOUNT

The Remuneration Committee takes into account levels of pay elsewhere in the Group when determining the pay levels for Executive Directors. The Remuneration Policy for all staff is, in principle, the same as that for Executive Directors in that all employees are offered similarly structured packages, with participation in annual bonus and long-term incentive plans. For Executive Directors with higher remuneration levels, a higher proportion of the compensation package is subject to performance pay, share based remuneration and deferral. This ensures that there is a strong link between remuneration, Company performance and the interests of shareholders.

The Company does not consult with employees on Executive Directors' remuneration. However, as noted above, the Committee is made aware of pay structures across the wider Group when setting the Remuneration Policy for Executive Directors.

POLICY TABLE

Base Salary

Purpose and Link to Strategy	Helps recruit, motivate and retain high-calibre Executive Directors by offering salaries at market competitive levels. Reflects individual experience and role.
Operation	Reviewed annually and fixed for 12 months, effective from 1 January. Positioning and annual increases influenced by: • role, experience and performance; • change in broader workforce salary; and • changes in responsibility or position. Salaries are benchmarked periodically against insurance company peers in the UK and in Bermuda.
Opportunity	No maximum.

Benefits

Purpose and Link to Strategy	Market competitive structure to support recruitment and retention. Medical cover aims to ensure minimal business interruption as a result of illness.
Operation	Executive Directors are entitled to healthcare, dental, vision, gym membership and life insurance. Executive Directors who are expatriates may be eligible for a housing allowance or other relocation-related expenses.
Opportunity	No maximum.

Pension

Purpose and Link to Strategy	Contribution towards funding post-retirement lifestyle.
Operation	The Company operates a defined contribution pension scheme (via outsourced pension providers) or cash-in-lieu of pension where contributions would exceed HMRC pension limits in the UK. There is a salary sacrifice structure in the UK. There is the opportunity for additional voluntary contributions to be made by individuals, if elected.
Opportunity	Company contribution is currently 10 per cent of base salary.

POLICY TABLE CONTINUED

Annual Bonus[1,2]

Purpose and Link to Strategy	Rewards the achievement of financial and personal targets.
Operation	Bonus targets (percentage of salary) are based on mechanistic calculations for financial and personal performance. The precise weightings may differ each year, although there will be a greater focus on financial as opposed to personal performance. The Committee, based upon input from the CEO, will have the ability to override the results of any mechanistic bonus calculation to either increase or decrease the amount payable (subject to the cap) to ensure a robust link between reward and performance. At least 25 per cent of each Executive Director's bonus is automatically deferred into shares as nil cost options over three years, with one third vesting each subsequent year. A dividend equivalent provision operates enabling dividends to be accrued (in cash or shares) on unvested deferred bonus shares in the form of nil cost options up to the point of exercise. If Lancashire's comprehensive income in the relevant full financial year should be negative, there will be no pay-out possible under the Relative Financial Performance element (details of the bonus metrics are included on page 68 of the Annual Report). The bonus is subject to claw back if the financial statements of the Company were materially misstated or an error occurred in assessing the performance conditions on bonus and/or if the Executive ceased to be a Director or employee due to gross misconduct.
Opportunity[3]	Bonus for achieving target level of performance as a percentage of salary is: • CEO – 200 per cent • CUO – 175 per cent (note this is not currently an Executive Director position) • CFO – 150 per cent Maximum opportunity is two times target. Note for 2015: The Committee may set bonus opportunities less than the amounts set out above – see Implementation of Policy section of the Annual Report on Remuneration.
Performance Metrics	**Financial Performance** The financial component is based on the Company's key financial measures of performance. For any year, these may include RoE, growth in BVS, combined ratio, investment return or any other financial KPI[4]. A sliding scale of targets applies for financial performance targets. Bonus is earned on an incremental basis once a predetermined threshold level is achieved. 25 per cent of the total bonus opportunity is payable for achieving threshold/median rising to maximum bonus for stretch/upper quartile performance. The degree of stretch in targets may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year. **Personal Performance** Personal performance is based upon achievement of clearly articulated objectives. A performance rating is attributed to participating Executive Directors, which determines the pay-out for this part of the bonus. The weightings applying to the bonus measures and the degree of stretch in objectives may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year. For Executive Directors, the financial component will have a higher weighting than the personal element.

Long Term Incentives (LTI)	
Purpose and Link to Strategy	Rewards Executive Directors for achieving superior returns for shareholders over a longer-term timeframe. Enables Executive Directors to build a meaningful shareholding over time and align goals with shareholders.
Operation[2,4]	RSS awards are made annually in the form of nil cost options with vesting dependent on the achievement of performance conditions over at least three financial years, commencing with the year of grant. This three year period is longer than the typical pattern of loss reserve development on the Group's insurance business, which is approximately two years. The number of awards will normally be determined by reference to the share price at 1 January in the year of grant unless the Committee at its discretion determines otherwise. The Remuneration Committee considers carefully the quantum of awards each year to ensure that they are competitive in light of peer practice and the targets set. Awards are subject to claw back if there is a material misstatement in the Company's financial statements, an error in the calculation of any performance conditions or if the Executive Director ceases to be a Director or employee due to gross misconduct. A dividend equivalent provision operates enabling dividends to be accrued (in cash or shares) on RSS awards up to the point of exercise.
Opportunity	Award levels are determined primarily by seniority. A maximum individual grant limit of 350 per cent of salary applies.
Performance Metrics	Awards vest at the end of a three year performance period based on performance measures reflecting the long-term strategy of the business at the time of grant. These may include measures such as TSR, RoE/BVS, Company profitability or any other relevant financial measures[1]. If more than one measure is used, the Committee will review the weightings between the measures chosen and the target ranges prior to each LTI grant to ensure that the overall balance and level of stretch remains appropriate. A sliding scale of targets applies for financial metrics with no more than 25 per cent vesting at threshold performance. For TSR, none of this part of the award will vest below median ranking and full vesting will require upper quartile performance or better. Awards vest on a proportionate basis for performance between the median and upper quartiles.

Share Ownership Guidelines[5]
Under the guidelines, the CEO is expected to maintain an interest equivalent in value to no less than two times salary over time. For other Executive Directors the threshold is one times salary. Until such time as the guideline threshold is achieved Executive Directors are required to retain no less than 50 per cent of the net of tax value of awards that vest under the RSS.

Chairman and Non-Executive Directors' (NEDs) fees	
Purpose and Link to Strategy	Helps recruit, motivate and retain a Chairman and Non-Executive Directors of a high calibre by offering a market competitive fee level.
Operation	The Chairman is paid a fee for his responsibilities as Chairman and also receives a separate fee for his position as Chairman of LUK. The level of these fees is reviewed periodically by the Committee and the CEO by reference to broadly comparable businesses in terms of size and operations. In general, the Non-Executive Directors are paid a single fee for all responsibilities, although supplemental fees may be payable where additional responsibilities are undertaken.
Opportunity	No maximum.

Notes

(1) The Committee operates the annual bonus plan and RSS according to their respective rules and in accordance with the Listing Rules. The Committee, consistent with normal market practice, retains discretion over a number of areas relating to the operation and administration of these plans and this discretion forms part of this policy.

(2) All historic awards that were granted under any current or previous share schemes operated by the Company but remain outstanding remain eligible to vest based on their original award terms and this provision forms part of the policy.

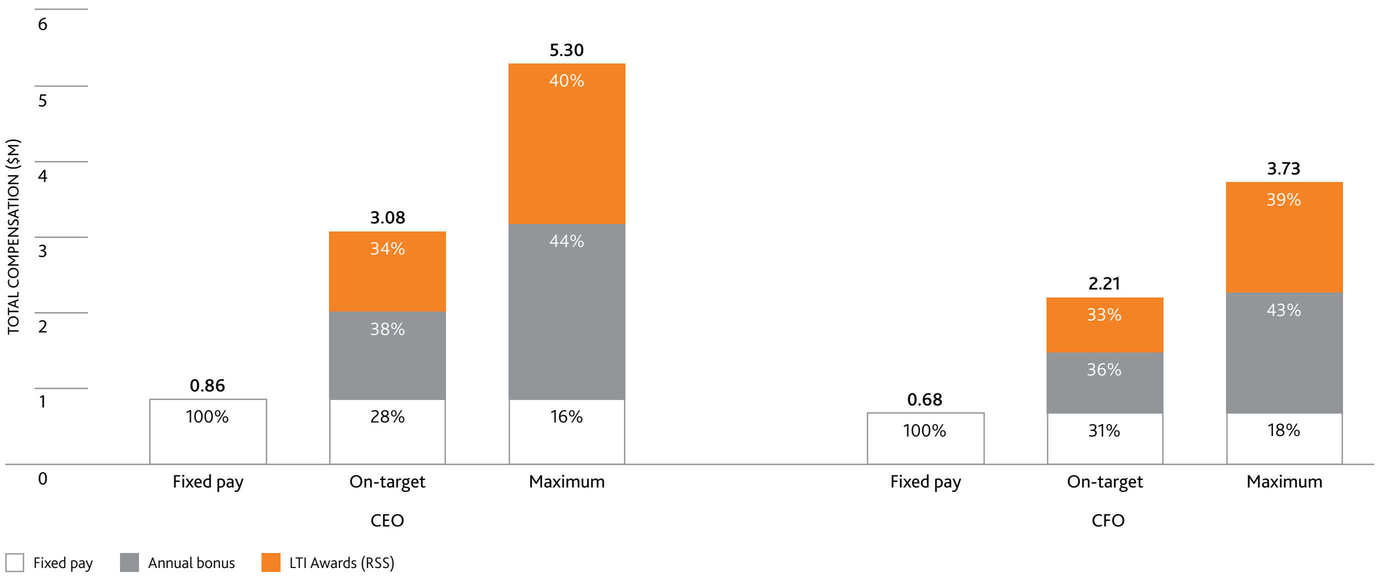
(3) The target bonuses set at the 2014 AGM in this policy were based on the incumbents in the roles at the time.

(4) Performance Measures; these may include the performance indicators shown on pages 20 to 21 or others described within the Annual Report Glossary commencing on page 160.

(5) Share Ownership interest equivalent is defined as wholly owned shares or fully vested rights over shares; since November 2014 unvested annual RSS bonus awards do not count towards share ownership.

ILLUSTRATIONS OF ANNUAL APPLICATION OF REMUNERATION POLICY

The charts below show the potential total remuneration opportunities for the Executive Directors in 2015 at different levels of performance under the policy.



Fixed pay = 2015 Salary + Actual value of 2014 Benefits + 2015 Pension Contribution.

On-target = Fixed Pay + Target Bonus (being half the Maximum Bonus Opportunity) + Target Value of 2015 RSS grant (assuming 50 per cent vesting with face values of 275 per cent and 276 per cent of salary for the CEO and CFO respectively).

Maximum = Fixed Pay + Maximum Bonus Opportunity + Maximum Value of 2015 RSS grant (assuming 100 per cent vesting shown as the face value of grant).

No account has been taken of any share price growth or dividend equivalents accrual.

APPROACH TO RECRUITMENT REMUNERATION

The remuneration package for a new Executive Director would be set in accordance with the terms of the Company's prevailing approved Remuneration Policy at the time of appointment and take into account the skills and experience of the individual, the market rate for a candidate of that experience and the importance of securing the relevant individual.

Salary would be provided at such a level as is required to attract the most appropriate candidate. The annual bonus and LTI potential would be in line with the Policy. In addition, the Committee may offer additional cash and/or share based elements to replace deferred or incentive pay forfeited by an executive leaving a previous employer. It would seek to ensure, where possible, that these awards would be consistent with awards forfeited in terms of vesting periods, expected value and performance conditions.

For an internal Executive Director appointment, any variable pay element awarded in respect of the prior role may be allowed to pay out according to its terms, adjusted as relevant to take into account the appointment. In addition, any other ongoing remuneration obligations existing prior to appointment may continue.

The Committee may agree that the Company will meet certain relocation expenses as appropriate.

SERVICE CONTRACTS AND LOSS OF OFFICE PAYMENT POLICY FOR EXECUTIVE DIRECTORS

Executive Directors have service contracts with six month notice periods. In the event of termination, the Executive Directors' contracts provide for compensation up to a maximum of base salary plus the value of benefits to which the Executive Directors are contractually entitled for the unexpired portion of the notice period. No Executive Director has a contractual right to a bonus for any period of notice not worked.

The Company seeks to apply the principle of mitigation in the payment of compensation on the termination of the service contract of any Executive Director. There are no special provisions in the service contracts for payments to Executive Directors on a change of control of the Company.

In the event of an exit of an Executive Director, the overriding principle will be to honour contractual remuneration entitlements and determine on an equitable basis the appropriate treatment of deferred and performance linked elements of the package, taking account of the circumstances. Failure will not be rewarded.

Depending on the leaver classification, an Executive Director may be eligible for certain payments or benefits continuation after cessation of employment.

If an Executive Director resigns or is summarily dismissed, salary, pension and benefits will cease on the last day of employment and there will be no further payments.

LEAVER ON ARRANGED TERMS OR GOOD LEAVER

If an Executive Director leaves on agreed terms, including compassionate circumstances, there may be payments after cessation of employment. Salary, pension and benefits will be paid up to the length of the agreed notice period or agreed period of gardening leave.

Subject to performance, a bonus may be payable at the discretion of the Committee pro-rata for the portion of the financial year worked.

Vested but unexercised deferred bonus shares will remain exercisable. Unvested deferred bonus shares will ordinarily vest in full, relative to the normal vesting period. All such vested awards must be exercised within 12 months of the vesting date. The Committee has discretion to permit such unvested awards to vest early rather than continue on the normal vesting timetable and also retains discretion, acting fairly and reasonably, as to whether or not to apply (or to apply to a lesser extent) the pro-rata reduction to the bonus shares where it feels the reduction would be inappropriate.

Vested but unexercised RSS awards may remain exercisable for 12 months. Unvested awards may vest on the normal vesting date unless the Committee determines that such awards shall instead vest at the time of cessation. Unvested awards will only vest to the extent that the performance conditions have been satisfied (over the full or curtailed period as relevant). A pro-rata reduction in the size of awards may apply, based upon the period of time after the grant date and ending on the date of cessation of employment relative to the three year vesting period.

Depending upon circumstances, the Committee may consider other payments in respect of an unfair dismissal award, outplacement support and assistance with legal fees.

TERMS OF APPOINTMENT FOR NON-EXECUTIVE DIRECTORS

The Non-Executive Directors serve subject to the Company's Bye-laws and under letters of appointment. They are appointed subject to re-election at the AGM and are also terminable by either party on six months' notice except in the event of earlier termination in accordance with the Bye-laws. The Non-Executive Directors are typically expected to serve for up to six years, although the Board may invite a Non-Executive Director to serve for an additional period. Their letters of appointment are available for inspection at the Company's registered office and at each AGM. The Company encourages share ownership by the Non-Executive Chairman and Non-Executive Directors, and Non-Executive Directors who do not own shares are encouraged to use a proportion of their fees to buy shares in the Company and retain such shareholdings for their remaining periods of office.

In accordance with best practice under the Code, the Board proposes to submit the Directors individually for re-election by the shareholders at the 2015 AGM.

ANNUAL REPORT ON REMUNERATION

This Annual Report on Remuneration together with the Chairman's Annual Statement, as detailed on page 44 will be subject to an advisory vote at the 2015 AGM. The information on page 69 with respect to Directors' Emoluments and onwards through page 78 has been audited.

IMPLEMENTATION OF REMUNERATION POLICY FOR 2015

In relation to the Policy described in the previous section, the following table sets out additional disclosure on the expected application of the Policy for 2015.

BASE SALARY AND FEES

Executive Directors

Increases and resulting salaries effective from 1 January 2015 are set out below:

- CEO – the incoming CEO's salary was set at $750,000 upon his promotion to CEO on 1 May 2014 and this was significantly lower than his predecessor's salary. The CEO's salary for 2015 was increased by 3 per cent to $772,500.
- CFO – salary increased by 3 per cent to $530,450.
- For 2015, increases of 3 per cent are in line with the salary increases across the general workforce population.

IMPLEMENTATION OF REMUNERATION POLICY FOR 2015 CONTINUED

Non-Executives

The Chairman's and Non-Executive Directors' fees remain the same for 2015:

- The fee for the Chairman is $325,000 per annum and the additional fee for the Chairman of LUK is $100,000.
- The Non-Executive Director fee is $175,000 per annum.

ANNUAL BONUS

For 2015, the CEO will have a target bonus of 150 per cent of salary and, therefore, a maximum opportunity of 300 per cent of salary which is within the approved policy limit and represents a 100 per cent of salary maximum opportunity reduction compared with the previous CEO. This lower bonus opportunity is driven off a significantly lower salary than the previous CEO's (as highlighted above). The CFO's target bonus opportunity will be in line with the policy at 150 per cent of salary (maximum 300 per cent).

As for 2014, the 2015 bonus will be based 75 per cent on financial performance and 25 per cent on personal performance.

Financial Performance (75 per cent)

The Company's most important financial KPI is Return on Equity which is the core indicator of the delivery of our strategic priorities of ensuring strong underwriting, effectively balancing risk and return and managing capital nimbly through the insurance cycle (see the strategic overview on pages 14 and 15 of this report). Accordingly, for 2015, the financial component comprises two parts – 60 per cent of this element is based on the performance of the Group's absolute RoE (measured as the internal rate of return of the change in the fully converted book value per share or 'FCBVS') plus dividends accrued and 40 per cent is based on the Group's relative RoE performance against appropriate peer companies (peer companies can be located on page 75). The RoE is to be adjusted for the effect of warrant exercises during the year.

- Absolute RoE:
  A sliding scale range of RoE targets is set with 25 per cent of bonus payable if the threshold level of increase in RoE is achieved (being 9 per cent), rising to 100 per cent of bonus target being payable for target growth in RoE of 11 per cent and 200 per cent of bonus target being payable for achieving the maximum RoE growth target of 19 per cent or higher. There is linear interpolation between these points. The Board considers that these target ranges are appropriately challenging in a difficult market and that the stretch target of 19 per cent would represent exceptional performance in the current market, but without encouraging excessive risk taking.
- Relative RoE:
  Relative performance will be measured against an identified comparator group of companies which can be seen on page 75. Vesting will be based on performance against a sliding scale with no vesting for below median performance, 25 per cent payable for achieving a median ranking, and up to 100 per cent for upper quartile or better. Vesting for performance in between the median and upper quartiles is determined on a proportionate basis.

Personal Performance (25 per cent)

This element of the bonus plan is based upon individual achievement of clearly articulated objectives created at the beginning of each year. The Committee has chosen not to disclose the personal performance objectives in advance as it considers them to be commercially sensitive. As in previous years there will be broad disclosure retrospectively in the 2015 Annual Report on Remuneration.

RESTRICTED SHARE SCHEME

Performance Conditions

2015 RSS awards are subject to RoE and relative TSR performance conditions. These metrics were chosen as RoE provides a focus on the Company's underlying financial performance and cycle management, and relative TSR provides an objective reward for stock market performance against the Company's peers.

Weighting

For 2015, the TSR/RoE weighting is 25 per cent on TSR and 75 per cent on RoE.

Target ranges

The RoE target range for 2015 awards is unchanged from the previous year:

- threshold – average RoE compared to the 13 week Treasury bill rate + 6 per cent;
- maximum – average RoE compared to the 13 week Treasury bill rate + 15 per cent; and
- none of the award will vest if RoE is below threshold, 25 per cent of the award will vest at threshold, and 100 per cent of the award will vest at maximum. Performance between threshold and maximum is determined on a straight-line basis.
- The Board and Committee consider that given current market conditions the stretch target represents exceptional and consistent cross cycle out-performance above the Group's stated strategic cross-cycle return of risk free plus 13 per cent. The target range closely aligns the longer term remuneration of our Executive Directors with consistent out-performance and the interests of our shareholders, but is not so stretching as to encourage excessive risk taking.

TSR target for 2015 awards:

Lancashire's TSR is compared against a comparator group comprising 11 peer companies as disclosed on page 75.

- 0 per cent will vest for a below median ranking;
- 25 per cent of the award will vest if Lancashire's performance is at the median; and
- 100 per cent will vest for upper quartile and above performance.
- vesting will be on a proportionate basis for performance between median and upper quartile.

Award levels

The CEO's RSS award level is less than his predecessor's. 2015 RSS award levels are as follows:

- CEO – 244,208 shares (275 per cent of salary);
- CFO – 168,149 shares (276 per cent of salary).

The number of shares awarded was determined based on the share price at 1 January 2015.

SINGLE FIGURE ON REMUNERATION

The following table presents the Executive Directors' emoluments in U.S. Dollars in respect of the year ended 31 December 2014.

Executive Directors		Salary $	Pension $	Taxable Benefits[1,6] $	Annual Bonus[7] $	Long-Term Incentives (RSS)[2,3] $	Other[9] $	Total[4] $
Alex Maloney[4,5], CEO	**2014**	**675,181**	**78,573**	**9,620**	**1,115,918**	**1,205,919**	**–**	**3,085,211**
	2013	453,534	86,830	13,279	1,366,703	4,065,805	–	5,986,151
Elaine Whelan[4], CFO	**2014**	**518,117**	**51,500**	**95,738**	**772,390**	**474,119**	**–**	**1,911,864**
	2013	499,865	50,000	107,913	1,158,675	1,399,685	–	3,216,138
Richard Brindle[4,8], Former CEO	**2014**	**368,576**	**36,858**	**7,127**	**1,180,355**	**4,690,533**	**644,914**	**6,928,363**
	2013	1,110,226	111,023	29,476	3,541,067	5,383,381	–	10,175,173

(1) Benefits comprise Bermudian payroll taxes, social insurance, medical, dental and vision coverage and housing and other allowances paid by the Company for expatriates (as is the case for the CFO), but exclude UK National Insurance contributions.

(2) For 2014, the long-term incentive values are based on the 2012 RSS awards which vest at 50 per cent on 12 February 2015 and are based on a 3 year performance period that ended on 31 December 2014. The values are based on the share price at 31 December 2014 and include the value of dividends accrued on vested shares.

(3) For 2013, the long-term incentive values are based on the 2011 RSS awards which vested at 100 per cent on 13 February 2014 and are based on a 3 year performance period that ended on 31 December 2013. The values include dividends that have accrued on vested shares.

(4) Some amounts were paid in pounds sterling and converted at the average exchange rate for the year of 1.6544.

(5) Alex Maloney's base salary and pension reflect his UK salary sacrifice pension contributions arrangement and are calculated at 4 months in his post as CUO (at an annual rate of $515,000) and 8 months as CEO (at an annual rate of $750,000).

(6) Elaine Whelan's taxable benefits have been restated to reflect the Bermudian payroll tax and social insurance portion that she received in 2013 and 2014, which was paid by the Company and considered an employee benefit. All employees in Bermuda are eligible for this benefit.

(7) For 2014 the Lancashire Group delivered solid results in a challenging market. Bonus targets were set at the beginning of 2014 and based on a clear split between Company financial performance and personal performance on a 75:25 (70:30 for the CFO in 2013) basis. Company financial performance had two components, absolute financial performance and relative financial performance weighted 60:40 respectively. The absolute component paid out at 138.86 per cent of target as the warrant adjusted RoE was 14.7 per cent against a warrant adjusted budget of 9.9 per cent and the relative component is provisionally cited at 0 per cent pending the final audited results of peer companies needed in order to calculate the final bonus payable. For the personal element of Executive Directors' bonus opportunity the pay-out ranged from 86 per cent to 75 per cent of the maximum. For full details of Executive Directors' bonuses and the associated performance delivered see pages 70 and 71.

(8) Richard Brindle retired from the Group and as a Director on 30 April 2014. Mr Brindle was afforded good leaver status and all RSS award interests were agreed to vest upon his departure using estimated TSR and RoE values at the time of his retirement. The amounts in the table above reflect all awards vesting in 2014. Further particulars of the vesting appear on page 72.

(9) For 2014 this includes all payments made to Mr Brindle in lieu of his six month notice period and converted at the exchange rate of 1.6885 as at 30 April 2014. Further particulars of the vesting appear on page 72.

NON-EXECUTIVE DIRECTORS' FEES

Current Non-Executive Directors		Fee $	Other $	Total $
Peter Clarke[1]	**2014**	**98,077**	**–**	**98,077**
	2013	–	–	–
Emma Duncan	**2014**	**175,000**	**–**	**175,000**
	2013	175,000	–	175,000
Simon Fraser	**2014**	**175,000**	**–**	**175,000**
	2013	27,178	–	27,178
Samantha Hoe-Richardson	**2014**	**175,000**	**–**	**175,000**
	2013	150,096	–	150,096
Martin Thomas	**2014**	**325,000**	**100,000**	**425,000**
	2013	325,000	100,000	425,000

NON-EXECUTIVE DIRECTORS' FEES CONTINUED

Former Non-Executive Directors		Fee $	Other $	Total $
John Bishop[2]	**2014**	**58,333**	**–**	**58,333**
	2013	175,000	–	175,000
Neil McConachie[2]	**2014**	**58,333**	**–**	**58,333**
	2013	175,000	–	175,000
Ralf Oelssner[2]	**2014**	**58,333**	**10,000**	**68,333**
	2013	175,000	56,000	231,000
Robert Spass[3]	**2014**	**175,000**	**–**	**175,000**
	2013	175,000	–	175,000
William Spiegel[3]	**2014**	**175,000**	**–**	**175,000**
	2013	175,000	–	175,000

(1) Peter Clarke was appointed as a Non-Executive Director with effect from 9 June 2014.

(2) John Bishop, Neil McConachie, and Ralph Oelssner retired from the Board on 30 April 2014 and were not proposed for re-election at the 2014 AGM.

(3) Robert Spass and William Spiegel retired from the Board on 31 December 2014.

2015 ANNUAL BONUS PAYMENTS IN RESPECT OF 2014 PERFORMANCE

As detailed in the Policy Report, each Executive Director participates in the annual bonus plan, under which performance is measured over a single financial year.

The target value of bonus is 150 per cent of salary for the current CEO (it was 175 per cent for the period between 1 January 2014 to 30 April 2014, during his time as Group CUO) and CFO respectively, and the maximum payable was two times the target value. The warrant adjusted RoE is 14.7 per cent, which reflects the total impact of warrants of 0.8 per cent on the actual 2014 RoE of 13.9 per cent. In setting the annual bonus RoE targets for 2014 the Committee agreed that the effect of warrant exercises should be excluded for annual bonus purposes due to the large number of warrants outstanding and potential volatile impact on the annual bonus performance metrics.

FINANCIAL PERFORMANCE

75 per cent of the 2014 bonus was based on Company performance conditions and the extent to which they were achieved is as follows:

Performance Measures	Weighting (of total Company element of 75%) %	Threshold %	Target %	Max %	Actual performance %	% vesting
Absolute RoE	60	9	12	19	14.7	138.86 of Target
Relative RoE	40	50	N/A	75	0	0 of Target
Total	100 (75 per cent of Total Bonus)					83.3 of Target payable in respect of Company performance

For 2014, the Lancashire Group delivered solid results in a challenging market. The absolute component paid out at 138.86 per cent of target as the warrant adjusted RoE was 14.7 per cent against a warrant adjusted target of 9.9 per cent and the relative component against the results of peer companies is provisionally stated below median (0 per cent pay out) pending the final audited results of peer companies needed in order to calculate the final bonus payable.

PERSONAL PERFORMANCE

25 per cent of the 2014 bonus was based on performance against clearly defined personal objectives set at the start of the year.

The table below sets out a summary of the 2014 personal objectives for each Executive Director.

Executive Director	Personal Performance
Alex Maloney	Effective leadership and management of the senior executive team and Group. Development of the general business strategy. Contribution aligned to the Lancashire Values.
Elaine Whelan	Effective leadership and management of the finance function and the Bermuda office. Development of the general business strategy. Contribution aligned to the Lancashire Values.

The personal targets were broadly common among the Executive Directors, with variances being attributable to the specifics of their respective roles and the perceived need for areas of personal development within their fields of expertise to be emphasised.

During the 2014 annual performance reviews of each Executive Director, a performance rating was assigned to determine the level of bonus pay-out each Executive Director was eligible for.

As expected for a solid performance year in a challenging market, the Executive Directors each achieved a high performance rating against their objectives. For the 2014 performance against personal objectives the following ratings were determined, expressed as a percentage of the maximum award for personal performance: CEO – 86 per cent, and CFO – 75 per cent.

A table of performance measures and total 2014 bonus achievement is set out below:

Executive Director	Financial performance (max % of total bonus) %	Personal performance (max % of total bonus) %	Bonus % of maximum awarded for 2014 %	Total[1] bonus value $	Value of bonus paid in cash (75 per cent of total bonus) $	Value of bonus deferred into RSS (25 per cent of total bonus)[2] $
Alex Maloney[3]	75	25	53	1,115,918	836,938	278,980
Elaine Whelan	75	25	50	772,390	579,292	193,098
Richard Brindle[4]	75	25	77	1,180,355	1,180,355	0

(1) For 2014 the Lancashire Group delivered solid results in a challenging market. Bonus targets were set at the beginning of 2014 and based on a clear split between Company financial performance and personal performance on a 75:25 (70:30 for the CFO in 2013) basis. Company financial performance had two components, absolute financial performance and relative financial performance weighted 60:40 respectively. The absolute component paid out at 138.86 per cent of target as the warrant adjusted RoE was 14.7 per cent against a warrant adjusted budget of 9.9 per cent and the relative component is provisionally cited at 0 per cent pending the final audited results of peer companies needed in order to calculate the final bonus payable. For the personal element of Executive Directors' bonus opportunity the pay-out ranged from 86 per cent to 75 per cent of the maximum. For full details of Executive Directors' bonuses and the associated performance delivered see page 70.

(2) 25 per cent of total bonus award will be deferred into Lancashire shares with one third vesting annually, each year, over a three-year period with the first third becoming exercisable in February 2016, subject to the Company being in an 'open period'. These awards vest on the relevant dates subject to continued employment only.

(3) Alex Maloney had a split role in 2014 and his bonus was calculated based on 4 months in his former role of CUO and 8 months of the year in his role as CEO.

(4) Richard Brindle retired from the Company effective 30 April 2014. Mr Brindle's annual bonus award was evaluated at the time of his retirement, and his 2013 performance was used as a proxy for the calculation of the 2014 bonus element and pro-rated for his time in office. Mr Brindle's total bonus payment was made in cash with no element deferred into RSS.

LONG-TERM SHARE AWARDS WITH PERFORMANCE PERIODS ENDING IN THE YEAR – 2012 RSS AWARD

The 2012 RSS awards are based on a three year performance period ending on 31 December 2014 and vest following the determination of financial results by the Board. The tables below set out the achievement against the performance conditions attached to the award, resulting in aggregate vesting of 50 per cent, and the actual number of awards vesting (with their estimated value).

	TSR (relative to a comparator group of 11 companies)		Average annual RoE (over 3 years in excess of 13 Week Treasury Bill Rate)	
Performance level	Performance required	% vesting	Performance required (%)	% vesting
Below threshold	Below median	0	Below 6	0
Threshold	Median	25	6	25
Stretch or above	Upper quartile or above	100	15 or above	100
Actual achieved		0	16.5	100

Details of the performance RSS awards granted on 28 February 2012 and 4 May 2012 with a performance period of 1 January 2012 – 31 December 2014 vesting for each Director, based on the above vesting, are shown in the table below:

Executive[3]	Number of shares at grant	Number of shares to lapse	Number of shares to vest	Dividend accrual on vested shares value[2] $	Value of shares including dividend accrual[1] $
Alex Maloney	187,165	93,582	93,583	391,837	1,205,919
Elaine Whelan	73,586	36,793	36,793	154,055	474,119

(1) The value of the vested shares is based on the share price on the date of vesting, being $8.69 (based on the exchange rate of 1.5534) on 31 December 2014. The vested awards are subject to the claw back provision set out on page 65.

(2) Dividends accrue on awards at the date of a dividend payment and upon exercise the cash value of the accrued dividends is paid to the employee on the number of vested awards.

(3) Details of Mr Brindle's award can be found in the Payments for Loss of Office section.

SCHEME INTERESTS AWARDED DURING THE YEAR

The table below sets out the performance RSS share awards that were granted as nil-cost options on 19 February 2014.

Executive	Grant Date[2]	Number of awards granted during the year	Face value of awards granted during the year[1,3] $	% vesting at threshold performance
Alex Maloney	19 February 2014	124,333	1,523,328	25
Elaine Whelan	19 February 2014	102,989	1,261,821	25
Richard Brindle	19 February 2014	207,938	2,547,656	25

(1) The share price on the date of performance awards grant was $12.25, when the RSS share awards were granted as nil-cost options.

(2) These awards are due to vest subject to performance conditions being met at the end of the performance period ending 31 December 2016 and becoming exercisable after the meeting of the Board in February 2017.

(3) The exercise share price is determined once an award has vested on the basis of the share price on the date an award is exercised.

LOSS OF OFFICE PAYMENTS

RETIREMENT ARRANGEMENTS FOR RICHARD BRINDLE

Richard Brindle retired from the Group as a Director on 30 April 2014 (the "departure date"), being the date his employment ceased and the date he relinquished his Executive Director responsibilities, although restrictive covenants based on those in his service contracts remained in effect. The details of Mr Brindle's retirement arrangements are included in the section below, as previously set forth in the FAQs on the Company website since 2 June 2014. As part of the terms of his retirement arrangements, Mr Brindle was paid the GBP equivalent (after the deduction of income tax and employee's national insurance contributions) of:

- $572,887 salary in lieu of his entitlement to six months' notice as specified in his employment contract.
- $57,289 in respect of his entitlement to pension contribution during the notice period.
- $14,738 in respect of his entitlement to benefits during the notice period.
- $1,180,355 being the pro-rated bonus for the period he was employed in 2014. The bonus amount was calculated based on the Committee's assessment of the extent to which the performance targets had been met for which it used as a proxy Mr Brindle's 2013 annual bonus (which was then pro-rated to the period of the year under review worked). Mr Brindle did not receive a performance rating in 2014 as he was no longer an Executive Director at the end of the evaluation period.
- The Company also provided assistance with legal and advisor fees, paying the advisor firms directly. The amounts paid are below a de minimis threshold.

Mr Brindle also held interests in RSS awards. As a retiring CEO and in recognition of Mr Brindle's significant contribution as a founder of the Company, the Remuneration Committee agreed that Mr Brindle should be treated as a good leaver and that awards should not be prorated for time but should be subject to performance conditions, where relevant. Accordingly, and in line with the plan rules:

- 176,654 vested but unexercised RSS awards and vested but unexercised Deferred Bonus RSS awards were exercisable for 12 months following his departure date.
- 132,643 unvested Deferred Bonus RSS awards were released in full on the departure date.
- 668,910 outstanding Performance RSS awards vested early on the departure date and were tested for performance at that date. The relative TSR condition was measured up to the departure date and the RoE condition was based on the first quarter RoE for 2014 and projected for the rest of that financial year. The future years of vesting conditions were based on the Company's internal projected budget. Details of the TSR and RoE targets for Performance RSS can be found on page 75. Accordingly, awards vested as follows:
  - 120,132 vested under the 2012 award – 0 per cent for the TSR element, 100 per cent for RoE; overall vesting of 50 per cent
  - 156,556 vested under the 2013 award – 0 per cent for the TSR element, 94.6 per cent for RoE; overall vesting of 70.9 per cent
  - 129,442 vested under the 2014 award – 0 per cent for the TSR element, 83.0 per cent for RoE; overall vesting of 62.3 per cent

Dividend equivalents up to the departure date have accrued to Mr Brindle on vested awards.

LEAVING ARRANGEMENTS FOR NEIL MCCONACHIE

Neil McConachie was an Executive Director in 2012 until he resigned from his Executive Director position and remained in a Non-Executive Director capacity with the Company. No awards were made to Mr McConachie in his capacity as a Non-Executive Director. At its meeting held on 4 February 2014 the Remuneration Committee decided that in light of Mr McConachie's decision to resign from the Board as a Non-Executive Director at the 2014 AGM, it was appropriate to afford him 'good leaver' status for all vested and unvested RSS awards, subject to a non-compete requirement, to vest on the usual vesting date with no pro-rata calculation applied. His fees for 2014 are disclosed on page 70 and he did not receive any payment for loss of office.

OTHER LEAVING ARRANGEMENTS

John Bishop and Ralph Oelssner retired from the Board effective from the 2014 AGM and Robert Spass and William Spiegel retired from the Board on 31 December 2014. Their fees are disclosed on page 70 and no retiring Non-Executive Director received any payment for loss of office.

DETAILS OF ALL OUTSTANDING SHARE AWARDS

In addition to awards made during the 2014 financial year, the table below sets out details of all outstanding RSS awards held by Directors.

PERFORMANCE AND DEFERRED BONUS AWARDS UNDER THE NIL-COST OPTION RESTRICTED SHARE SCHEME (RSS)

		Grant date[1]	Exercise price	Awards held at 1-Jan-14	Awards granted during the period	Awards vested during the period	Awards lapsed during the period	Awards exercised during the period	Awards held at 31-Dec-14	End of performance period
Alex Maloney, Group CEO	Performance RSS	24-Feb-11	–	236,198	–	236,198	–	236,198	–	31-Dec-13
	Performance RSS	28-Feb-12	–	187,165	–	–	–	–	187,165	31-Dec-14
	Deferred Bonus RSS[5]	5-Mar-12	–	8,969	–	4,484	–	4,484	4,485	
	Performance RSS	28-Feb-13	–	131,969	–	–	–	–	131,969	31-Dec-15
	Deferred Bonus RSS[5]	5-Mar-13	–	17,543	–	5,847	–	5,848	11,695	
	Performance RSS	19-Feb-14	–	–	124,333	–	–	–	124,333	31-Dec-16
	Deferred Bonus RSS[5]	5-Mar-14	–	–	29,430	–	–	–	29,430	
Total				**581,844**	**153,763**	**246,529**	**–**	**246,530**	**489,077**	
Elaine Whelan, Group CFO & LICL CEO	Performance RSS	25-Mar-10	–	45,581	–	–	–	45,581	–	31-Dec-12
	Performance RSS	24-Feb-11	–	81,313	–	81,313	–	81,313	–	31-Dec-13
	Deferred Bonus RSS[5]	24-Feb-11	–	3,005	–	–	–	3,005	–	
	Performance RSS	28-Feb-12	–	48,586	–	–	–	–	48,586	31-Dec-14
	Deferred Bonus RSS[5]	5-Mar-12	–	12,897	–	5,159	–	7,738	5,159	
	Performance RSS – Interim	4-May-12	–	25,000	–	–	–	–	25,000	31-Dec-14
	Performance RSS	28-Feb-13	–	116,087	–	–	–	–	116,087	31-Dec-15
	Deferred Bonus RSS[5]	5-Mar-13	–	15,120	–	5,040	–	5,040	10,080	
	Performance RSS	19-Feb-14	–	–	102,989	–	–	–	102,989	31-Dec-16
	Deferred Bonus RSS[5]	5-Mar-14	–	–	23,956	–	–	–	23,956	
Total				**347,589**	**126,945**	**91,512**	**–**	**142,677**	**331,857**	

PERFORMANCE AND DEFERRED BONUS AWARDS UNDER THE NIL-COST OPTION RESTRICTED SHARE SCHEME (RSS) CONTINUED

Former Directors		Grant date[1]	Exercise price	Awards held at 1-Jan-14	Awards granted during the period	Awards vested during the period	Awards lapsed during the period	Awards exercised during the period	Awards held at 30-Apr-14	End of performance period
Richard Brindle[6], Former Group CEO	Performance RSS	24-Feb-11	–	312,741	–	312,741	–	176,655	136,086	31-Dec-13
	Performance RSS[7]	28-Feb-12	–	240,263	–	120,132	120,131	–	120,132	31-Dec-14
	Deferred Bonus RSS[5]	5-Mar-12	–	43,414	–	43,414	–	–	43,414	
	Performance RSS[8]	28-Feb-13	–	220,709	–	156,556	64,153	–	156,556	31-Dec-15
	Deferred Bonus RSS[5]	5-Mar-13	–	56,584	–	56,584	–	–	56,584	
	Performance RSS[9]	19-Feb-14	–	–	207,938	129,442	78,496	–	129,442	
	Deferred Bonus RSS[5]	5-Mar-14	–	–	73,213	73,213	–	–	73,213	
				873,711	**281,151**	**892,082**	**262,780**	**176,655**	**715,427**	
Neil McConachie[10], Former Non-Executive Director	Performance RSS	24-Feb-11	–	261,994	–	261,994	–	–	261,994	31-Dec-13
	Performance RSS	28-Feb-12	–	146,833	–	–	–	–	146,833	31-Dec-14
	Deferred bonus RSS[5]	5-Mar-12	–	17,257	–	8,628	–	–	17,257	
	Deferred bonus RSS[5]	5-Mar-13	–	7,664	–	2,555	–	–	7,664	
				433,748	**–**	**273,177**	**–**	**–**	**433,748**	

(1) The market values of the common shares on the dates of grant were:

- 25 March 2010 £4.86
- 24 February 2011 £6.00
- 28 February 2012 £7.90
- 5 March 2012 £7.58
- 4 May 2012 £7.99
- 28 February 2013 £9.09
- 5 March 2013 £9.08
- 19 February 2014 £7.34
- 5 March 2014 £7.26

(2) The vesting of the RSS performance awards prior to 2013 grants is subject to two performance conditions as follows:

- Half of each award is subject to a performance condition measuring the TSR performance of the Company against the TSR performance of a select group of comparator companies (see page 75 for a list of comparator companies for each grant year), over a three-year performance period. 25 per cent of this half of the award vests for median performance by the Company, rising to 100 per cent vesting of this half of the award for upper quartile performance by the Company or better (with proportionate vesting between these two points).
- The other half of each award is subject to a performance condition based on average annual RoE over a three-year performance period. 25 per cent of this half of the award will vest if average annual RoE over the performance period exceeds the criteria set out in the table on page 75, whilst all of this part of the award will vest if the Company's average RoE is equal to the more stringent criteria set out in the table on page 75. Between these two points vesting will take place on a straight-line basis from 25 per cent to 100 per cent for RoE performance.

(3) The vesting of the RSS performance awards from 2013 grants forward is subject to two performance conditions as follows:

- 25 per cent of each award is subject to a performance condition measuring the TSR performance of the Company against the TSR performance of a select group of comparator companies (see page 75 for a list of comparator companies for each grant year), over a three-year performance period. 25 per cent of this half of the award vests for median performance by the Company, rising to 100 per cent vesting of this half of the award for upper quartile performance by the Company or better (with proportionate vesting between these two points).
- The other 75 per cent of each award is subject to a performance condition based on average annual RoE over a three-year performance period. 25 per cent of this half of the award will vest if average annual RoE over the performance period exceeds the criteria set out in the table on page 75, whilst all of this part of the award will vest if the Company's average RoE is equal to the more stringent criteria set out in the table on page 75. Between these two points vesting will take place on a straight-line basis from 25 per cent to 100 per cent for RoE performance.

(4) The vesting dates of the RSS mainstream awards are subject to being out of a close period and, for the 2010 to 2014 performance awards, are as follows:

- 2010 – 21 February 2013;
- 2011 – 13 February 2014;
- 2012 – 12 February 2015;
- 2013 – first open period following the release of the Company's 2015 year-end results; and
- 2014 – first open period following the release of the Company's 2016 year-end results.

(5) The vesting dates of the RSS Deferred Bonus awards are subject to being out of a close period and, for the 2012 to 2014 Deferred Bonus awards, are as follows:

- 2012 – vest 33.33 per cent over a three year period at the first open period following the release of the Company's year-end results 2012, 2013 and 2014;
- 2013 – vest 33.33 per cent over a three year period at the first open period following the release of the Company's year-end results 2013, 2014 and 2015; and
- 2014 – vest 33.33 per cent over a three year period at the first open period following the release of the Company's year-end results 2014, 2015 and 2016.

(6) Richard Brindle retired from the Group and as a Director on 30 April 2014. Mr Brindle was afforded good leaver status and all RSS award interests were agreed to vest upon his departure using estimated TSR and RoE values at the time of his retirement. The amounts in the table above reflect all awards vesting in 2014. Further particulars of the vesting appear on page 72.

(7) Mr Brindle's 2012 performance award was vested in line with the plan rules using estimated TSR and RoE values at the time of his retirement. Vesting was based on 0 per cent vesting for the TSR element and 100 per cent for the RoE element; an overall vesting of 50 per cent.

(8) Mr Brindle's 2013 performance award was vested in line with the plan rules using estimated TSR and RoE values at the time of his retirement. Vesting was based on 0 per cent vesting for the TSR element and 94.6 per cent for the RoE element; an overall vesting of 70.9 per cent.

(9) Mr Brindle's 2014 performance award was vested in line with the plan rules using estimated TSR and RoE values at the time of his retirement. Vesting was based on 0 per cent vesting for the TSR element and 83 per cent for the RoE element; an overall vesting of 62.3 per cent.

(10) Neil McConachie was an Executive Director until 30 June 2012. No awards have been made to Mr McConachie in his capacity as a Non-Executive Director. At its meeting held on 4 February 2014 the Remuneration Committee decided that in light of Mr McConachie's decision to resign from the Board as a Non-Executive Director at the 2014 AGM, it was appropriate to afford him 'good leaver' status for all vested and unvested RSS awards, subject to a non-compete requirement. Pro-ration remains subject to a final determination by the Remuneration Committee.

TSR TARGETS FOR RSS

	2011	2012	2013*	2014*	2015*
100%	75th percentile	75th percentile	75th percentile	75th percentile	75th percentile
25%	= median	= median	= median	= median	= median
Nil	< median	< median	< median	< median	< median

ROE TARGETS FOR RSS

	2011	2012	2013*	2014*	2015*
100%	13 week Tr + 15%	13 week Tr + 15%	13 week Tr +15%	13 week Tr +15%	13 week Tr +15%
25%	13 week Tr + 6%	13 week Tr + 6%	13 week Tr + 6%	13 week Tr + 6%	13 week Tr + 6%
Nil	<13 week Tr + 6%	<13 week Tr + 6%	<13 week Tr + 6%	<13 week Tr + 6%	<13 week Tr + 6%

* From 2013 onwards the split of targets has changed from 50 per cent RoE / 50 per cent TSR to 75 per cent RoE and 25 per cent TSR.

Peer Companies	2011 awards	2012 awards	2013 awards	2014 awards	2015 awards
Amlin plc	X	X	X	X	X
Argo Limited[1]		X	X	X	X
Aspen Insurance Holdings Limited	X	X	X	X	X
Axis Capital Holdings Limited	X	X	X	X	X
Beazley plc	X	X	X	X	X
Catlin Group Ltd.	X	X	X	X	X
Endurance Specialty Holdings Ltd.	X	X	X	X	X
Flagstone Reinsurance Holdings Limited[2]	X	X			
Hiscox Ltd.	X	X	X	X	X
Montpelier Re Holdings Ltd.	X	X	X	X	X
Renaissance Re Holdings Ltd.	X	X	X	X	X
Validus Holdings Ltd.	X	X	X	X	X

(1) Argo was used as a comparator company from the fourth quarter of 2012.

(2) Flagstone was acquired by Validus with effect from 30 November 2012 and so was used as a comparator company for 2012 up to 30 September 2012.

DIRECTORS' SHAREHOLDINGS AND SHARE INTERESTS

A policy for formal shareholding guidelines was introduced in 2012. This requires the CEO to build and maintain a shareholding in the Company worth two-times annual salary and for the CFO to build and maintain a shareholding of one times annual salary as set out in the Policy Report.

Details of the Directors' interests in shares are shown in the table below.

	Number of Ordinary Shares						
	At 1 January 2014	At 31 December 2014					
Director	Legally owned	Legally owned	Subject to deferral under the RSS	Subject to performance conditions under the RSS	Vested but unexercised awards under other share based plans	Total	Shareholding guideline achieved?
Alex Maloney	191,415	321,841	45,610	443,467	–	810,918	Yes
Elaine Whelan	94,225	233,820	39,195	292,662	–	565,677	Yes
Peter Clarke	–	–	N/A	N/A	N/A	–	N/A
Emma Duncan	–	–	N/A	N/A	N/A	–	N/A
Simon Fraser	–	–	N/A	N/A	N/A	–	N/A
Samantha Hoe-Richardson	3,947	3,947	N/A	N/A	N/A	3,947	N/A
Robert Spass	153,679	–	N/A	N/A	N/A	–	N/A
William Spiegel	–	–	N/A	N/A	N/A	–	N/A
Martin Thomas	6,950	6,950	N/A	N/A	N/A	6,950	N/A

Former Director	Number of Ordinary Shares At 1 January 2014 Legally owned	At 30 April 2014 Legally owned	Subject to deferral under the RSS	Subject to performance conditions under the RSS[3]	Vested but unexercised awards under other share based plans	Total	Shareholding guideline achieved?
John Bishop[2]	–	–	N/A	N/A	N/A	–	N/A
Richard Brindle[2]	858,022	858,022	173,211	542,216	6,413,442	7,986,891	Yes
Neil McConachie[2]	–	–	24,921	408,827	–	433,748	N/A
Ralf Oelssner[2]	–	–	N/A	N/A	N/A	–	N/A

(1) For the purpose of the shareholding guideline, legally owned shares are counted together with the net of tax value of deferred bonus and vested (but unexercised) long-term incentive awards.

(2) Richard Brindle retired from the Group and as a Director and John Bishop, Neil McConachie and Ralph Oelssner retired as Non-Executive Directors on 30 April 2014, therefore legal ownership of shares has only been tracked and reported for the relevant period.

(3) The awards for Richard Brindle reflect the performance conditions that were applied at the time of his retirement. Further details of the vesting can be found on page 72.

Warrants over the Company's shares were awarded to the Company's founders and management prior to the admission of the Company's shares to trading on AIM. Details of the Former CEO's awards, which were granted on 16 December 2005, are set out as below. Other Executive Directors had exercised their warrants prior to 2012.

Richard Brindle's Warrants held at 1 January 2014[2]	Warrants exercised during the period	Warrants sold during the period	Warrants held at 30 April 2014	Exercise price $	Date from which first exercisable[1]	Expiry date
46,260	–	–	46,260	5.00	16 Dec 2005	16 Dec 2015
3,718,912	–	–	3,718,912	5.00	16 Dec 2005	16 Dec 2015
288,843	–	–	288,843	5.00	31 Dec 2007	16 Dec 2015
1,906,305	–	–	1,906,305	3.90	16 Dec 2008	16 Dec 2015
47,155	–	–	47,155	3.90	31 Dec 2008	16 Dec 2015
405,967	–	–	405,967	2.60	31 Dec 2009	16 Dec 2015
6,413,442			6,413,442			

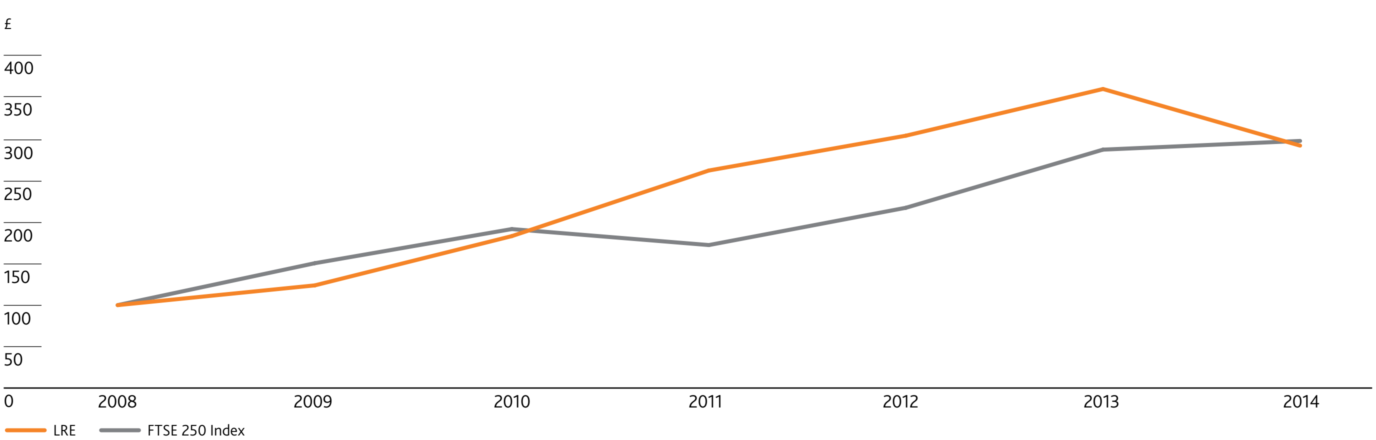
(1) There is a contractual obligation to make a dividend equivalent payment on each vested warrant. The value of dividend equivalents paid in respect of the above warrants to Richard Brindle in 2014 was £1,165,727 (2013 – £6,822,340).

(2) The market value of the common shares on 16 December 2005, the date of warrant grant, was £3.21.

PERFORMANCE GRAPH

The following graph shows the Company's performance, measured by TSR, compared with the performance of the FTSE 250 Index. The Company's common shares commenced trading on the main market of the LSE on 16 March 2009 and the Company joined the FTSE 250 Index on 22 June 2009 and is currently a constituent of this.

TOTAL SHAREHOLDER RETURN



Source: Thomson Reuters

This graph shows the value, by 31 December 2014, of £100 invested in Lancashire Holdings Limited on 31 December 2008 compared with the value of £100 invested in the FTSE 250 Index. The other points plotted are the values at intervening financial year-ends.

TOTAL REMUNERATION HISTORY FOR CEO

The table below sets out the total single figure remuneration for the CEOs over the last six years with the annual bonus paid as a percentage of the maximum and the percentage of long-term share awards vesting in the year. It should be noted that the current CEO was appointed 1 May 2014.

	2009	2010	2011	2012	2013	Richard Brindle 2014[1]	Alex Maloney 2014[2]
Total remuneration ($000s)	7,244	9,945	9,623	10,460	10,175	**9,391**	**2,169**
Annual bonus (%)	68	94	73	73	80	**80**	**53**
LTI vesting (%)	N/A	99.57	100	99	100	**61**[3]	**50**

(1) Richard Brindle retired from the Group and as a Director on 30 April 2014.

(2) Alex Maloney was appointed CEO effective 1 May 2014, after the retirement of Mr Brindle.

(3) Mr Brindle was afforded good leaver status and all RSS award interests were agreed to vest upon his departure, using estimated TSR and RoE values at the time of his retirement. The amounts in the table above reflect all awards vesting in 2014. Further particulars of the vesting appear on page 72.

The table above shows the total remuneration figure for the former CEO during each of those financial years; the current CEO is reflected for the current year only, from 1 May 2014, being the only year he has held the post to-date. The total remuneration figure includes the annual bonus and LTI awards which vested based on performance in those years. The annual bonus and LTI percentages show the pay-out for each year as a percentage of the maximum.

PERCENTAGE CHANGE IN CEO REMUNERATION

The following table sets out the percentage change in the aggregate value of salary, benefits and bonus for the Chief Executive from the preceding year and the average percentage change in respect of the employees of the Company taken as a whole.

	Year on year change CEO[1] %	Average year on year change employees[2] %
Base salary	-22	-22
Benefits[3]	-29	-70
Bonus	-44	-16

(1) A blended CEO rate is used for 2014 to account for CEO changes through the year.

(2) Employee numbers were calculated on a per head count basis as at 31 December 2013 and 31 December 2014. 2013 annual costs include the Lloyd's segment of the Company's costs from 7 November 2013 only, the date the acquisition of Cathedral completed.

(3) Fluctuations in foreign exchange rates and the Company's share price have attributed to the decrease in benefit costs in 2014, specifically to payroll taxes on equity compensation.

RELATIVE IMPORTANCE OF THE SPEND ON PAY

The following table sets out the percentage change in dividends and overall spend on pay in the year ending 31 December 2014 compared to the year ending 31 December 2013. The increase in employee remuneration costs is mainly attributed to inclusion of Cathedral employee remuneration costs being reported for the full year of 2014.

	2014 $m[1]	2013 $m	Percentage change %
Employee remuneration costs	**77.4**	59.4	30.3
Dividends	**321.0**	325.6	-1.4

(1) The total employee remuneration costs for 2013 includes the Lloyd's segment of the Company's costs from 7 November 2013, the date the acquisition of Cathedral completed.

COMMITTEE MEMBERS, ATTENDEES AND ADVICE

The Remuneration Committee comprised the following members during the year and to the date of this Report (all of whom are independent Non-Executive Directors):

Remuneration Committee Members	Position	Comments
Simon Fraser	LHL Remuneration Committee Chairman	Independent; Attended 6 of a potential maximum meetings of 6 in 2014
Peter Clarke	Member from 4 November 2014	Independent; No meetings held subsequent to appointment
Emma Duncan	Member from 5 November 2010	Independent; Attended 6 of a potential maximum meetings of 6 in 2014
Former Members		
Ralf Oelssner	Retired from Committee 30 April 2014	Independent; Attended 0 of a potential maximum meetings of 4 in 2014[1]
William Spiegel	Retired from Committee 31 December 2014	Independent; Attended 5 of a potential maximum meetings of 6 in 2014

(1) See note 7 on page 50.

The Remuneration Committee's responsibilities are contained in its Terms of Reference, a copy of which is available on the Company's website. These responsibilities include determining the framework for the remuneration, including pension arrangements, for all Executive Directors, the Chairman and senior executives. The Committee is also responsible for approving employment contracts for senior executives.

REMUNERATION COMMITTEE ADVISER

The Remuneration Committee is advised by NBS, a trading name of Aon Hewitt, being a subsidiary of Aon plc. NBS was appointed by the Remuneration Committee in 2007. NBS has discussions with the Remuneration Committee Chairman regularly on Committee process and topics which are of particular relevance to the Company.

Aon Benfield (which is part of Aon but is a separate business division to Aon Hewitt) provides reinsurance broking services to Lancashire.

The primary role of NBS is to provide independent and objective advice and support to the Committee's Chairman and members. In order to manage any possible conflict of interest, NBS operates as a distinct business within the Aon Group and there is a robust separation between the business activities and management of NBS and all other parts of Aon Hewitt and the wider Aon Group. The Committee is satisfied that the advice that it receives is objective and independent. NBS is also a signatory to the Remuneration Consultants Group ('RCG') Code of Conduct which sets out guidelines for managing conflicts of interest, and has confirmed to the Committee its compliance with the RCG Code.

The total fees paid to NBS in respect of its services to the Committee for the year ending 31 December 2014 were $160,691 (2013 – $174,004). Fees are predominantly charged on a 'time spent' basis.

ENGAGEMENT WITH SHAREHOLDERS

Details of votes cast for and against the resolution to approve last year's Remuneration Report and the Remuneration Policy are shown below and any matters discussed with shareholders during the year are provided in the Implementation Report starting on page 67.

	Vote to approve Directors' Remuneration Policy		Vote to approve Annual Report on Remuneration	
	Total number of votes	% of votes cast	Total number of votes	% of votes cast
For	132,963,855	90.1	102,131,849	69.9
Against	14,530,236	9.9	44,035,683	30.1
Total	147,494,091	100.0	146,167,532	100.0
Abstentions	554,388		1,880,947	

Approved by the Board of Directors and signed on behalf of the Board

SIMON FRASER
LHL REMUNERATION COMMITTEE CHAIRMAN
11 February 2015

OVERVIEW OF THE GROUP

Lancashire Holdings Limited (the Company) is a Bermuda incorporated company with operating subsidiaries in Bermuda, London and Lloyd's.

The Company's common shares were admitted to trading on AIM in December 2005 and were subsequently moved up to the Official List and to trading on the main market of the LSE on 16 March 2009. The shares have been included in the FTSE 250 index since 22 June 2009.

PRINCIPAL ACTIVITIES

The Company's principal activity, through its wholly owned subsidiaries, is the provision of global specialty insurance and reinsurance products. On 7 November 2013, the Company completed the acquisition of Cathedral Capital Limited, an established Lloyd's insurer, and in July 2013 set up Kinesis, a third-party capital and underwriting management facility, to complement Lancashire's longstanding specialty insurance activities. An analysis of the Group's business performance can be found in the Business review on pages 24 to 32.

DIVIDENDS

For the year ended 31 December 2014, the following dividends were declared:

- an interim dividend of $0.05 per common share and warrant was declared on 23 July 2014 and paid on 24 September 2014 in pounds sterling at the pound/U.S. dollar exchange rate of 1.6592 or £0.0301 per common share and warrant;
- a special dividend of $1.20 per common share and warrant was declared on 4 November 2014 and paid on 19 December 2014 in pounds sterling at the pound/U.S. dollar exchange rate of 1.5705 or £0.7641 per common share and warrant;
- a final dividend of $0.10 per common share and warrant was declared on 11 February 2015; and
- an additional special dividend of $0.50 per common share and warrant was declared on 11 February 2015.

Both the final dividend and the additional special dividend are to be paid on 15 April 2015 in pounds sterling at the pound/U.S. dollar exchange rate on the record date of 20 March 2015 or approximately £0.39 in the aggregate, per common share and warrant.

DIVIDEND POLICY

Lancashire intends to maintain a strong balance sheet at all times, while generating an attractive risk-adjusted total return for shareholders. We actively manage capital to achieve those aims. Capital management is expected to include the payment of a sustainable annual (interim and final) dividend, supplemented by special dividends from time to time. Dividends will be linked to past performance and future prospects.

Under most scenarios, the annual dividend is not expected to reduce from one year to the next. Special dividends are expected to vary substantially in size and in timing.

DIRECTORS

CURRENT DIRECTORS

- Peter Clarke (Non-Executive Director) (appointed effective 9 June 2014)
- Emma Duncan (Non-Executive Director)
- Simon Fraser (Senior Independent Non-Executive Director) (appointed SID effective 30 April 2014)
- Samantha Hoe-Richardson (Non-Executive Director)
- Alex Maloney (Chief Executive Officer) (appointed CEO effective 30 April 2014)
- Tom Milligan (Non-Executive Director) (appointed effective 3 February 2015)
- Martin Thomas (Non-Executive Chairman)
- Elaine Whelan (Chief Financial Officer)

DIRECTORS WHO RETIRED DURING THE YEAR

- John Bishop (Non-Executive Director) (retired effective 30 April 2014)
- Richard Brindle (Chief Executive Officer) (retired effective 30 April 2014)
- Neil McConachie (Non-Executive Director) (retired effective 30 April 2014)
- Ralf Oelssner (Senior Independent Non-Executive Director) (retired effective 30 April 2014)
- Robert Spass (Non-Executive Director) (retired effective 1 January 2015)
- William Spiegel (Non-Executive Director) (retired effective 1 January 2015)

DIRECTORS' INTERESTS

The Directors' beneficial interests in the Company's common shares as at 31 December 2014 and 2013 including interests held by family members were as follows:

Director	Common shares held at 31 December 2014	Common shares held at 31 December 2013
Peter Clarke	–	–
Emma Duncan	–	–
Simon Fraser	–	–
Samantha Hoe-Richardson	3,947	3,947
Alex Maloney[1]	321,841	191,415
Martin Thomas	6,950	6,950
Elaine Whelan[2]	233,820	94,225
Former Director		
John Bishop	N/A	–
Richard Brindle[3]	N/A	858,022
Neil McConachie	N/A	–
Ralf Oelssner	N/A	–
Robert Spass[4]	–	153,679
William Spiegel	–	–

There have been no changes in Directors' shareholdings between the end of the financial year and the date of this Report.

(1) Includes 100,000 shares owned by his spouse, Amanda Maloney. Alex Maloney conducted the following transactions in the Company's shares during 2014:

- 7 May – exercise of 236,198 RSS awards and 10,332 deferred bonus RSS awards and related sale of 116,104 shares to cover tax liabilities, at a price of £6.68 realising £775,269.

(2) Includes 2,600 shares owned by her spouse, Kilian Whelan. Elaine Whelan conducted the following transactions in the Company's shares during 2014:

- 7 May – exercise of 126,894 RSS awards and 15,783 deferred bonus RSS awards and related sale of 3,082 shares to cover tax liabilities, at a price of £6.68 realising £20,580.

(3) Richard Brindle conducted the following transactions in the Company's shares during 2014, prior to his retirement:

- 13 February – exercise of 176,655 RSS awards and subsequent sale of 176,655 shares at a price of £7.29 realising £1,287,902.

(4) Robert Spass conducted the following transactions in the Company's shares during 2014:

- 24/25 February – sold 153,679 shares at a price of $12.11 realising $1,860,385;
- 6 May – cashless exercise of 150,000 Founder warrants resulting in the acquisition of 85,536 shares; and
- 14 May – sold 85,536 shares at a price of £6.62 realising £566,077.

Two former Directors held warrants over the Company's shares which were awarded prior to the Company's admission to AIM in December 2005 along with other warrants awarded to the Company's founders and employees. At the time of his retirement on 31 December 2014 Robert Spass was the beneficial owner of 410,000 Founder warrants. Richard Brindle also held warrants at the time of his retirement on 30 April 2014 and further details of the Executive Directors' warrants are included in the Directors' Remuneration Report on page 76.

In November 2014, Richard Brindle sold the entirety of his 5.5 per cent shareholding in KCML to LHL and other existing KCML shareholders pursuant to the terms of the KCML subscripted shareholders' agreement. At the same time, Alex Maloney increased his shareholding in KCML from 1.1 per cent to 1.2 per cent. Following the transaction LHL owns 92.7 per cent of KCML, with the balance of the shares owned by senior Lancashire and KCML employees.

TRANSACTION IN OWN SHARES

The Company repurchased 2,498,433 of its own common shares from 8 September 2014 through 20 November 2014 for a total consideration of approximately $25.0 million. These repurchases were made pursuant to resolutions of the shareholders passed at the AGM held on 30 April 2014 granting authority for the repurchase of up to 18,544,580 shares. All of the repurchased shares were initially held in treasury.

The Group's current repurchase programme has 16,046,147 common shares remaining to be purchased at 31 December 2014 (approximately $139.6 million at the 31 December 2014 share price). The purpose of the Company's repurchase programme is to acquire shares to use in the future towards satisfying its obligations under both its RSS awards and the Company's warrants. The shares repurchased have been held as treasury shares. Further details of the share repurchase authority and programme are set out in note 23 to the consolidated financial statements on page 153. The repurchase programme is subject to renewal at the 2015 AGM in an amount of up to 10 per cent of the then issued common share capital.

The Company did not repurchase any of its own common shares during 2013.

DIRECTORS' REMUNERATION

Details of the Directors' remuneration are set out in the Directors' Remuneration Report on pages 61 to 78.

SUBSTANTIAL SHAREHOLDERS

As at 11 February 2015, the Company was aware of the following interests of 3 per cent or more in the Company's issued share capital:

Name	Number of shares as at 11 February 2015	% of shares in issue
Invesco Limited	27,364,567	14.4
Setanta Asset Management Limited	15,225,288	8.0
Woodford Investment Management LLP	13,286,694	7.0
Legal & General Group Plc	10,457,693	5.5
Franklin Mutual Advisers, LLC	9,772,203	5.2
Standard Life Investments (Holdings) Limited	8,655,337	4.6
Alken Luxembourg S.A.	6,632,554	3.5
BlackRock, Inc.	6,279,133	3.3

CORPORATE GOVERNANCE – COMPLIANCE STATEMENT

The Company's compliance with the Code is summarised in the Corporate Governance section of this Report on pages 49 to 51.

The Company confirms, in accordance with the principle of 'comply or explain', that there are no areas of material non-compliance with the Code.

DONATIONS

In November 2013, the Board of Directors approved a cash donation of $2,000,000 (2013 – $1,400,000) to the Lancashire Foundation, payable in respect of 2014.

Lancashire established the Lancashire Foundation as a Bermuda charitable trust in 2007, with the aim of creating a trust for the benefit of charitable causes in Bermuda, the UK and worldwide. During 2012, the assets of the Lancashire Foundation were transferred to the Lancashire Foundation charitable trust established in England and Wales and registered with the Charity Commission. The Lancashire Foundation's trustees are two senior employees, one former employee, a subsidiary non-executive director and the Group Chairman. The Trustees make donations following recommendations made by the Company's Donations Committee consisting of the Group's employees.

A summary of the work of the Lancashire Foundation during 2014 can be found in the Corporate Responsibility section on pages 38 to 41.

The Group did not make any political donations or expenditure during 2014 or 2013.

HEALTH AND SAFETY

The Group considers the health and safety of its employees to be a management responsibility equal to that of any other function.

The Group operates in compliance with health and safety legislative requirements in Bermuda and the UK.

GREENHOUSE GAS EMISSIONS

The Group's greenhouse gas emissions are detailed in the Corporate Responsibility section on pages 39 to 40.

EMPLOYEES

Lancashire is an equal opportunity employer, and does not tolerate unfair discrimination of any kind in any area of employment or corporate life. The Group believes that education and training for employees is a continuous process and employees are encouraged to discuss training needs with their managers. The Group's health and safety, equal opportunities, training and other policies are available to all employees in the staff handbook which is available on the Group's intranet.

CREDITOR PAYMENT POLICY

The Group aims to pay all creditors promptly and in accordance with contractual and legal obligations.

FINANCIAL INSTRUMENTS AND RISK EXPOSURES

Information regarding the Group's risk exposure is included in the risk disclosures section on pages 100 to 126 of the consolidated financial statements. The Group's use of derivative financial instruments can be found on pages 115 to 116.

ACCOUNTING STANDARDS

The Group's consolidated financial statements are prepared in accordance with accounting principles generally accepted under IFRS as adopted by the European Union. Where IFRS is silent, as it is in respect of the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, the Board determines appropriate measurement bases, to provide the most useful information to users of the consolidated financial statements, using their judgement and considering U.S. GAAP.

ANNUAL GENERAL MEETING

The notice of the 2015 AGM, to be held on 29 April 2015 at the Company's head office, 29th Floor, 20 Fenchurch Street, London EC3M 3BY, UK, is contained in a separate circular to shareholders enclosed with this Annual Report and Accounts. The notice of the AGM is also available on the Company's website.

ELECTRONIC AND WEB COMMUNICATIONS

Provisions of the Bermuda Companies Act 1981 enable companies to communicate with shareholders by electronic and/or website communications. The Company will notify shareholders (either in writing or by other permitted means) when a relevant document or other information is placed on the website and a shareholder may request a hard copy version of the document or information.

GOING CONCERN AND VIABILITY STATEMENT

The Business Review section on pages 24 to 32 sets out details of the Group's financial performance, capital management, business environment and outlook. In addition, further discussion of the principal risks and material uncertainties affecting Lancashire can be found on pages 36 to 37. Starting on page 100 the risk disclosures section of the consolidated financial statements set out the principal risks the Group is exposed to, including insurance, market, liquidity, credit, operational and strategic, together with the Group's policies for monitoring, managing and mitigating its exposures to these risks. The Board considers annually and on a rolling basis a three year strategic plan for the business which the Company progressively implements. The three-year strategic plan was last approved by the Board on 30 April 2014. The Board receives quarterly reports from the Chief Risk Officer and sets and approves risk tolerances for the business.

During 2014, the Board carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. The Directors believe that the Group is well placed to manage its business risks successfully, having taken into account the current economic outlook. Accordingly, the Board believes that, taking into account the Group's current position, and subject to the principal risks faced by the business, the Group will be able to continue in operation and to meet its liabilities as they fall due for the period up to 31 December 2016, being the period considered under the Group's current three-year strategic plan.

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue its operational existence for the foreseeable future and for a period of at least twelve months from the date of this report. Accordingly, the Board continues to adopt and consider appropriate the going concern basis in preparing the Annual Report and Accounts.

AUDITORS

Resolutions will be proposed at the Company's 2015 AGM to re-appoint Ernst & Young LLP as the Company's auditors and to authorise the Directors to set the auditors' remuneration. Ernst & Young have served as the Company's auditors since 2005.

The Company plans to perform an audit tender process during 2016 and to recommend an auditor to the shareholders to vote on at the 2017 AGM.

DISCLOSURE OF INFORMATION TO THE AUDITORS

Each of the persons who is a Director at the date of approval of this Annual Report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- the Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Approved by the Board of Directors and signed on behalf of the Board.

CHRISTOPHER HEAD
COMPANY SECRETARY
11 February 2015

The Directors are responsible for preparing the Annual Report and the Group's consolidated financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period. The consolidated financial statements have been prepared in accordance with IFRS. Where IFRS is silent, as it is in respect of the measurement of insurance products, U.S. GAAP is considered. Further detail on the basis of preparation is described in the consolidated financial statements. In preparing the consolidated financial statements, the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the Group's consolidated financial statements;
- provide additional disclosures where compliance with the specific requirements of IFRS are considered to be insufficient to enable users to understand the impact of particular transactions, events and conditions on the financial position and performance; and
- prepare the consolidated financial statements on the going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business.

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

DIRECTORS' RESPONSIBILITY STATEMENT

The Directors confirm that to the best of their knowledge:

1. the consolidated financial statements, prepared in accordance with IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Group;
2. the Board considers the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy; and
3. the Strategy and the Business review include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that the Group faces.

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

By order of the Board

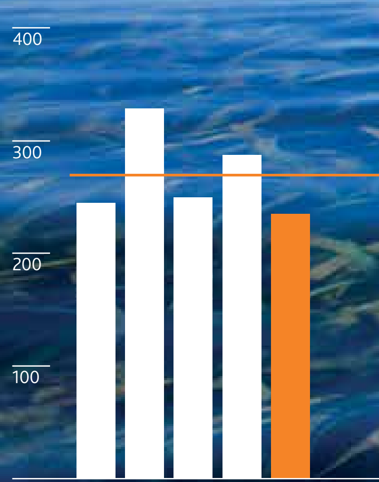
11 February 2015

At Lancashire, *we adapt to advance*

We have taken some significant strategic steps in response to changes in a challenging market, both cyclical and secular. Thanks to our foresight, we have been able to adapt to our environment.

PROBABLE MAXIMUM LOSS
Although it can be a simplistic measure, and we don't place over-reliance on models, the PMLs are a reasonable proxy for the relative amounts of risk we are retaining across the cycle. In the current depressed markets we have brought risk levels down, largely through the use of additional reinsurance.

$235.2m



5 Year average
$269.1m

OPINION ON FINANCIAL STATEMENTS

In our opinion the consolidated financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2014 and of its profit for the year then ended; and
- have been properly prepared in accordance with IFRSs as adopted by the European Union.

WHAT WE HAVE AUDITED

We have audited the consolidated financial statements of Lancashire Holdings Limited and its subsidiaries (collectively "the Group") for the year ended 31 December 2014, which comprise:

- the consolidated statement of comprehensive income;
- the consolidated balance sheet;
- the consolidated statement of changes in shareholders' equity;
- the statement of consolidated cash flows; and
- the accounting policies, the risk disclosures, and the related notes to the accounts 1 to 31.

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Company's members, as a body, in accordance with our engagement letter dated 26 November 2013. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

OUR ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT AND RESPONSE TO THAT RISK

The table below shows the risks we identified that have had the greatest effect on the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team together with our audit response to the risk.

In 2013, we identified a risk relating to the fair value adjustments recognised and the valuation of intangible assets on the acquisition of the Cathedral Group. This year we have considered the risk of impairment of those intangible assets as we comment on below.

VALUATION OF LOSS RESERVES

Refer to page 53 (Audit Committee report), page 97 (accounting policy) and page 108 (disclosures)

Risk	Response
The valuation of loss reserves incorporates a significant amount of judgement. It is reasonably possible that uncertainties inherent in the reserving process, delays in insureds or ceding companies reporting losses to the Group, together with the potential for unforeseen adverse developments, could lead to the ultimate amount paid varying materially from the amount estimated at this reporting date.	We understood, assessed and tested the design and operational effectiveness of the key controls in Lancashire's reserving process, including the review and approval of the reserves, and controls over the extraction of data from the claims systems. Supported by our actuarial specialists, we evaluated management's methodology against market practice and challenged management's assumptions and their assessment of major sensitivities, based on our market knowledge and industry data where available. Using management's data, we independently re-projected the loss and loss adjustment expense reserves for LUK, LICL, and Cathedral on both a gross and net basis, investigating significant differences between our projections and management's booked reserves. Using our own valuation we then considered whether the loss and loss adjustment expense reserves held at the year-end fall within a reasonable range of possible estimates. We considered the results of the third party actuarial review of the loss and loss adjustment reserves as at the reporting date, presented to the Audit Committee, again, specifically to identify and understand any significant differences in projections. In light of our work outlined above, we considered the adequacy of disclosures of the judgements and uncertainties being made by the Directors in the insurance risk note on page 108 and note 13 related to loss and loss adjustment expense reserves.

GOODWILL AND INTANGIBLE ASSETS

Refer to page 53 (Audit Committee report), page 96 (accounting policy) and page 148 (disclosures)

Risk	Response
The acquisition of Cathedral in 2013 resulted in the recognition of goodwill and indefinite life syndicate participation rights with a fair value of $71.2 million and $82.6 million respectively. During 2014 we considered the risk that these assets may be impaired. In testing for impairment judgement is applied by management in deriving: • the forecast cash flows; and • the pre-tax discount rates applied to those cash flows.	Management's impairment assessment of the recorded value of goodwill and the syndicate participation rights was performed as at 30 September 2014. We evaluated and challenged this assessment, including: • validating that the cash flows used are consistent with the three year forecast approved by the Board; • challenging the three year plan, having regard to back testing performed by management to support the robustness of the forecast process and having regard to market conditions; • satisfied ourselves whether the pre-tax discount rate applied is appropriate by assessing the cost of capital for the group and comparable businesses; • assessing whether long term growth assumptions are consistent with economic and industry forecasts; and • challenging the adequacy of sensitivity analysis performed by management, by re-performing our own stress tests of assumptions in isolation and in combination to consider reasonably possible alternative scenarios.

REVENUE RECOGNITION – PREMIUM ESTIMATES

Refer to page 53 (Audit Committee report) and page 96 (accounting policy)

Risk	Response
For certain contracts written, premium is initially recognised based on estimates of ultimate premiums. This occurs for contracts where pricing is based on variables which are not known with certainty at the point of binding the contract. Subsequent adjustments to those estimates, which arise as updated information relating to those pricing variables becomes available, are recorded in the period in which they are determined. These estimates are judgemental and therefore could result in misstatements of revenue recognised in the financial statements.	We evaluated and tested the key controls over the premium estimation process, which include the periodic review by management of estimated premiums, taking into account any third party information received from brokers or insureds. For a sample of policies we verified the year end estimated premium income, including considering the basis of estimation and corroborating evidence such as information from brokers. We have analysed the development, during the period, of estimates recognised as at 31 December 2013 to identify if there was any indication of management bias.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

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

In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OUR APPLICATION OF MATERIALITY

We apply the concept of materiality both in planning and performing our audit, and in evaluating the effect of identified misstatements on our audit and of uncorrected misstatements, if any, on the financial statements and in forming our opinion in the Audit Report.

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

We determined materiality for the Group to be $10.0 million (2013: $10.0 million), which is approximately 5 per cent of pre-tax profit. This provided a basis for determining the nature, timing and extent of risk assessment procedures, identifying and assessing the risk of material misstatement and determining the nature, timings and extent of further audit procedures.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement is that overall performance materiality (i.e. our tolerance for misstatement in an individual account or balance) for the Group should be 50 per cent of materiality, namely $5.0 million (2013: $5.0 million). Our objective in adopting this approach is to ensure that total uncorrected and undetected audit differences do not exceed our materiality of $10.0 million for the financial statements as whole.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in the light of other relevant qualitative considerations.

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of $0.5 million (2013: $0.5 million), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

OVERVIEW OF THE SCOPE OF OUR AUDIT

Following our assessment of the risk of material misstatement to the Group financial statements, our audit scope focused on the insurance components, LUK, LICL and Cathedral, which are all subject to full scope audit procedures for the year ended 31 December 2014. These components accounted for:

- 100 per cent of the Group's insurance losses for the year (refer 'Valuation of insurance contract liabilities' risk and related audit response above);
- 100 per cent of the Group's gross premiums written (refer 'Revenue recognition – premium estimates' risk and related audit response above); and
- 97 per cent of the Group's pre-tax profit.

Audits of these components are performed at a performance materiality level calculated by reference to a proportion of Group materiality appropriate to the relative scale of the component concerned, ranging from $4.0 million to $1.2 million.

The Group audit team visited all of the full scope components, reviewing key working papers and participating in the component teams' planning and execution of the audit of those risks as applicable to those components.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibilities Statement set out on page 83, the Directors are responsible for the preparation of the consolidated financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the consolidated financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

The Company has also instructed us to audit the section of Directors' Remuneration Report that has been described as audited and state whether it has been properly prepared in accordance with the basis of preparation described therein.

OPINION ON OTHER MATTERS

In our opinion the part of the Directors' Remuneration Report that is described as having been audited has been properly prepared in accordance with the basis of preparation as described therein.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following:

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- is otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the Directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the Audit Committee which we consider should have been disclosed.

Under the Listing Rules we are required to review:

- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review.

ERNST & YOUNG LLP
London

11 February 2015

(1) The maintenance and integrity of the Lancashire Holdings Limited website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

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

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
For the year ended 31 December 2014

	Notes	2014 $m	2013 $m
Gross premiums written	2	**907.6**	679.7
Outwards reinsurance premiums	2	**(164.8)**	(122.1)
Net premiums written		**742.8**	557.6
Change in unearned premiums	2	**(37.0)**	24.3
Change in unearned premiums on premiums ceded	2	**9.8**	(13.8)
Net premiums earned		**715.6**	568.1
Net investment income	3	**28.6**	25.4
Net other investment income	3	**1.4**	1.4
Net realised (losses) gains and impairments	3	**(5.9)**	12.6
Share of profit of associates	17	**5.9**	9.2
Other income	27	**19.3**	4.1
Net foreign exchange (losses) gains		**(0.1)**	21.8
Total net revenue		**764.8**	642.6
Insurance losses and loss adjustment expenses	2, 13	**237.9**	250.0
Insurance losses and loss adjustment expenses recoverable	2, 13	**(11.4)**	(61.9)
Net insurance losses		**226.5**	188.1
Insurance acquisition expenses	2, 4	**161.8**	135.1
Insurance acquisition expenses ceded	2, 4	**(8.4)**	(9.3)
Other operating expenses	5, 6, 25	**111.3**	85.0
Equity based compensation	6	**23.3**	16.7
Total expenses		**514.5**	415.6
Results of operating activities		**250.3**	227.0
Financing costs	7	**23.8**	8.9
Profit before tax		**226.5**	218.1
Tax credit	8	**3.1**	3.8
Profit for the year		**229.6**	221.9
Profit (loss) for the year attributable to:			
Equity shareholders of LHL		**229.3**	222.5
Non-controlling interests		**0.3**	(0.6)
Profit for the year		**229.6**	221.9
Other comprehensive loss to be reclassified to profit or loss in subsequent periods			
Net change in unrealised gains/losses on investments	3, 10	**(2.2)**	(33.3)
Tax provision on net change in unrealised gains/losses on investments	10	**0.1**	0.8
Other comprehensive loss	10	**(2.1)**	(32.5)
Total comprehensive income for the year		**227.5**	189.4
Total comprehensive income (loss) attributable to:			
Equity shareholders of LHL		**227.2**	190.0
Non-controlling interests		**0.3**	(0.6)
Total comprehensive income for the year		**227.5**	189.4
Earnings per share			
Basic	26	**$1.24**	$1.31
Diluted	26	**$1.16**	$1.17

CONSOLIDATED BALANCE SHEET

As at 31 December 2014

	Notes	2014 $m	2013 $m
Assets			
Cash and cash equivalents	9, 22	**303.5**	403.0
Accrued interest receivable		**7.7**	8.9
Investments	10, 11, 22	**1,986.9**	2,016.0
Reinsurance assets			
– Unearned premiums on premiums ceded	12	**24.7**	14.9
– Reinsurance recoveries	13	**112.4**	183.0
– Other receivables	12, 14	**5.3**	10.8
Deferred acquisition costs	15	**104.6**	73.8
Other receivables		**36.6**	18.7
Inwards premiums receivable from insureds and cedants	14	**316.2**	288.4
Corporation tax receivable		**4.3**	5.6
Investment in associates	11, 17	**52.7**	64.7
Property, plant and equipment	18	**9.1**	2.8
Intangible assets	19, 28	**153.8**	177.2
Total assets		**3,117.8**	3,267.8
Liabilities			
Insurance contracts			
– Losses and loss adjustment expenses	13	**752.6**	853.4
– Unearned premiums	20	**479.1**	442.1
– Other payables	20, 21	**40.8**	28.9
Amounts payable to reinsurers	12, 21	**34.2**	30.9
Deferred acquisition costs ceded	15	**0.1**	0.2
Other payables	21	**83.5**	80.7
Deferred tax liability	16	**38.7**	38.7
Interest rate swap	22	**4.9**	0.2
Long-term debt	22	**326.6**	332.3
Total liabilities		**1,760.5**	1,807.4
Shareholders' equity			
Share capital	23	**96.1**	92.7
Own shares	23	**(43.3)**	(36.8)
Share premium		**–**	192.2
Contributed surplus		**855.9**	645.7
Accumulated other comprehensive income	10	**0.8**	2.9
Other reserves	24	**31.2**	55.2
Retained earnings		**416.1**	507.8
Total shareholders' equity attributable to equity shareholders of LHL		**1,356.8**	1,459.7
Non-controlling interests	27	**0.5**	0.7
Total shareholders' equity		**1,357.3**	1,460.4
Total liabilities and shareholders' equity		**3,117.8**	3,267.8

The consolidated financial statements were approved by the Board of Directors on 11 February 2015 and signed on its behalf by:

MARTIN THOMAS
DIRECTOR/CHAIRMAN

ELAINE WHELAN
DIRECTOR/CFO

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
For the year ended 31 December 2014

	Notes	Share capital $m	Own shares $m	Share premium $m	Contributed surplus $m	Accumulated other comprehensive income $m	Other reserves $m	Retained earnings $m	Shareholders' equity attributable to equity shareholders of LHL $m	Non-controlling interests $m	Total shareholders' equity $m
Balance as at 31 December 2012		84.3	(57.1)	2.4	654.4	35.4	57.1	610.9	1,387.4	–	1,387.4
Total comprehensive income for the year	10	–	–	–	–	(32.5)	–	222.5	190.0	(0.6)	189.4
Issue of shares	23	8.4	–	189.8	–	–	–	–	198.2	–	198.2
Issue of shares to non-controlling interests	27	–	–	–	–	–	–	–	–	1.3	1.3
Distributed by trust	23	–	30.1	–	(38.7)	–	–	–	(8.6)	–	(8.6)
Shares donated to trust	23, 27	–	(12.8)	–	12.8	–	–	–	–	–	–
Dividends on common shares	23	–	–	–	–	–	–	(276.7)	(276.7)	–	(276.7)
Dividend equivalents on warrants	24	–	–	–	–	–	–	(48.9)	(48.9)	–	(48.9)
Warrant exercises – Founder	24	–	3.0	–	(1.1)	–	(1.9)	–	–	–	–
Equity based compensation – tax	8	–	–	–	–	–	1.6	–	1.6	–	1.6
Equity based compensation – exercises	6, 23, 24	–	–	–	18.3	–	(18.3)	–	–	–	–
Equity based compensation – expense	6	–	–	–	–	–	16.7	–	16.7	–	16.7
Balance as at 31 December 2013		92.7	(36.8)	192.2	645.7	2.9	55.2	507.8	1,459.7	0.7	1,460.4
Total comprehensive income for the year	10	**–**	**–**	**–**	**–**	**(2.1)**	**–**	**229.3**	**227.2**	**0.3**	**227.5**
Share premium reclassification	29	**–**	**–**	**(192.2)**	**192.2**	**–**	**–**	**–**	**–**	**–**	**–**
Share repurchases	23	**–**	**(25.0)**	**–**	**–**	**–**	**–**	**–**	**(25.0)**	**–**	**(25.0)**
Purchase of shares from non-controlling interests	27	**–**	**–**	**–**	**(0.6)**	**–**	**–**	**–**	**(0.6)**	**(0.5)**	**(1.1)**
Distributed by trust	23	**–**	**21.6**	**–**	**(28.3)**	**–**	**–**	**–**	**(6.7)**	**–**	**(6.7)**
Shares donated to trust	23, 27	**–**	**(8.1)**	**–**	**8.1**	**–**	**–**	**–**	**–**	**–**	**–**
Dividends on common shares	23	**–**	**–**	**–**	**–**	**–**	**–**	**(288.9)**	**(288.9)**	**–**	**(288.9)**
Dividend equivalents on warrants	24	**–**	**–**	**–**	**–**	**–**	**–**	**(32.1)**	**(32.1)**	**–**	**(32.1)**
Warrant exercises	23, 24	**3.4**	**5.0**	**–**	**33.1**	**–**	**(27.4)**	**–**	**14.1**	**–**	**14.1**
RSS compensation	6	**–**	**–**	**–**	**(9.8)**	**–**	**–**	**–**	**(9.8)**	**–**	**(9.8)**
Equity based compensation – tax	8	**–**	**–**	**–**	**–**	**–**	**(4.4)**	**–**	**(4.4)**	**–**	**(4.4)**
Equity based compensation – exercises	6, 23, 24	**–**	**–**	**–**	**15.5**	**–**	**(15.5)**	**–**	**–**	**–**	**–**
Equity based compensation – expense	6	**–**	**–**	**–**	**–**	**–**	**23.3**	**–**	**23.3**	**–**	**23.3**
Balance as at 31 December 2014		**96.1**	**(43.3)**	**–**	**855.9**	**0.8**	**31.2**	**416.1**	**1,356.8**	**0.5**	**1,357.3**

STATEMENT OF CONSOLIDATED CASH FLOWS

For the year ended 31 December 2014

	Notes	2014 $m	2013 $m
Cash flows from operating activities			
Profit before tax		**226.5**	218.1
Tax paid		**1.0**	(0.4)
Depreciation	5	**2.1**	1.4
Amortisation of intangible asset	19	**23.4**	13.2
Interest expense on long-term debt	7	**15.5**	13.2
Interest and dividend income		**(50.5)**	(43.9)
Net amortisation of fixed income securities		**9.9**	12.9
Equity based compensation	6	**23.3**	16.7
Foreign exchange losses (gains)		**7.3**	(11.8)
Share of profit of associates	17	**(5.9)**	(9.2)
Net other investment income	3	**(1.4)**	(1.4)
Net realised losses (gains) and impairments	3	**5.9**	(12.6)
Net unrealised losses (gains) on interest rate swaps		**4.7**	(7.8)
Changes in operational assets and liabilities			
– Insurance and reinsurance contracts		**(35.5)**	(26.1)
– Other assets and liabilities		**(13.8)**	5.4
Net cash flows from operating activities		**212.5**	167.7
Cash flows from investing activities			
Interest and dividends received		**52.0**	44.4
Net purchase of property, plant and equipment		**(8.7)**	(0.1)
Investment in associates		**17.9**	26.6
Acquisition of subsidiaries, net of cash acquired	28	**–**	(227.2)
Purchase of investments		**(2,153.7)**	(1,277.9)
Proceeds on sale of investments		**2,159.0**	1,521.2
Net cash flows from investing activities		**66.5**	87.0
Cash flows used in financing activities			
Interest paid		**(15.5)**	(12.0)
Proceeds from issue of shares, net of share issue costs	23	**–**	198.2
Dividends paid	23	**(321.0)**	(325.6)
Share repurchases		**(25.0)**	–
Warrant exercises		**14.1**	–
RSS compensation		**(9.8)**	–
Distributions by trust		**(6.7)**	(8.6)
(Repurchase) issue of shares to non-controlling interests	27	**(1.1)**	1.3
Net cash flows used in financing activities		**(365.0)**	(146.7)
Net (decrease) increase in cash and cash equivalents		**(86.0)**	108.0
Cash and cash equivalents at beginning of year		**403.0**	295.8
Effect of exchange rate fluctuations on cash and cash equivalents		**(13.5)**	(0.8)
Cash and cash equivalents at end of year	9	**303.5**	403.0

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

BASIS OF PREPARATION

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

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

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

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

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

IFRS 9, Financial Instruments: Classification and Measurement, has been issued but is not yet effective, and therefore has not yet been adopted by the Group. The Group continues to apply IAS 39, Financial Instruments: Recognition and Measurement and classifies its fixed income and equity securities as AFS or FVTPL. The new standard is effective for annual periods beginning on or after 1 January 2018 and is not expected to have a material impact on the results and disclosures reported in the consolidated financial statements. It will, however, result in a reclassification of fixed income securities from AFS to FVTPL and a reclassification of the net change in unrealised gains and losses on investments from accumulated other comprehensive income to profit or loss.

IFRS 10, Consolidated Financial Statements, issued in May 2011, redefines the principle of control and establishes control as the basis for determining which entities are consolidated in an entity's financial statements. IFRS 12, Disclosure of Involvement with Other Entities, was issued concurrently and sets out the disclosure requirements for consolidated financial statements. Both standards were effective from 1 January 2014 and did not have a material impact on the Group's results or disclosure requirements.

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

USE OF ESTIMATES

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

The most significant estimate made by management is in relation to losses and loss adjustment expenses. This is discussed on page 97 and also in the risk disclosures section from page 108. Estimates in relation to losses and loss adjustment expenses recoverable are discussed on page 97.

Estimates are also made in determining the estimated fair value of certain financial instruments and equity compensation plans. The estimation of the fair value of financial instruments is discussed on pages 97 and 98 and in note 10. Management judgement is applied in determining impairment charges. The estimation of the fair value of equity based compensation awards granted is discussed in note 6.

Intangible assets are recognised on the acquisition of a subsidiary. The fair value of intangible assets arising from the acquisition of a subsidiary is largely based on the estimated expected cash flows of the business acquired and the contractual rights of that business. The Group determines whether indefinite life intangible assets are impaired at least on an annual basis. This requires an estimation of the recoverable amount of the CGU to which the intangible assets are allocated. The assumptions made by management in performing impairment tests of intangible assets are subject to estimation uncertainty. Details of the key assumptions used in the estimation of the recoverable amounts of the CGU are contained in note 19.

BASIS OF CONSOLIDATION

The consolidated financial statements comprise the financial statements of the Group and its subsidiaries as at 31 December 2014. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date when such control ceases. Intercompany balances, profits and transactions are eliminated. The Group participates on the syndicates at Lloyd's, which are managed by the Group's managing agent subsidiary. In view of the several liability of underwriting members at Lloyd's, the Group recognises its proportion of all the transactions undertaken by the syndicates in which it participates within its consolidated statement of comprehensive income. Similarly, the Group's proportion of the syndicates' assets and liabilities has been reflected in its balance sheet. This proportion is calculated by reference to the Group's participation as a percentage of each syndicate's total capacity for each year of account.

Subsidiaries' accounting policies are generally consistent with the Group's accounting policies. Where they differ, adjustments are made on consolidation to bring accounting policies in line.

ASSOCIATES

Investments, in which the Group has significant influence over the operational and financial policies of the investee, are recognised at cost and thereafter accounted for using the equity method. Under this method, the Group records its proportionate share of income and loss from such investments in its statement of comprehensive income for the period. Adjustments are made to associates' accounting policies, where necessary, in order to be consistent with the Group's accounting policies.

FOREIGN CURRENCY TRANSLATION

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

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

BUSINESS COMBINATIONS

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the fair value of consideration transferred at the acquisition date. On acquisition of a business the Group assesses the financial assets acquired and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions at the acquisition date. Unpaid loss reserves and loss reserves recoverable assumed through a business combination are initially measured at fair value, using an applicable risk-free discount rate and having regard to the expected settlement dates of the claims. Unearned premiums and unearned premiums ceded acquired through a business combination are initially measured in accordance with the Group's existing accounting policies. The difference between the acquired amount and the fair value of these assets and liabilities is recognised as a separately identifiable intangible asset and recorded as the value of in-force business. Other identifiable assets acquired and liabilities and contingent liabilities assumed, which meet the conditions for recognition under IFRS 3, Business Combinations, are recognised at their fair value at the acquisition date. The excess of the fair value of consideration transferred over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. Costs directly related to an acquisition are expensed in the consolidated statement of comprehensive income when incurred.

INTANGIBLE ASSETS

The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite depending on the nature of the asset. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Intangible assets with indefinite useful lives are tested for impairment at least annually at the CGU level by comparing the net present value of the future earnings stream of the CGU to the carrying value of the intangible asset and the related net assets. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether the indefinite life assessment continues to be supportable.

GOODWILL

Goodwill is deemed to have an indefinite life and, after initial recognition, is measured at cost less any accumulated impairment losses. Goodwill is tested for impairment annually, or when events or changes in circumstance indicate that it might be impaired.

SYNDICATE PARTICIPATION RIGHTS

Syndicate participation rights purchased in a business combination are initially measured at fair value and are subsequently measured at cost less any impairment. Syndicate participation rights are considered to have an indefinite life as they will provide benefits over an indefinite future period and are therefore not subject to an annual amortisation charge. The value of the syndicate participation rights is reviewed for impairment at least annually.

VALUE OF IN-FORCE BUSINESS

The value of in-force business acquired in a business combination is initially recognised as the difference between the fair value of the net unearned premiums acquired and the measurement of the net unearned premiums acquired using the Group's existing accounting policies. The value of in-force business has a finite useful life and subsequent to initial recognition it is carried at cost less accumulated amortisation and is amortised over the remaining life of the acquired insurance contracts. The portion of the value of in-force business which replaced the deferred acquisition costs carried on Cathedral's historical balance sheet was amortised in net acquisition costs in the statement of comprehensive income. The remaining amortisation was charged to other operating expenses.

INSURANCE CONTRACTS

CLASSIFICATION

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Contracts that do not transfer significant insurance risk are accounted for as investment contracts. Insurance risk is transferred when an insurer agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder.

PREMIUMS AND ACQUISITION COSTS

Premiums are first recognised as written at the later of a contract's binding or inception date. The Group writes both excess of loss and pro-rata (proportional) contracts. For the majority of excess of loss contracts, premiums written are recorded based on the minimum and deposit or flat premium, as defined in the contract. Subsequent adjustments to the minimum and deposit premium are recognised in the period in which they are determined. For pro-rata contracts and excess of loss contracts where no deposit is specified in the contract, premiums written are recognised based on estimates of ultimate premiums provided by the insureds or ceding companies. Initial estimates of premiums written are recognised in the period in which the contract incepts, or the period in which the contract is bound if later. Subsequent adjustments, based on reports of actual premium by the insureds or ceding companies, or revisions in estimates, are recorded in the period in which they are determined.

Premiums written are earned rateably over the term of the underlying risk period of the insurance contract, except where the period of risk differs significantly from the contract period. In these circumstances, premiums are recognised over the period of risk in proportion to the amount of insurance protection provided. The portion of the premium related to the unexpired portion of the risk period is reflected in unearned premiums.

Where contract terms require the reinstatement of coverage after an insured's or ceding company's loss, the estimated mandatory reinstatement premiums are recorded as premiums written when a specific loss event occurs. Reinstatement premiums are not recorded for losses included within the provision for IBNR which do not relate to a specific loss event.

Inwards premiums receivable from insureds and cedants are recorded net of commissions, brokerage, premium taxes and other levies on premiums, unless the contract specifies otherwise. These balances are reviewed for impairment, with any impairment loss recognised as an expense in the period in which it is determined.

Acquisition costs represent commissions, brokerage, profit commissions and other variable costs that relate directly to the successful securing of new contracts and the renewing of existing contracts. They are generally deferred over the period in which the related premiums are earned to the extent they are recoverable out of expected future revenue margins. All other acquisition costs are recognised as an expense when incurred.

OUTWARDS REINSURANCE

Outwards reinsurance premiums comprise the cost of reinsurance contracts entered into. Outwards reinsurance premiums are accounted for in the period in which the contract incepts, or the period in which the contract is bound if later. The provision for reinsurers' share of unearned premiums represents that part of reinsurance premiums ceded which are estimated to be earned in future financial periods. Unearned reinsurance commissions are recognised as a liability using the same principles.

Any amounts recoverable from reinsurers are estimated using the same methodology as the underlying losses. The Group monitors the creditworthiness of its reinsurers on an ongoing basis and assesses any reinsurance assets for impairment, with any impairment loss recognised as an expense in the period in which it is determined.

LOSSES

Losses comprise losses and loss adjustment expenses paid in the period and changes in the provision for outstanding losses, including the provision for IBNR and related expenses. Losses and loss adjustment expenses are charged to income as they are incurred.

A portion of the Group's business is in classes with high attachment points of coverage, including property catastrophe excess of loss. Reserving for losses in such programmes is inherently complicated in that losses in excess of the attachment level of the Group's policies are characterised by high severity and low frequency and other factors which could vary significantly as losses are settled. This limits the volume of industry loss experience available from which to reliably predict ultimate losses following a loss event.

Losses and loss adjustment expenses represent the estimated ultimate cost of settling all losses and loss adjustment expenses arising from events which have occurred up to the balance sheet date, including a provision for IBNR. The Group does not discount its liabilities for unpaid losses. Outstanding losses are initially set on the basis of reports of losses received from third parties. ACRs are determined where the Group's best estimate of the reported loss is greater than that reported. Estimated IBNR reserves may also consist of a provision for additional development in excess of losses reported by insureds or ceding companies, as well as a provision for losses which have occurred but which have not yet been reported by insureds or ceding companies. IBNR reserves are set on a best estimate basis and are estimated by management using various actuarial methods as well as a combination of own loss experience, historical insurance industry loss experience, underwriters' experience, estimates of pricing adequacy trends and management's professional judgement.

The estimation of the ultimate liability arising is a complex process which incorporates a significant amount of judgement. It is reasonably possible that uncertainties inherent in the reserving process, delays in insureds or ceding companies reporting losses to the Group, together with the potential for unforeseen adverse developments, could lead to a material change in losses and loss adjustment expenses.

LIABILITY ADEQUACY TESTS

At each balance sheet date, the Group performs a liability adequacy test using current best estimates of future cash outflows generated by its insurance contracts, plus any investment income thereon. If, as a result of these tests, the carrying amount of the Group's insurance liabilities is found to be inadequate, the deficiency is charged to income for the period, initially by writing off deferred acquisition costs and subsequently by establishing a provision.

FINANCIAL INSTRUMENTS

CASH AND CASH EQUIVALENTS

Cash and cash equivalents are carried in the consolidated balance sheet at amortised cost and include cash in hand, deposits held on call with banks and other short-term highly liquid investments with a maturity of three months or less at the date of purchase. Carrying amounts approximate fair value due to the short-term nature and high liquidity of the instruments.

Interest income earned on cash and cash equivalents is recognised on the effective interest rate method. The carrying value of accrued interest income approximates estimated fair value due to its short-term nature and high liquidity.

INVESTMENTS

The Group's fixed income and equity securities are quoted investments that are classified as AFS or at FVTPL and are carried at estimated fair value. The classification is determined at the time of initial purchase and depends on the category of investment. Fixed income investments in principal protected equity linked notes are designated as at FVTPL.

The Group's hedge funds are unquoted investments classified at FVTPL and are carried at estimated fair value. Estimated fair values are determined using a combination of the most recent NAVs provided by each fund's independent administrator and the estimated performance provided by each hedge fund manager.

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

On derecognition of an investment, previously recorded unrealised gains and losses are removed from accumulated other comprehensive income in shareholders' equity and included in current period income. Changes in estimated fair value of investments classified as at FVTPL are recognised in current period income.

Amortisation and accretion of premiums and discounts on AFS fixed income securities are calculated using the effective interest rate method and are recognised in current period net investment income. Interest income is recognised on the effective interest rate method. The carrying value of accrued interest income approximates estimated fair value due to its short-term nature and high liquidity. Dividends on equity securities are recorded as revenue on the date the dividends become payable to the holders of record.

The Group regularly reviews the carrying value of its AFS investments for evidence of impairment. An investment is impaired if its carrying value exceeds the estimated fair value and there is objective evidence of impairment to the asset. Such evidence would include a prolonged decline in estimated fair value below cost or amortised cost, where other factors, such as expected cash flows, do not support a recovery in value. If an impairment is deemed appropriate, the difference between cost or amortised cost and estimated fair value is removed from accumulated other comprehensive income in shareholders' equity and charged to current period income. Impairment losses on fixed income securities may be subsequently reversed through income while impairment losses on equity securities are not subsequently reversed through income.

DERIVATIVE FINANCIAL INSTRUMENTS

Derivatives are recognised at estimated fair value on the date a contract is entered into, the trade date, and are subsequently carried at estimated fair value. Derivative instruments with a positive estimated fair value are recorded as derivative financial assets and those with a negative estimated fair value are recorded as derivative financial liabilities.

Derivative financial instruments include exchange-traded future and option contracts, forward foreign currency contracts, interest rate swaps, credit default swaps and interest rate swaptions. They derive their value from the underlying instrument and are subject to the same risks as that underlying instrument, including liquidity, credit and market risk. Estimated fair values are based on exchange or broker-dealer quotations, where available, or discounted cash flow models, which incorporate the pricing of the underlying instrument, yield curves and other factors. Changes in the estimated fair value of instruments that do not qualify for hedge accounting are recognised in current period income. The Group does currently not hold any derivatives classified as hedging instruments. For discounted cash flow techniques, estimated future cash flows are based on management's best estimates and the discount rate used is an appropriate market rate.

Derivative financial assets and liabilities are offset and the net amount is reported in the consolidated balance sheet only to the extent there is a legally enforceable right of offset and there is an intention to settle on a net basis, or to realise the assets and liabilities simultaneously. Derivative financial assets and liabilities are derecognised when the Group has transferred substantially all of the risks and rewards of ownership or the liability is discharged, cancelled or expired.

OTHER INCOME

Managing agent's fees and commissions and underwriting service fees are recognised in line with services provided. Contingent profit commissions are recognised when it is virtually certain that they will be realised.

LONG-TERM DEBT

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

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is carried at historical cost, less accumulated depreciation and any impairment in value. Depreciation is calculated to write off the cost over the estimated useful economic life on a straight-line basis as follows:

IT equipment	33% per annum
Office furniture and equipment	20% to 33% per annum
Leasehold improvements	20% per annum

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant or equipment is derecognised on disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Gains and losses on the disposal of property, plant and equipment are determined by comparing proceeds with the carrying amount of the asset, and are included in the consolidated statement of comprehensive income. Costs for repairs and maintenance are charged to income as incurred.

LEASES

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

EMPLOYEE BENEFITS

EQUITY COMPENSATION PLANS

The Group currently operates an RSS under which nil-cost options have been granted. The Group has also operated a management warrant plan and an LTIP option plan in the past. The fair value of the equity instruments granted is estimated on the date of grant. The estimated fair value is recognised as an expense pro-rata over the vesting period of the instrument, adjusted for the impact of any non-market vesting conditions. No adjustment to vesting assumptions is made in respect of market vesting conditions.

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

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

PENSIONS

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

TAX

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

Deferred tax is recognised on all temporary differences between the assets and liabilities in the consolidated balance sheet and their tax base, except when the deferred tax liability arises from the initial recognition of goodwill. Deferred tax assets or liabilities are accounted for using the balance sheet liability method. Deferred tax assets are recognised to the extent that realising the related tax benefit through future taxable profits is likely.

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

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

OWN SHARES

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

RISK DISCLOSURES: INTRODUCTION

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

The primary objective of the Group's ERM is to ensure that the capital resources held are matched to the risk profile of the Group and that the balance between risk and reward is considered as part of all key business decisions. The Group has formulated, and keeps under review, a risk appetite which is set by the Board of Directors. The Group's appetite for risk will vary marginally from time to time to reflect the potential risks and rewards that present themselves. However, protecting the Group's capital and providing investors with a superior risk-adjusted return over the long term are constants. The risk appetite of the Group is central to how the business is run and permeates into the risk appetites that the individual operating entity Boards of Directors have adopted. These risk appetites are expressed through detailed risk tolerances at both a Group and an operating entity level. Risk tolerances represent the maximum amount of capital, generally on a modeled basis, that the Group and its entities are prepared to expose to certain risks.

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

RISK AND RETURN COMMITTEE

The RRC seeks to optimise risk-adjusted return and facilitate the appropriate use of the Internal Model, including considering its effectiveness. It ensures that all key areas of risk are discussed according to a schedule that covers fortnightly, monthly, quarterly, semi-annual and annual reviews. The RRC meets fortnightly and is responsible for coordinating and overseeing ERM activities within the risk profile, appetites and tolerances set by the Group and individual entity Boards of Directors. The RRC includes the Group CEO and members from the finance, actuarial and underwriting functions and includes representation from Cathedral. The CRO attends the meetings and reports on the RRC's activities to the Group and individual entity Boards of Directors and the Risk Committee of Cathedral.

CHIEF RISK OFFICER

The primary role of the CRO is to facilitate the effective operation of ERM throughout the Group at all levels. The role includes but is not limited to the following responsibilities:

- drive ERM culture, ownership and execution on three levels: Board, executive management, and operationally within the business;
- facilitate the identification, assessment and evaluation of existing and emerging risks by management and the Board;
- ensure that these risks are given due consideration and are embedded within management's and the Board's oversight and decision making process;
- be consulted, and opine on, policy in areas such as, but not limited to, underwriting, claims, investments, operations and capital management; and
- provide timely, accurate, reliable, factual, objective and accessible information and analysis to guide, coach and support decision making.

Responsibility for the management of individual risks has been assigned to, and may form part of the performance objectives of, the risk owners within the business. Risk owners ensure that these risks and controls are consistent with their day-to-day processes and the entries made in the Group risk registers, which are a direct input into BLAST. The CRO provides regular reports to the business outlining the status of the Group's ERM activities and strategy, as well as formal reports to the Boards of Directors of the Group and the individual operating entities in this regard including the Risk Committee of Cathedral. The CRO ultimately has the right to report directly to the Group and entity regulators if he feels that management is not appropriately addressing areas of concern.

INTERNAL AUDIT

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

ECONOMIC CAPITAL MODEL

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

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

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

BLAST covers the risks for LICL, LUK and Kinesis but does not cover Cathedral's risk. Owing to the particular requirements of Lloyd's regulations, Cathedral has its own Internal Model which is vetted by Lloyd's as part of its own capital and solvency regulations. To formulate an overall Group view of risk, exposures from Cathedral are combined with LICL, LUK and Kinesis using Lancashire's proprietary internal models.

The six primary risk categories, insurance risk, market risk, liquidity risk, credit risk, operational risk and strategic risk, are discussed in detail on pages 102 to 126.

A. INSURANCE RISK

The Group underwrites worldwide, predominantly short-tail, insurance and reinsurance contracts that transfer insurance risk, including risks exposed to both natural and man-made catastrophes. The Group's exposure in connection with insurance contracts is, in the event of insured losses, whether premiums will be sufficient to cover the loss payments and expenses. Insurance and reinsurance markets are cyclical and premium rates and terms and conditions vary by line of business depending on market conditions and the stage of the cycle. Market conditions are impacted by capacity and recent loss events, and broader economic cycle impacts amongst other factors. The Group's underwriters assess likely losses using their experience and knowledge of past loss experience, industry trends and current circumstances. This allows them to estimate the premiums sufficient to meet likely losses and expenses and desired levels of profitability consistent with the Group's risk-adjusted RoE targets.

The Group considers insurance risk at an individual contract level, at a sector level, a geographic level and at an aggregate portfolio level. This ensures careful risk selection, limits on concentration and appropriate portfolio diversification are accomplished. The four principle classes of business for the Group, excluding the Lloyd's segment, are Property, Energy, Marine and Aviation. These classes, plus the Group's Lloyd's segment, are deemed to be the Group's five operating segments. The level of insurance risk tolerance per peril is set by the respective Boards of Directors at both the LHL and entity level.

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

- the Group has a rolling three-year strategic plan that helps establish the over-riding business goals that the Board of Directors aims to achieve;
- a detailed business plan is produced annually which includes expected premiums and combined ratios by class and considers risk-adjusted profitability, capital usage and requirements. The plan is approved by the Board of Directors and is monitored, reviewed and updated on an ongoing basis;
- for Cathedral the Syndicate Budget Forecast and Business Plan are subject to review and approval by Lloyd's;
- BLAST and SHARP are used to measure occurrence risks, aggregate risks and correlations between classes and other non-insurance risks, and the outputs and assumptions are reviewed periodically by the RRC;
- each authorised class has a predetermined normal maximum line structure;
- each underwriter has a clearly defined limit of underwriting authority;
- the Group and individual operating entities have predetermined tolerances on probabilistic and deterministic losses of capital for certain single events;
- risk levels versus tolerances are monitored on a regular basis;
- a daily underwriting call is held for LICL and LUK to peer review insurance proposals, opportunities and emerging risks;
- a daily post-binding review process with exception reporting to management based on underwriting authority operates at Cathedral;
- sophisticated pricing and aggregation models are utilised in certain areas of the underwriting process, and are updated frequently;
- BLAST and other modeling tools are deployed to model catastrophes and resultant losses to the portfolio and the Group; and
- reinsurance may be purchased to mitigate both frequency and severity of losses on a treaty or facultative basis and to improve risk-adjusted RoE as modeled in BLAST.

Some of the Group's business provides coverage for natural catastrophes (e.g. hurricanes, earthquakes and floods) and is subject to potential seasonal variation. A proportion of the Group's business is exposed to large catastrophe losses in North America, Europe and Japan as a result of windstorms. The level of windstorm activity, and landfall thereof, during the North American, European and Japanese wind seasons may materially impact the Group's loss experience. The North American and Japanese wind seasons are typically June to November and the European wind season November to March. The Group also bears exposure to large losses arising from other non-seasonal natural catastrophes, such as earthquakes, tsunamis, droughts, floods and tornadoes, from risk losses throughout the year and from war, terrorism and political risk and other events. The Group's associate bears exposure to catastrophe losses and any significant loss event could potentially result in impairment in the value of the Group's investment in associates.

The Group's exposures to certain peak zone elemental losses, as a percentage of tangible capital, including long-term debt, are shown below. Net loss estimates are before income tax and net of reinstatement premiums and outwards reinsurance. The exposure to catastrophe losses that would result in an impairment in the investment in associates is included in the figures below.

As at 31 December 2014		100 year return period estimated net loss		250 year return period estimated net loss	
		$m	% of tangible capital	$m	% of tangible capital
Zones	**Perils**				
Gulf of Mexico[1]	Hurricane	**254.2**	**16.6**	**377.2**	**24.7**
Non-Gulf of Mexico – U.S.	Hurricane	**254.0**	**16.6**	**455.8**	**29.8**
California	Earthquake	**154.8**	**10.1**	**247.5**	**16.2**
Pan-European	Windstorm	**133.2**	**8.7**	**205.0**	**13.4**
Japan	Earthquake	**116.0**	**7.6**	**184.8**	**12.1**
Japan	Typhoon	**61.2**	**4.0**	**94.6**	**6.2**
Pacific North West	Earthquake	**39.5**	**2.6**	**123.3**	**8.1**

(1) Landing hurricane from Florida to Texas.

As at 31 December 2013		100 year return period estimated net loss		250 year return period estimated net loss	
		$m	% of tangible capital	$m	% of tangible capital
Zones	**Perils**				
Gulf of Mexico[1]	Hurricane	307.6	19.0	440.2	27.3
Non-Gulf of Mexico – U.S.	Hurricane	227.8	14.1	451.4	28.0
California	Earthquake	130.6	8.1	239.0	14.8
Pan-European	Windstorm	210.7	13.0	319.3	19.8
Japan	Earthquake	154.8	9.6	266.9	16.5
Japan	Typhoon	132.9	8.2	249.0	15.4
Pacific North West	Earthquake	49.4	3.1	176.4	10.9

(1) Landing hurricane from Florida to Texas.

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

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

	2014		2013	
	$m	%	$m	%
Worldwide offshore	**287.4**	**31.7**	253.3	37.3
Europe	**221.7**	**24.4**	38.4	5.6
U.S. and Canada	**172.5**	**19.0**	101.5	14.9
Far East	**59.6**	**6.6**	39.9	5.9
Middle East	**42.7**	**4.7**	16.7	2.5
Worldwide, including the U.S. and Canada[1]	**23.2**	**2.6**	151.0	22.2
Worldwide, excluding the U.S. and Canada[2]	**9.5**	**1.0**	19.4	2.9
Rest of world	**91.0**	**10.0**	59.5	8.7
Total	**907.6**	**100.0**	679.7	100.0

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

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

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

	2014		2013	
	$m	%	$m	%
Lloyd's	**284.3**	**31.3**	24.5	3.6
Property	**263.0**	**28.9**	333.4	49.0
Energy	**239.4**	**26.4**	209.9	30.9
Marine	**67.7**	**7.5**	63.0	9.3
Aviation	**53.2**	**5.9**	48.9	7.2
Total	**907.6**	**100.0**	679.7	100.0

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

I. LLOYD'S

Gross premiums written, for the year:

	2014 $m	2013 $m
Property reinsurance	**104.3**	3.4
Property direct and facultative	**80.7**	13.0
Marine cargo	**37.5**	5.0
Aviation and satellite	**27.6**	2.6
Energy	**25.9**	–
Contingency	**4.8**	0.5
Terrorism	**3.5**	–
Total	**284.3**	24.5

Property reinsurance predominantly includes property catastrophe excess of loss, per risk excess of loss and property retrocession lines of business. Property catastrophe excess of loss and per risk excess of loss provide protection for elemental and non-elemental risks and are written on an excess of loss treaty basis within the U.S. and internationally. The U.S. property catastrophe excess of loss book is particularly focused on regional clients. Property retrocession is written on an excess of loss basis through treaty arrangements. It provides coverage for elemental risks when sold on a catastrophe basis and both elemental and non-elemental risks when sold on a per risk retrocession basis. Protection is generally given on a regional basis and may cover specific property risks or all catastrophe perils. It is also generally written on an UNL basis, meaning loss payments are linked to the ceding company's own loss.

Property direct and facultative is a worldwide book of largely commercial property business, written both in the open market and under delegated authorities. The account spans small individual locations to Fortune 500 accounts but with a bias towards small to medium sized risks. Policies are generally provided both for non-elemental and elemental perils, although not all risks include both elemental and non-elemental coverage. Coverage is generally written on a full value, primary or excess of loss basis, although the very largest accounts are currently seldom written at the primary level.

Marine cargo is an international account and is written either on a direct basis or by way of reinsurance. It covers the (re)insurance of commodities or goods in transit. Typically, transit cover is provided on an all-risks basis for marine perils for the full value of the goods concerned, although higher value or capacity business may be written on a layered basis. Static cover is also provided for losses to cargo, from both elemental and non-elemental causes, whilst static at points along its route. In addition, the cargo account can include specie and fine art, vault risks, artwork on exhibition and marine war business relating to cargo in transit.

Aviation and satellite includes aviation reinsurance, aviation war, general aviation and aviation satellite lines of business. Aviation reinsurance provides excess of loss catastrophe cover to the insurers of the world's major airlines and aircraft and aircraft manufacturers. This includes cover for the aircraft themselves as well as losses arising from passenger and third party liability claims against airlines and/or manufacturers. Aviation war covers loss or damage to aviation assets from war, terrorism and similar causes. General aviation covers fixed wing and rotor wing aircraft typically with 50 passenger seats or less and covers both commercial and private clients. A significant part of the aviation satellite account is written through Satec, a specialist underwriting agency, to which underwriting authority is delegated. Satellite insurance is purchased by launch operators, satellite manufacturers and satellite operators to protect against launch or deployment failure or subsequent failure in orbit. Policies are typically written for launch plus one year in orbit. Thereafter orbit cover is normally provided on an annual basis.

Energy risks are written mostly on a direct basis and may be ground-up or for primary or excess layers on either a first loss or full value basis. Worldwide offshore energy policies are typically package policies which may include physical damage, well control, business interruption and third-party liability sections. Coverage can include fire and explosion and elemental risks. Individual assets covered can be high-value and are therefore mostly written on a subscription basis, meaning that coverage is placed with multiple underwriters. Construction energy contracts generally cover all risks of platforms, FPSO and drilling units under construction at yard and offshore, during towing and installation. Onshore construction contracts are generally not written.

Contingency focuses on the sports, leisure and entertainment industries, with a significant emphasis on the music industry. It provides coverage for non-appearance and event cancellation. Generally business is written on a full value basis.

Terrorism business can be written either ground-up or for primary or excess layers, with cover provided for U.S. and worldwide property risks, but typically excluding nuclear, chemical and biological coverage in most territories. Cover is generally provided to medium to large commercial and industrial enterprises. Policies are typically written for scheduled locations and exposure is controlled by setting limits on aggregate exposure within a 'blast zone' radius. The term of these contracts may be multi-year reflecting the term of the underlying exposures. Reinsurance may be purchased on a facultative or treaty basis.

II. PROPERTY

Gross premiums written, for the year:

	2014 $m	2013 $m
Property catastrophe excess of loss	**124.2**	97.5
Terrorism	**55.2**	67.8
Property political risk	**44.4**	66.4
Property retrocession	**18.1**	80.8
Property direct and facultative	**1.0**	10.0
Other property	**20.1**	10.9
Total	**263.0**	333.4

Property catastrophe excess of loss covers elemental risks and is written on an excess of loss treaty basis. The property catastrophe excess of loss portfolio is written within the U.S. and also internationally. Cover is offered for specific perils and regions or countries.

Terrorism business can be written either ground-up or for primary or excess layers, with cover provided for U.S. and worldwide property risks, but typically excluding nuclear, chemical and biological coverage in most territories. Cover is generally provided to medium to large commercial and industrial enterprises. Policies are typically written for scheduled locations and exposure is controlled by setting limits on aggregate exposure within a 'blast zone' radius. The term of these contracts is often multi-year reflecting the term of the underlying exposures. Some national pools are also written, which may include nuclear, chemical and biological coverage and may have an element of life coverage.

Property political risk cover is written either ground-up or on an excess of loss basis. Coverage that the Group provides in the political risk book is split between confiscation perils coverage and sovereign/quasi-sovereign obligor coverage. Confiscation perils coverage protects against CEND (Confiscation, Expropriation, Nationalisation, and Deprivation) and may be extended to include other perils. Sovereign/quasi-sovereign obligors coverage protects against the non-payment or non-honouring of an obligation by a sovereign or quasi-sovereign entity. Cover is provided to medium to large commercial and industrial clients as well as bank and commodity trading clients. The term of these contracts is often multi-year reflecting the term of the underlying exposures. The Group does not provide cover against purely private obligor credit risk.

Property retrocession is written on an excess of loss basis through treaty arrangements and covers elemental risks. Cover may be on a worldwide or regional basis and may cover specific risks or all catastrophe perils. Coverage may be given on a UNL basis, meaning that loss payments are linked directly to the ceding company's own loss, or on an ILW basis, meaning that loss payments are linked to the overall industry insured loss as measured by independent third-party loss index providers.

A small number of property direct and facultative risks continue to be written with modest lines mostly to support client relationships in other classes of business. Cover is generally provided to medium to large commercial and industrial enterprises with high-value locations for non-elemental perils, including fire and explosion, and elemental (natural catastrophe) perils which can include flood, windstorm, earthquake, brush fire, tsunami and tornado.

The Group is exposed to large natural catastrophe losses, such as windstorm and earthquake loss, primarily from assuming property catastrophe excess of loss and property retrocession portfolio risks. Exposure to such events is controlled and measured by setting limits on aggregate exposures in certain classes per geographic zone and through loss modeling. The accuracy of the latter exposure analysis is limited by the quality of data and the effectiveness of the modeling. It is possible that a catastrophic event significantly exceeds the expected modeled event loss. The Group's appetite and exposure guidelines for large losses are set out on pages 102 and 103.

Reinsurance may be purchased to mitigate exposures to large natural catastrophe losses in the U.S., Canada and worldwide with certain exclusions. Reinsurance may also be purchased to reduce the Group's worldwide exposure to large risk losses. Reinsurance is typically purchased on an excess of loss basis, however ILWs or quota share arrangements may be entered into.

III. ENERGY

Gross premiums written, for the year:

	2014 $m	2013 $m
Worldwide offshore energy	**149.9**	149.2
Gulf of Mexico offshore energy	**69.9**	34.4
Energy liabilities	**8.5**	8.8
Construction energy	**6.5**	12.9
Other energy	**4.6**	4.6
Total	**239.4**	209.9

Energy risks are written mostly on a direct basis and may be ground-up or for primary or excess layers on either a first loss or full value basis. Worldwide offshore energy policies are typically package policies which may include physical damage, business interruption and third-party liability sections. Coverage can include fire and explosion and elemental risks. Individual assets covered can be high-value and are therefore mostly written on a subscription basis, meaning that coverage is placed with multiple underwriters.

Gulf of Mexico offshore energy programmes cover elemental and non-elemental risks. Most policies have sub-limits on coverage for elemental losses. These programmes are exposed to Gulf of Mexico windstorms. Exposure to such events is controlled and measured through loss modeling. The accuracy of this exposure analysis is limited by the quality of data and the effectiveness of the modeling. It is possible that a catastrophic event significantly exceeds the expected modeled event loss. The Group's appetite and exposure guidelines to large losses are set out on pages 102 and 103.

The Group also writes energy liability business on a stand-alone basis. Unlike the liability contained within the energy packages that Lancashire writes, stand-alone energy liability is written on an excess of loss basis only. Coverage is worldwide and provides coverage for all kinds of damages and loss to third parties. Coverage is generally restricted to offshore assets.

Construction energy contracts generally cover all risks of platform and drilling units under construction at yards and offshore, during towing and installation. Onshore construction contracts are generally not written.

Reinsurance protection may be purchased to protect a portion of loss from elemental and non-elemental energy claims, and from the accumulation of smaller, attritional losses. Reinsurance is typically purchased on an excess of loss basis but, from time to time, quota share arrangements may be entered into. Reinsurance may be purchased on a facultative or treaty basis.

IV. MARINE

Gross premiums written, for the year:

	2014 $m	2013 $m
Marine hull and total loss	**29.6**	24.8
Marine P&I clubs	**12.8**	10.7
Marine builders risk	**12.2**	10.3
Marine hull war	**10.3**	15.0
Other marine	**2.8**	2.2
Total	**67.7**	63.0

With the exception of the marine P&I clubs, where excess layers are written, most policies are written on a ground-up basis. Marine hull and total loss is generally written on a direct basis and covers marine risks on a worldwide basis, primarily for physical damage. Marine P&I clubs is mostly the reinsurance of the International Group of Protection and Indemnity Clubs and covers marine liabilities. Marine builders risk covers the building of ocean going vessels in specialised yards worldwide and their testing and commissioning. Marine hull war is mostly direct insurance of loss of vessels from war, piracy or terrorist attack, with a very limited amount of facultative reinsurance.

The largest expected exposure in the marine class is from physical loss rather than from elemental loss events, although there is exposure to elemental perils and to the costs for removal of wreck.

Reinsurance may be purchased to reduce the Group's exposure to both large risk losses and an accumulation of smaller, attritional losses. Reinsurance is typically purchased on a treaty excess of loss basis.

V. AVIATION

Gross premiums written, for the year:

	2014 $m	2013 $m
AV52	**25.9**	26.5
Aviation satellite	**24.8**	16.8
Other aviation	**2.5**	5.6
Total	**53.2**	48.9

AV52 is written on a risk attaching excess of loss basis and provides coverage for third-party liability, excluding own passenger liability, resulting from acts of war or hijack of aircraft. Cover excludes countries whose governments provide a backstop coverage, but does, since 2014, include some U.S. commercial airlines.

Aviation satellite cover is written on a full value, primary or excess of loss basis and can provide cover for satellite launch, satellite in-orbit or both satellite launch and in-orbit. Coverage for in-orbit can be provided on an annual or multi-year basis and both launch and in-orbit can cover loss of earnings as well as physical damage.

Reinsurance may be purchased to mitigate exposures to an AV52 event loss. Reinsurance is typically purchased on a treaty excess of loss basis.

REINSURANCE

The Group, in the normal course of business and in accordance with its risk management practices, seeks to reduce certain types of loss that may arise from events that could cause unfavourable underwriting results, and to improve the modeled risk-adjusted RoE by entering into reinsurance arrangements. Reinsurance does not relieve the Group of its obligations to policyholders. Under the Group's reinsurance security policy, reinsurers are assessed and approved as appropriate security based on their financial strength ratings, amongst other factors. The RRC has defined limits by reinsurer by rating. The RRC considers reinsurers that are not rated or do not fall within the predefined rating categories on a case-by-case basis, and would usually require collateral to be posted to support such obligations. There are specific guidelines for these collateralised contracts. The RRC monitors the creditworthiness of its reinsurers on an ongoing basis and formally reviews the Group's reinsurance arrangements at least quarterly.

Reinsurance protection is typically purchased on an excess of loss basis, however it may also include ILW covers or quota share arrangements. The mix of reinsurance cover is dependent on the specific loss mitigation requirements, market conditions and available capacity. Reinsurance may also be purchased to optimise the risk-adjusted return of the underwriting portfolio. The structure varies between types of peril and sub-class. The Group regularly reviews its catastrophe exposures and may purchase reinsurance in order to reduce the Group's net exposure to a large natural catastrophe loss and/or to reduce net exposures to other large losses. The Group can purchase both facultative and treaty reinsurance. There is no guarantee that reinsurance coverage will be available to meet all potential loss circumstances, as it is possible that the cover purchased is not sufficient to transfer the totality of the Group's exposure. Any loss amount which exceeds the programme would be retained by the Group. Some parts of the reinsurance programme have limited reinstatements, therefore the number of claims which may be recovered from second or subsequent losses in those particular circumstances is limited.

INSURANCE LIABILITIES

For most insurance and reinsurance companies, the most significant judgement made by management is the estimation of loss and loss adjustment expense reserves. The estimation of the ultimate liability arising from claims made under insurance and reinsurance contracts is a critical estimate for the Group particularly given the nature of the business written.

Under generally accepted accounting principles, loss reserves are not permitted until the occurrence of an event which may give rise to a claim. As a result, only loss reserves applicable to losses incurred up to the reporting date are established, with no allowance for the provision of a contingency reserve to account for expected future losses or for the emergence of new types of latent claims. Claims arising from future events can be expected to require the establishment of substantial reserves from time to time. All reserves are reported on an undiscounted basis.

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

The extent of reliance on management's judgement in the reserving process differs as to whether the business is insurance or reinsurance, whether it is short-tail or long-tail and whether the business is written on an excess of loss or on a pro-rata basis. Over a typical annual period, the Group expects to write the large majority of programmes on a direct excess of loss basis. The Group does not currently write a significant amount of long-tail business.

INSURANCE VERSUS REINSURANCE

Loss reserve calculations for direct insurance business are not precise in that they deal with the inherent uncertainty of assumptions regarding future reporting and development patterns, frequency and severity trends, claims settlement practices, potential changes in the legal environment and other factors, such as inflation. These estimates and judgements are based on numerous factors and may be revised as additional experience or other data becomes available or reviewed as new or improved methodologies are developed or as current laws or regulations change.

Furthermore, as a broker market reinsurer, management must rely on loss information, reported to brokers by other insurers and their loss adjusters, who must estimate their own losses at the policy level, often based on incomplete and changing information. The information management receives varies by cedant and may include paid losses, estimated case reserves and an estimated provision for IBNR reserves. Additionally, reserving practices and the quality of data reporting may vary among ceding companies which adds further uncertainty to the estimation of the ultimate losses.

SHORT-TAIL VERSUS LONG-TAIL

In general, claims relating to short-tail risks, such as the majority of risks underwritten by the Group, are reported more promptly than those relating to long-tail risks, including the majority of casualty risks. However, the timeliness of reporting can be affected by such factors as the nature of the event causing the loss, the location of the loss, and whether the losses are from policies in force with insureds, primary insurers, reinsurers or vendor binding authorities.

EXCESS OF LOSS VERSUS PROPORTIONAL

For excess of loss contracts, which make up the majority of the Group's business, management are aided by the fact that each policy has a defined limit of liability arising from one event. Once that limit has been reached, there is no further exposure to additional losses from that policy for the same event. For proportional business, an initial estimated loss and loss expense ratio is generally used. This is based upon information provided by the insured or ceding company and/or their broker and management's historical experience of that treaty, if any, and the estimate is adjusted as actual experience becomes known.

TIME LAGS

There is a time lag inherent in reporting from the original claimant to the primary insurer or binding authority holder to the broker and then to the reinsurer. Also, the combination of low claims frequency and high severity makes the available data more volatile and less useful for predicting ultimate losses. In the case of proportional contracts, reliance is placed on an analysis of a contract's historical experience, industry information, and the professional judgement of underwriters in estimating reserves for these contracts. In addition, if available, reliance is placed partially on ultimate loss ratio forecasts as reported by insureds or cedants, which are normally subject to a quarterly or six-month lag.

UNCERTAINTY

As a result of the time lag described above, an estimation must be made of IBNR reserves, which consist of a provision for additional development in excess of the case reserves reported by insureds or ceding companies, as well as a provision for claims which have occurred but which have not yet been reported by insureds or ceding companies. Due to the degree of reliance that is necessarily placed on insureds or ceding companies for claims reporting, the associated time lag, the low frequency/high severity nature of much of the business that the Group underwrites, and the varying reserving practices among ceding companies, reserve estimates are highly dependent on management judgement and are therefore uncertain. During the loss settlement period, which may be years in duration, additional facts regarding individual claims and trends often will become known, and current laws and case law may change as well as regulatory directives, with a consequent impact on reserving. The claims count on the types of insurance and reinsurance that the Group writes, which are low frequency and high severity in nature, is generally low.

For certain catastrophic events there are greater uncertainties underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Complexity resulting from problems such as policy coverage issues, multiple events affecting one geographic area and the resulting impact on claims adjusting (including the allocation of claims to the specific event and the effect of demand surge on the cost of building materials and labour) by, and communications from, insureds or ceding companies, can cause delays to the timing with which the Group is notified of changes to loss estimates.

As at 31 December 2014, management's estimates for IBNR represented 31.6 per cent of total net loss reserves (31 December 2013 – 31.8 per cent). The majority of the estimate relates to potential claims on non-elemental risks where timing delays in insured or cedant reporting may mean losses could have occurred which the Group was not made aware of by the balance sheet date.

B. MARKET RISK

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

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

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

I. INSURANCE RISK

The Group is exposed to insurance market risk from several sources, including the following:

- the advent or continuation of a soft market, which may result in a stabilisation or decline in premium rates and/or terms and conditions for certain lines, or across all lines;
- the actions and reactions of key competitors, which may directly result in volatility in premium volumes and rates, fee levels and other input costs;
- market events which may cause a limit in the availability of cover, including unusual inflation in rates, causing political intervention or national remedies;
- failure to maintain broker, binding authority and client relationships, leading to a limited or substandard choice of risks inconsistent with the Group's risk appetite; and
- changes in regulation including capital, governance or licensing requirements.

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

- reviews and amends underwriting plans and outlook as necessary;
- reduces exposure to market sectors where conditions have reached unattractive levels;
- purchases appropriate, cost-effective reinsurance cover to mitigate exposures;
- closely monitors changes in rates and terms and conditions;
- ensures through continuous capital management that it does not allow surplus capital to drive underwriting appetite;
- holds a daily underwriting meeting for LICL and LUK to discuss, inter alia, market conditions and opportunities;
- reviews all new and renewal business post-underwriting for Cathedral;
- regularly reviews output from BLAST to assess up-to-date profitability of classes and sectors;
- holds a quarterly Underwriting and Underwriting Risk Committee meeting to review underwriting strategy;
- holds a fortnightly RRC meeting to monitor estimated exposures to peak zone elemental losses and RDS; and
- holds regular documented meetings with regulators.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest bearing.

II. INVESTMENT RISK

Movements in investments resulting from changes in interest and inflation rates and currency exchange rates, amongst other factors, may lead to an adverse impact on the value of the Group's investment portfolio. Investment guidelines are established by the Investment Committee of the Board of Directors to manage this risk. Investment guidelines set parameters within which the Group's external investment managers must operate. Important parameters include guidelines on permissible assets, duration ranges, credit quality, currency, maturity, sectors, geographical, sovereign and issuer exposures. Compliance with guidelines is monitored on a monthly basis. Any adjustments to the investment guidelines are approved by the IRRC and the Board of Directors.

The Group's fixed income portfolios are managed by four external investment managers. The Group also has a diversified portfolio of multi-strategy low volatility hedge funds, and a small equity portfolio. The performance of the managers is monitored on an ongoing basis.

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

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

The Group reviews the composition, duration and asset allocation of its investment portfolio on a regular basis in order to respond to changes in interest rates and other market conditions. If certain asset classes are anticipated to produce a higher return within management's risk tolerance, an adjustment in asset allocation may be made. Conversely, if the risk profile is expected to move outside of tolerance levels, adjustments may be made to reduce the risks in the portfolio.

The investment portfolio is currently structured to perform better in a risk-on environment in order to mitigate the impact of a potential rise in interest rates. The Group endeavours to limit losses in risk-on, risk-off, and interest rate hike scenarios. The Group models various periods of significant stress in order to better understand the investment portfolio's risks and exposures. The scenarios represent what could, and most likely will occur (albeit not in the exact form of the scenarios, which are based on historic periods of volatility). The Group also monitors the portfolio impact of more severe disaster scenarios consisting of extreme shocks.

The IRRC meets at least quarterly to ensure that the Group's strategic and tactical investment actions are consistent with investment risk preferences, appetite, risk and return objectives and tolerances. The IRRC also helps further develop the risk tolerances to be incorporated into the ERM framework.

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

As at 31 December 2014	Core $m	Core %	Core plus $m	Core plus %	Surplus $m	Surplus %	Total $m	Total %
– Short-term investments	**0.1**	**–**	**30.3**	**1.7**	**–**	**–**	**30.4**	**1.7**
– Fixed income funds	**15.4**	**0.8**	**–**	**–**	**–**	**–**	**15.4**	**0.8**
– U.S. treasuries	**145.3**	**8.0**	**129.0**	**7.1**	**88.7**	**4.9**	**363.0**	**20.0**
– Other government bonds	**49.5**	**2.7**	**1.7**	**0.1**	**32.8**	**1.8**	**84.0**	**4.6**
– U.S. municipal bonds	**0.9**	**–**	**0.3**	**–**	**27.7**	**1.5**	**28.9**	**1.5**
– U.S. government agency debt	**1.4**	**0.1**	**–**	**–**	**16.1**	**0.9**	**17.5**	**1.0**
– Asset backed securities	**89.1**	**4.9**	**28.8**	**1.6**	**66.2**	**3.6**	**184.1**	**10.1**
– U.S. government agency mortgage backed securities	**40.6**	**2.2**	**41.9**	**2.3**	**85.5**	**4.7**	**168.0**	**9.2**
– Non-agency mortgage backed securities	**9.5**	**0.5**	**4.0**	**0.2**	**7.3**	**0.4**	**20.8**	**1.1**
– Agency commercial mortgage backed securities	**–**	**–**	**0.3**	**–**	**2.1**	**0.1**	**2.4**	**0.1**
– Non-agency commercial mortgage backed securities	**4.6**	**0.3**	**14.3**	**0.8**	**20.7**	**1.1**	**39.6**	**2.2**
– Bank loans	**–**	**–**	**–**	**–**	**127.9**	**7.0**	**127.9**	**7.0**
– Corporate bonds	**307.9**	**17.0**	**153.5**	**8.5**	**243.7**	**13.5**	**705.1**	**39.0**
Total fixed income securities – AFS	**664.3**	**36.5**	**404.1**	**22.3**	**718.7**	**39.5**	**1,787.1**	**98.3**
Fixed income securities – at FVTPL	**–**	**–**	**–**	**–**	**31.2**	**1.7**	**31.2**	**1.7**
Total fixed income securities	**664.3**	**36.5**	**404.1**	**22.3**	**749.9**	**41.2**	**1,818.3**	**100.0**

As at 31 December 2013	Core $m	Core %	Core plus $m	Core plus %	Surplus $m	Surplus %	Total $m	Total %
– Short-term investments	145.4	7.3	75.8	3.8	9.8	0.5	231.0	11.6
– Fixed income funds	26.3	1.3	–	–	–	–	26.3	1.3
– U.S. treasuries	98.7	4.9	53.1	2.7	65.5	3.3	217.3	10.9
– Other government bonds	45.5	2.3	13.6	0.7	48.8	2.4	107.9	5.4
– U.S. municipal bonds	2.3	0.1	3.4	0.2	15.7	0.8	21.4	1.1
– U.S. government agency debt	11.0	0.5	3.5	0.2	83.7	4.2	98.2	4.9
– Asset backed securities	66.6	3.3	30.6	1.5	54.2	2.7	151.4	7.5
– U.S. government agency mortgage backed securities	39.3	2.0	71.3	3.6	141.4	7.0	252.0	12.6
– Non-agency mortgage backed securities	3.8	0.2	1.8	0.1	3.2	0.2	8.8	0.5
– Agency commercial mortgage backed securities	1.6	0.1	0.9	–	1.7	0.1	4.2	0.2
– Non-agency commercial mortgage backed securities	7.1	0.4	11.8	0.6	19.0	0.9	37.9	1.9
– Bank loans	–	–	–	–	107.8	5.4	107.8	5.4
– Corporate bonds	271.7	13.6	173.4	8.7	256.8	12.9	701.9	35.2
Total fixed income securities – AFS	719.3	36.0	439.2	22.1	807.6	40.4	1,966.1	98.5
Fixed income securities – at FVTPL	–	–	–	–	29.6	1.5	29.6	1.5
Total fixed income securities	719.3	36.0	439.2	22.1	837.2	41.9	1,995.7	100.0

Corporate bonds, fixed income securities at FVTPL, bank loans and other government bonds by country are as follows:

As at 31 December 2014	Financials $m	Other industries $m	Total corporate bonds and bank loans $m	Other government bonds $m	Total corporate bonds, bank loans and other government bonds $m
United States	**141.5**	**382.5**	**524.0**	**–**	**524.0**
United Kingdom	**49.8**	**37.4**	**87.2**	**0.4**	**87.6**
Canada	**29.7**	**19.7**	**49.4**	**24.6**	**74.0**
Australia	**34.1**	**7.5**	**41.6**	**9.8**	**51.4**
France	**10.3**	**14.6**	**24.9**	**8.4**	**33.3**
Netherlands	**13.2**	**11.4**	**24.6**	**6.4**	**31.0**
Germany	**2.8**	**15.8**	**18.6**	**9.8**	**28.4**
Norway	**15.5**	**0.8**	**16.3**	**5.0**	**21.3**
Japan	**10.2**	**7.7**	**17.9**	**–**	**17.9**
Switzerland	**15.6**	**0.7**	**16.3**	**–**	**16.3**
Sweden	**13.9**	**–**	**13.9**	**0.2**	**14.1**
Luxembourg	**–**	**7.2**	**7.2**	**–**	**7.2**
Mexico	**–**	**3.0**	**3.0**	**3.6**	**6.6**
Hong Kong	**–**	**4.9**	**4.9**	**–**	**4.9**
United Arab Emirates	**–**	**0.2**	**0.2**	**3.5**	**3.7**
Other	**4.6**	**9.6**	**14.2**	**12.3**	**26.5**
Total	**341.2**	**523.0**	**864.2**	**84.0**	**948.2**

As at 31 December 2013	Financials $m	Other industries $m	Total corporate bonds and bank loans $m	Other government bonds $m	Total corporate bonds, bank loans and other government bonds $m
United States	121.3	331.4	452.7	–	452.7
Canada	53.8	16.0	69.8	26.1	95.9
United Kingdom	41.3	52.2	93.5	0.4	93.9
Australia	22.9	9.7	32.6	10.0	42.6
France	7.4	24.4	31.8	6.6	38.4
Germany	3.8	13.3	17.1	15.3	32.4
Norway	29.0	0.8	29.8	2.0	31.8
Netherlands	14.1	10.9	25.0	5.8	30.8
Sweden	19.8	–	19.8	1.3	21.1
Switzerland	11.7	4.2	15.9	–	15.9
Belgium	–	7.4	7.4	–	7.4
Supranationals	7.2	–	7.2	–	7.2
Japan	2.6	2.6	5.2	–	5.2
Emerging market corporates	4.8	11.3	16.1	–	16.1
Emerging market sovereign	–	–	–	9.9	9.9
Emerging market agency	–	–	–	26.9	26.9
Other	4.0	11.4	15.4	3.6	19.0
Total	343.7	495.6	839.3	107.9	947.2

The sector allocation of the corporate bonds, fixed income securities at FVTPL and bank loans is as follows:

	2014		2013	
As at 31 December	$m	%	$m	%
Industrial	**487.3**	**56.5**	452.8	53.9
Financial	**338.3**	**39.1**	336.5	40.1
Utility	**35.7**	**4.1**	42.8	5.1
Supranationals	**2.9**	**0.3**	7.2	0.9
Total	**864.2**	**100.0**	839.3	100.0

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

The Group's investment portfolio is mainly comprised of fixed income securities and cash and cash equivalents. The fixed income funds are overseas deposits held by Syndicate 2010 and Syndicate 3010 in trust for the benefit of the policyholders in those overseas jurisdictions. They consist of high quality, short duration fixed income securities. The Group also has a small equity portfolio. The estimated fair value of the Group's fixed income portfolio is generally inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Group's fixed income securities would tend to rise and vice versa.

The sensitivity of the price of fixed income securities, and certain derivatives, to movements in interest rates is indicated by their duration. The greater a security's duration, the greater its price volatility to movements in interest rates. The sensitivity of the Group's fixed income and derivative investment portfolio to interest rate movements is detailed below, assuming linear movements in interest rates:

	2014		2013	
As at 31 December	$m	%	$m	%
Immediate shift in yield (basis points)				
100	**(30.6)**	**(1.7)**	(23.3)	(1.2)
75	**(22.9)**	**(1.3)**	(18.3)	(0.9)
50	**(15.3)**	**(0.8)**	(12.7)	(0.6)
25	**(7.6)**	**(0.4)**	(6.6)	(0.3)
(25)	**7.6**	**0.4**	6.8	0.3
(50)	**15.1**	**0.8**	14.0	0.7
(75)	**22.7**	**1.2**	21.3	1.1
(100)	**30.2**	**1.7**	28.9	1.4

The Group mitigates interest rate risk on the investment portfolio by establishing and monitoring duration ranges in its investment guidelines. The Group may manage duration through the use of interest rate futures and swaptions from time to time. The duration of the core portfolio is matched to the modeled duration of the insurance reserves, within a permitted range. The permitted duration range for the core plus portfolio is between zero and four years and the surplus portfolio is between one and five years.

The durations of the externally managed portfolios are as follows:

As at 31 December	2014 years	2013 years
Core portfolio	**1.7**	1.2
Core plus portfolio	**1.9**	1.2
Surplus portfolio	**1.8**	1.9
Overall portfolio (including duration overlay)	**1.5**	1.1

The overall duration for fixed income, managed cash and cash equivalents and certain derivatives is 1.5 years (2013 – 1.0 year).

In addition to duration management, the Group uses VaR on a monthly basis to measure potential losses in the estimated fair values of its cash and invested assets and to understand and monitor risk. The VaR calculation is performed using variance/covariance risk modeling to capture the cash flows and embedded optionality of the portfolio. Securities are valued individually using market standard pricing models. These security valuations serve as the input to many risk analytics, including full valuation risk analyses, as well as parametric methods that rely on option adjusted risk sensitivities to approximate the risk and return profiles of the portfolio.

The principal VaR measure that is produced is an annual VaR at the 99th percentile confidence level. The annual VaR, at the 99th percentile confidence level, measures the minimum amount the assets should be expected to lose over a one year time horizon, under normal conditions, 1 per cent of the time.

The Group's annual VaR calculations are as follows:

	2014		2013	
As at 31 December	**$m**	**% of shareholders' equity**	$m	% of shareholders' equity
99th percentile confidence level	**38.1**	**2.8**	32.6	2.2

DERIVATIVE FINANCIAL INSTRUMENTS

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

The Group currently invests in the following derivative financial instruments:

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

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

As at 31 December 2014	**Net other investment loss $m**	**Net realised losses $m**	**Net foreign exchange losses $m**	**Financing costs $m**
Treasury futures	**–**	**(6.0)**	**–**	**–**
Forward foreign currency contracts	**–**	**–**	**(0.7)**	**–**
Interest rate swaps – investments	**(0.1)**	**(0.1)**	**–**	**–**
Interest rate swaps – debt	**–**	**–**	**–**	**(7.4)**
Swaptions	**(2.2)**	**(2.1)**	**–**	**–**
Total	**(2.3)**	**(8.2)**	**(0.7)**	**(7.4)**

As at 31 December 2013	Net other investment income $m	Net realised gains (losses) $m	Net foreign exchange gains $m	Financing gain $m
Eurodollar futures	–	0.3	–	–
Treasury futures	–	4.8	–	–
Forward foreign currency contracts	–	–	12.0	–
Interest rate swaps – investments	(0.1)	(0.3)	–	–
Interest rate swaps – debt	–	–	–	5.2
Credit default swaps	(0.3)	0.2	–	–
Swaptions	2.2	–	–	–
Total	1.8	5.0	12.0	5.2

The estimated fair values of the Group's derivative instruments are as follows:

As at 31 December	2014 Other investments $m	2014 Other receivables $m	2014 Other payables $m	2014 Interest rate swaps $m	2013 Other investments $m	2013 Other receivables $m	2013 Interest rate swaps $m
Forward foreign currency contracts	**0.7**	**3.8**	**(1.8)**	**–**	–	0.1	–
Interest rate swaps – investments	**–**	**–**	**–**	**–**	(0.1)	–	–
Interest rate swaps – debt	**–**	**–**	**–**	**(4.9)**	–	–	(0.2)
Swaptions	**–**	**–**	**–**	**–**	4.9	–	–
Credit default swaps	**–**	**–**	**–**	**–**	(0.1)	–	–
Total	**0.7**	**3.8**	**(1.8)**	**(4.9)**	4.7	0.1	(0.2)

A. FUTURES

The Group's investment guidelines permit the use of futures which provide the Group with participation in market movements, determined by the underlying instrument on which the futures contract is based, without holding the instrument itself or the individual securities. This approach allows the Group more efficient and less costly access to the exposure than would be available by the exclusive use of individual fixed income and money market securities. Exchange-traded futures contracts may also be used as substitutes for ownership of the physical securities.

All futures contracts are held on a non-leveraged basis. An initial margin is provided, which is a deposit of cash and/or securities in an amount equal to a prescribed percentage of the contract value. The fair value of futures contracts is estimated daily and the margin is adjusted accordingly with unrealised gains and/or losses settled daily in cash and/or securities. A realised gain or loss is recognised when the contract is closed.

Futures contracts expose the Group to market risk to the extent that adverse changes occur in the estimated fair values of the underlying securities. Exchange-traded futures are, however, subject to a number of safeguards to ensure that obligations are met. These include the use of clearing houses (thus reducing counterparty credit risk), the posting of margins and the daily settlement of unrealised gains and losses. The amount of credit risk is therefore considered low. The investment guidelines restrict the maximum notional futures position as a percentage of the investment portfolio's estimated fair value.

As at 31 December, the Group had the following exposure to treasury futures:

As at 31 December	2014 Notional long $m	2014 Notional short $m	2014 Net notional long (short) $m	2013 Notional long $m	2013 Notional short $m	2013 Net notional long (short) $m
Treasury futures	**89.1**	**169.9**	**(80.8)**	80.5	86.2	(5.7)
Total	**89.1**	**169.9**	**(80.8)**	80.5	86.2	(5.7)

A Eurodollar futures contract is an exposure to 3 month LIBOR, based on a commitment to a $1.0 million deposit. The estimated fair value is based on expectations of 3 month LIBOR, is determined using exchange-traded prices and was negligible as at 31 December 2014 and 2013. The contracts currently held by the Group will expire in 2015.

The sensitivity of the Group's Eurodollar futures position to interest rate movements is not material as at 31 December 2014 and 2013.

B. OPTIONS

The Group's investment guidelines permit the use of exchange-traded options on U.S. treasury futures and Eurodollar futures, which are used to manage exposure to interest rate risk and also to hedge duration. Exchange-traded options are held on a similar basis to futures and are subject to similar safeguards. Options are contractual arrangements that give the purchaser the right, but not the obligation, to either buy or sell an instrument at a specific set price at a predetermined future date. The Group may enter into option contracts that are secured by holdings in the underlying securities or by other means which permit immediate satisfaction of the Group's obligations. The notional amount of options is not material as at 31 December 2014 and 2013.

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

C. FORWARD FOREIGN CURRENCY CONTRACTS

A forward foreign currency contract is a commitment to purchase or sell a foreign currency at a future date, at a defined rate. The Group may utilise forward foreign currency contracts to gain exposure to a certain currency or market rate or manage the impact of fluctuations in foreign currencies on the value of its foreign currency denominated investments, debt and/or insurance related currency exposures.

Forward contracts expose the Group to credit, market and liquidity risks. Credit risk arises from the potential inability of counterparties to perform under the terms of the contract. The Group is exposed to market risk to the extent that adverse changes occur in the exchange rate of the underlying foreign currency. Liquidity risk represents the possibility that the Group may not be able to rapidly adjust the size of its forward positions at a reasonable price in times of high volatility and financial stress. These risks are mitigated by requiring a minimum counterparty credit quality, restricting the maximum notional exposure as a percentage of the investment portfolio's estimated fair value and restricting exposures to foreign currencies, individually and in aggregate, as a percentage of the investment portfolio's estimated fair value.

The notional amount of a derivative contract is the underlying quantity upon which payment obligations are calculated. A long position is equivalent to buying the underlying currency whereas a short position is equivalent to having sold the underlying currency.

The Group has the following open forward foreign currency contracts:

	2014			2013		
As at 31 December	Notional long $m	Notional short $m	Net notional long (short) $m	Notional long $m	Notional short $m	Net notional long (short) $m
Canadian Dollar	**0.4**	**20.7**	**(20.3)**	0.5	–	0.5
Australian Dollar	**10.0**	**26.3**	**(16.3)**	10.5	28.5	(18.0)
British Pound	**–**	**8.1**	**(8.1)**	–	9.4	(9.4)
Brazilian Real	**–**	**–**	**–**	3.9	6.6	(2.7)
Chinese Renminbi	**–**	**–**	**–**	0.3	0.3	–
Malaysian Ringgit	**3.7**	**–**	**3.7**	3.9	–	3.9
Euro	**43.2**	**26.4**	**16.8**	52.6	24.5	28.1
Japanese Yen	**5.1**	**5.1**	**–**	–	–	–
Other[1]	**–**	**–**	**–**	0.3	0.3	–
Total	**62.4**	**86.6**	**(24.2)**	72.0	69.6	2.4

(1) Individual currencies included in 'other' have a notional payable and receivable of less than $2.0 million for 2013.

D. SWAPS

The Group's investment guidelines permit the use of interest rate swaps and credit default swaps which are primarily traded OTC. Swaps are recorded at estimated fair value at the end of each period with unrealised gains and losses recorded in the consolidated statement of comprehensive income.

Interest rate swaps are used to manage interest rate exposure, portfolio duration or capitalise on anticipated changes in interest rate volatility without investing directly in the underlying securities. Interest rate swap agreements entail the exchange of commitments to pay or receive interest, such as an exchange of floating rate payments for fixed rate payments, with respect to a notional amount of principal. These agreements involve elements of credit and market risk. Such risks include the possibility that there may not be a liquid market, that the counterparty may default on its obligation to perform, or that there may be unfavourable movements in interest rates. These risks are mitigated through defining a minimum counterparty credit quality and a maximum notional exposure to interest rate swaps as a percentage of the investment portfolio's estimated fair value. The notional amount of interest rate swaps held in the investment portfolio is not material as at 31 December 2014 and 2013. The notional amount of interest rate swaps held internally for the purposes of hedging the interest rate exposure on the Group's subordinated loan notes as at 31 December 2014 is $252.3 million (31 December 2013 – $259.8 million)

The Group uses credit default swaps as a way to add or reduce credit risk to an individual issuer, or a basket of issuers, without investing directly in their securities. As at 31 December 2014, the maximum amount of loss the Group could incur on its open credit default swaps was the notional value of $nil (31 December 2013 – $4.1 million).

E. SWAPTIONS

The Group uses swaptions, options on interest rate swaps, to manage interest rate risk exposure and portfolio and yield curve duration. The Group, as the purchaser of a swaption, is subject to the credit risk of the counterparty but is only subject to market risk to the extent of the premium paid. As a swaption writer, the Group is not subject to credit risk but is subject to market risk, due to its obligation to make payments under the terms of the contract. These risks are mitigated through maximum allowable notional exposures as a percentage of the investment portfolio's estimated fair value. The estimated fair value of these instruments is $nil as at 31 December 2014 (31 December 2013 – $4.9 million).

III. DEBT RISK

The Group has issued long-term debt as described in note 22. The LHL issued subordinated loan notes due in 2035 bear interest at a floating rate that is reset on a quarterly basis, plus a fixed margin of 3.70 per cent. The Group is subject to interest rate risk on the coupon payments of these subordinated loan notes. The Group has mitigated the interest rate risk by entering into interest rate swap contracts as follows:

	Maturity date	Interest hedged
Subordinated loan notes $97.0 million	15 December 2035	100%
Subordinated loan notes €24.0 million	15 June 2035	100%

The interest rate swaps expire on 15 December 2020, therefore the Group currently has no interest rate risk on the LHL issued subordinated loan notes due in 2035.

The senior unsecured notes maturing 1 October 2022 bear interest at a fixed rate of 5.70 per cent and therefore the Group is not exposed to interest rate risk on this long-term debt.

On the acquisition of Cathedral, the Group assumed subordinated loan notes as described in note 22. The Group is subject to interest rate risk on the coupon payment of this long-term debt. An increase of 100 basis points on the EURIBOR and LIBOR three month deposit rates would result in an increase in the interest expense on long term debt for the Group of approximately $0.8 million on an annual basis.

IV. CURRENCY RISK

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

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

The Group hedges non-U.S. dollar liabilities primarily with non-U.S. dollar assets, but may also use derivatives to mitigate foreign currency exposures. The Group's main foreign currency exposure relates to its insurance obligations, cash holdings, investments, premiums receivable, dividends payable and the euro denominated subordinated loan notes long-term debt liabilities discussed in note 22. These positions may not be hedged depending on the currency outlook. See page 117 for a listing of the Group's open forward foreign currency contracts.

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

Assets	U.S. $ $m	Sterling $m	Euro $m	Japanese Yen $m	Other $m	Total $m
Cash and cash equivalents	173.4	42.8	27.2	28.6	31.5	303.5
Accrued interest receivable	7.7	–	–	–	–	7.7
Investments	1,885.7	18.8	41.2	–	41.2	1,986.9
Reinsurance assets	119.8	15.3	3.9	–	3.4	142.4
Deferred acquisition costs	81.8	4.8	10.9	0.6	6.5	104.6
Other receivables	10.8	25.1	–	–	0.7	36.6
Inwards premiums receivable from insureds and cedants	263.5	15.9	27.6	0.2	9.0	316.2
Corporation tax receivable	–	4.3	–	–	–	4.3
Investment in associates	52.7	–	–	–	–	52.7
Property, plant and equipment	0.3	8.8	–	–	–	9.1
Intangible assets	153.8	–	–	–	–	153.8
Total assets as at 31 December 2014	**2,749.5**	**135.8**	**110.8**	**29.4**	**92.3**	**3,117.8**

Liabilities	U.S. $ $m	Sterling $m	Euro $m	Japanese Yen $m	Other $m	Total $m
Losses and loss adjustment expenses	550.1	51.9	65.6	43.3	41.7	752.6
Unearned premiums	379.6	20.2	48.4	4.8	26.1	479.1
Insurance contracts – other payables	34.8	1.4	2.2	0.3	2.1	40.8
Amounts payable to reinsurers	30.0	2.4	1.0	–	0.8	34.2
Deferred acquisition costs ceded	0.1	–	–	–	–	0.1
Other payables	46.5	36.8	0.1	–	0.1	83.5
Deferred tax liability	17.4	21.3	–	–	–	38.7
Interest rate swap	1.6	–	3.3	–	–	4.9
Long-term debt	284.4	–	42.2	–	–	326.6
Total liabilities as at 31 December 2014	**1,344.5**	**134.0**	**162.8**	**48.4**	**70.8**	**1,760.5**

Assets	U.S. $ $m	Sterling $m	Euro $m	Japanese Yen $m	Other $m	Total $m
Cash and cash equivalents	227.6	63.8	44.9	39.4	27.3	403.0
Accrued interest receivable	8.7	0.1	0.1	–	–	8.9
Investments	1,897.6	39.8	45.9	–	32.7	2,016.0
Reinsurance assets	170.3	34.6	2.3	0.3	1.2	208.7
Deferred acquisition costs	57.4	2.2	7.1	0.8	6.3	73.8
Other receivables	8.7	10.0	–	–	–	18.7
Inwards premiums receivable from insureds and cedants	232.1	18.0	26.7	0.6	11.0	288.4
Corporation tax receivable	–	5.6	–	–	–	5.6
Investment in associates	64.7	–	–	–	–	64.7
Property, plant and equipment	1.0	1.8	–	–	–	2.8
Intangible assets	177.2	–	–	–	–	177.2
Total assets as at 31 December 2013	2,845.3	175.9	127.0	41.1	78.5	3,267.8

Liabilities	U.S. $ $m	Sterling $m	Euro $m	Japanese Yen $m	Other $m	Total $m
Losses and loss adjustment expenses	569.9	74.1	91.1	77.7	40.6	853.4
Unearned premiums	348.4	22.8	35.3	7.4	28.2	442.1
Insurance contracts – other payables	24.2	0.1	2.6	–	2.0	28.9
Amounts payable to reinsurers	25.3	5.2	0.3	–	0.1	30.9
Deferred acquisition costs ceded	0.1	–	–	0.1	–	0.2
Other payables	47.7	32.9	0.1	–	–	80.7
Deferred tax liability	19.4	17.2	–	–	2.1	38.7
Interest rate swap	(1.4)	–	1.6	–	–	0.2
Long-term debt	284.4	–	47.9	–	–	332.3
Total liabilities as at 31 December 2013	1,318.0	152.3	178.9	85.2	73.0	1,807.4

The impact on net income of a proportional foreign exchange movement of 10.0 per cent up and 10.0 per cent down against the U.S. dollar at the year end spot rates would be an increase or decrease of $3.8 million (2013 – $2.3 million).

The 31 December 2014 losses and loss adjustment expenses include the equivalent of $21.0 million (2013 – $57.2 million) of Japanese Yen denominated insurance liabilities that are contained within the Group's outwards reinsurance programme which limits the Group's net liability to $30.0 million. The Group has therefore not hedged the foreign currency exposure in relation to these losses.

The Group uses forward foreign currency contracts for the purposes of managing currency exposures. See page 117 for details of the Group's open forward foreign currency contracts.

C. LIQUIDITY RISK

Liquidity risk is the risk that cash may not be available to pay obligations when they are due without incurring an unreasonable cost. The Group's main exposures to liquidity risk are with respect to its insurance and investment activities. The Group is exposed if proceeds from financial assets are not sufficient to fund obligations arising from its insurance contracts. The Group can be exposed to daily calls on its available investment assets, principally to settle insurance claims.

Exposures in relation to insurance activities are as follows:

- large catastrophic events, or multiple medium-sized events in quick succession, resulting in a requirement to pay a large value of claims within a relatively short time frame;
- failure of insureds or cedants to meet their contractual obligations with respect to the payment of premiums in a timely manner; and
- failure of reinsurers to meet their contractual obligations with respect to the payment of claims in a timely manner.

Exposures in relation to investment activities are as follows:

- adverse market movements and/or a duration mismatch to obligations, resulting in investments being disposed of at a significant realised loss; and
- an inability to liquidate investments due to market conditions.

The maturity dates of the Group's fixed income portfolio are as follows:

As at 31 December 2014	Core $m	Core plus $m	Surplus $m	Total $m
Less than one year	**103.7**	**58.9**	**43.6**	**206.2**
Between one and two years	**168.1**	**117.1**	**42.4**	**327.6**
Between two and three years	**200.0**	**80.6**	**75.5**	**356.1**
Between three and four years	**20.9**	**19.6**	**65.3**	**105.8**
Between four and five years	**21.9**	**29.1**	**97.5**	**148.5**
Over five years	**5.9**	**9.5**	**243.8**	**259.2**
Asset backed and mortgage backed securities	**143.8**	**89.3**	**181.8**	**414.9**
Total fixed income securities	**664.3**	**404.1**	**749.9**	**1,818.3**

As at 31 December 2013	Core $m	Core plus $m	Surplus $m	Total $m
Less than one year	265.9	153.2	56.7	475.8
Between one and two years	162.2	68.7	101.5	332.4
Between two and three years	123.4	30.2	57.6	211.2
Between three and four years	30.7	34.3	153.5	218.5
Between four and five years	15.1	23.2	54.3	92.6
Over five years	3.6	13.2	194.1	210.9
Asset backed and mortgage backed securities	118.4	116.4	219.5	454.3
Total fixed income securities	719.3	439.2	837.2	1,995.7

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

As at 31 December 2014		Years until liability becomes due – undiscounted values				
	Balance sheet $m	Less than one $m	One to three $m	Three to five $m	Over five $m	Total $m
Losses and loss adjustment expenses	**752.6**	**299.0**	**270.0**	**102.2**	**81.4**	**752.6**
Insurance contracts – other payables	**40.8**	**30.5**	**9.6**	**0.7**	**–**	**40.8**
Amounts payable to reinsurers	**34.2**	**34.2**	**–**	**–**	**–**	**34.2**
Other payables	**83.5**	**83.5**	**–**	**–**	**–**	**83.5**
Interest rate swap	**4.9**	**2.5**	**2.2**	**0.4**	**(0.2)**	**4.9**
Long-term debt	**326.6**	**13.2**	**35.3**	**38.0**	**546.6**	**633.1**
Total	**1,242.6**	**462.9**	**317.1**	**141.3**	**627.8**	**1,549.1**

As at 31 December 2013		Years until liability becomes due – undiscounted values				
	Balance sheet $m	Less than one $m	One to three $m	Three to five $m	Over five $m	Total $m
Losses and loss adjustment expenses	853.4	381.2	312.4	96.7	63.1	853.4
Insurance contracts – other payables	28.9	26.6	1.5	0.8	–	28.9
Amounts payable to reinsurers	30.9	30.9	–	–	–	30.9
Other payables	80.7	80.7	–	–	–	80.7
Interest rate swap	0.2	2.5	3.5	(1.2)	(4.6)	0.2
Long-term debt	332.3	13.3	34.0	41.8	629.7	718.8
Total	1,326.4	535.2	351.4	138.1	688.2	1,712.9

Actual maturities of the above may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. The prepayment options for the Group's long-term debt are discussed in note 22. While the estimation of the ultimate liability for losses and loss adjustment expenses is complex and incorporates a significant amount of judgement, the timing of payment of losses and loss adjustment expenses is also uncertain and cannot be predicted as simply as for other financial liabilities. Actuarial and statistical techniques, past experience and management's judgement have been used to determine a likely settlement pattern.

The Group manages its liquidity risks via its investment strategy to hold high quality, highly liquid securities, sufficient to meet its insurance liabilities and other near-term liquidity requirements. The creation of the core portfolio with its subset of guidelines aims to ensure funds are readily available to meet potential insurance liabilities in an extreme event plus other near-term liquidity requirements. In addition, the Group has established asset allocation and maturity parameters within the investment guidelines such that the majority of the investments are in high quality assets which could be converted into cash promptly and at minimal expense. The Group monitors market changes and outlooks and reallocates assets as deemed necessary.

D. CREDIT RISK

Credit risk is the risk that a counterparty may fail to pay, or repay, a debt or obligation. The Group is exposed to credit risk on its fixed income investment portfolio and derivative instruments, its inwards premiums receivable from insureds and cedants, and on any amounts recoverable from reinsurers.

Credit risk on the fixed income portfolio is mitigated through the Group's policy to invest in instruments of high credit quality issuers and to limit the amounts of credit exposure with respect to particular ratings categories and any one issuer. Securities rated below an S&P or equivalent rating of BBB-/Baa3 may comprise no more than 10.0 per cent of shareholders' equity. In addition, no one issuer, with the exception of U.S. government and agency securities, other G10 government guaranteed securities (excluding Italy) and Australian sovereign debt should exceed 5.0 per cent of shareholders' equity. The Group is therefore not exposed to any significant credit concentration risk on its investment portfolio, except for fixed income securities issued by the U.S. government and government agencies and other highly rated governments.

Credit risk on exchange-traded derivative instruments is mitigated by the use of clearing houses to reduce counterparty credit risk, require the posting of margins and settle unrealised gains and losses daily. Credit risk on OTC derivatives is mitigated by monitoring the creditworthiness of the counterparties and by requiring collateral to be posted for positions which have accrued gains by amounts exceeding predetermined thresholds.

Credit risk on inwards premiums receivable from insureds and cedants is managed by conducting business with reputable broking organisations, with whom the Group has established relationships, and by rigorous cash collection procedures. The Group also has a broker approval process in place. Binding authorities are subject to standard market controls including credit control. Credit risk from reinsurance recoverables is primarily managed by the review and approval of reinsurer security by the RRC, as discussed on page 108.

The table below presents an analysis of the Group's major exposures to counterparty credit risk, based on their rating. The table includes amounts due from policyholders and unsettled investment trades. The quality of these receivables is not graded but, based on management's historical experience, there is limited default risk associated with these amounts.

As at 31 December 2014	Other investments $m	Cash and fixed income securities $m	Inwards premiums receivable and other receivables $m	Reinsurance recoveries $m
AAA	–	**385.9**	–	–
AA+, AA, AA-	–	**765.8**	–	–
A+, A, A-	**0.7**	**642.4**	**85.0**	**103.0**
BBB+, BBB, BBB-	–	**193.1**	–	**0.1**
Other[1]	–	**134.6**	**273.1**	**9.3**
Total	**0.7**	**2,121.8**	**358.1**	**112.4**

(1) Reinsurance recoveries classified as "other" include $4.2 million of reserves that are fully collateralised.

As at 31 December 2013	Other investments $m	Cash and fixed income securities $m	Inwards premiums receivable and other receivables $m	Reinsurance recoveries $m
AAA	–	568.8	–	–
AA+, AA, AA-	–	865.9	–	–
A+, A, A-	4.9	665.8	97.0	148.1
BBB+, BBB, BBB-	(0.2)	186.8	–	0.3
Other[1]	–	111.4	220.9	34.6
Total	4.7	2,398.7	317.9	183.0

(1) Reinsurance recoveries classified as "other" include $33.2 million of reserves that are fully collateralised; $26.8 million of these are with ARL.

The two counterparties to the Group's long-term debt interest rate swaps are currently rated A+ and A- by S&P respectively.

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

	2014 $m	2013 $m
Less than 90 days past due	**23.6**	13.5
Between 91 and 180 days past due	**6.7**	2.2
Over 180 days past due	**3.2**	3.6
Total	**33.5**	19.3

Provisions of \$1.2 million (2013 – \$0.2 million) have been made for impaired or irrecoverable balances and \$1.0 million (2013 – \$0.3 million) was released from the consolidated statement of comprehensive income in respect of bad debts. No provisions have been made against balances recoverable from reinsurers.

E. OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes or systems. The Group and its subsidiaries have identified and evaluated their key operational risks and these are incorporated in the risk registers and modeled directly within BLAST. The Group has also established, and monitors compliance with, internal operational risk tolerances. The RRC reviews operational risk on at least an annual basis and operational risk is covered in the CRO's quarterly report to the LHL and Entity Boards and the Cathedral Risk Committee reporting.

In order to manage operational risks, the Group has implemented a robust governance framework. Policies and procedures are documented and identify the key risks and controls within processes. The Group's Internal Audit function provides independent feedback with regard to the accuracy and completeness of key risks and controls, and independently verifies the effective operation of these through substantive testing. All higher risk areas are subject to an annual audit while compliance with tax operating guidelines is audited quarterly. Frequency of audits for all other areas varies from quarterly at the most frequent to a minimum of once every three years, on a rotational basis.

F. STRATEGIC RISK

The Group has identified several strategic risks. These include:

- the risks that either the poor execution of the business plan or an inappropriate business plan in itself results in a strategy that fails to adequately reflect the trading environment, resulting in an inability to optimise performance, including reputational risk;
- the risks of the failure to maintain adequate capital, accessing capital at an inflated cost or the inability to access capital. This includes unanticipated changes in vendor, regulatory and/or rating agency models that could result in an increase in capital requirements or a change in the type of capital required; and
- the risks of succession planning, staff retention and key man risks as strategic risks.

The Group has maintained elevated risk scores in the risk register relating to the integration of Cathedral into the Group's financial and actuarial reporting, but these will be reviewed in 2015.

I. BUSINESS PLAN RISKS

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

- an iterative annual forward-looking business planning process with cross departmental involvement, including the Cathedral team;
- evaluation of and approval of the annual business plan by the Board of Directors;
- regular monitoring of actual versus planned results;
- periodic review and re-forecasting as market conditions change; and
- feedback to senior management via the daily UMCC and fortnightly RRC meetings.

II. CAPITAL MANAGEMENT RISK

The total capital of the Group is as follows:

As at 31 December	2014 $m	2013 $m
Shareholders' equity	**1,356.8**	1,459.7
Long-term debt	**326.6**	332.3
Total capital	**1,683.4**	1,792.0
Intangible assets	**(153.8)**	(177.2)
Total tangible capital	**1,529.6**	1,614.8

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

- regular monitoring of current and prospective regulatory and rating agency capital requirements;
- regular discussion with the Cathedral management team regarding Lloyd's capital requirements;
- oversight of capital requirements by the Board of Directors;
- ability to purchase sufficient, cost effective reinsurance;
- maintaining contact with vendors, regulators and rating agencies in order to stay abreast of upcoming developments; and
- participation in industry groups such as the International Underwriters Association, the Association of Bermuda Insurers and Reinsurers and the Lloyd's Market Association.

The Group reviews the level and composition of capital on an ongoing basis with a view to:

- maintaining sufficient capital for underwriting opportunities and to meet obligations to policyholders;
- maximising the risk-adjusted return to shareholders within predetermined risk tolerances;
- maintaining adequate financial strength ratings; and
- meeting internal and regulatory capital requirements.

Capital is increased or returned as appropriate. The retention of earnings generated leads to an increase in capital. Capital raising can include debt or equity and returns of capital may be made through dividends, share repurchases, a redemption of debt or any combination thereof. Other capital management tools and products available to the Group may also be utilised. All capital actions require approval by the Board of Directors.

Internal methods have been developed to review the profitability of classes of business and their estimated capital requirements plus the capital requirements of the combination of a wide range of other risk categories. These approaches are used by management in decision making. The operating entities also conduct capital requirement assessments under internal measures and local regulatory requirements. Refer to note 30 for a discussion of the regulatory capital requirements of the Group's operating entities.

The Group's aim is to provide its shareholders with an RoE of 13.0 per cent in excess of a risk-free rate over the insurance cycle. The return is generated within a broad framework of risk parameters. The return is measured by management in terms of the IRR of the increase in FCBVS in the period adjusted for dividends accrued. This aim is a long-term goal, acknowledging that management expects both higher and lower results in the shorter term. The cyclicality and volatility of the insurance market is expected to be the largest driver of this pattern. Management monitors these peaks and troughs – adjusting the Group's portfolio to make the most effective use of available capital and seeking to maximise the risk-adjusted return.

IRR achieved is as follows:

	Annual return %	Compound annual return %	Inception to date return %
31 December 2005[1]	(3.2)	n/a	(3.2)
31 December 2006	17.8	14.0	14.0
31 December 2007	31.4	22.4	50.3
31 December 2008	7.8	17.9	63.7
31 December 2009	26.5	19.8	105.8
31 December 2010	23.3	20.3	152.4
31 December 2011	13.4	19.5	191.2
31 December 2012	16.7	19.2	242.7
31 December 2013	18.9	19.2	308.0
31 December 2014	13.9	18.9	375.3

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

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

	Annual return %	Compound annual return %	Inception to date return %
31 December 2005[1]	(3.4)	n/a	(3.4)
31 December 2006	13.0	9.2	9.2
31 December 2007	26.9	17.8	40.8
31 December 2008	6.4	14.3	52.7
31 December 2009	26.4	17.1	94.6
31 December 2010	23.2	18.2	141.1
31 December 2011	13.3	17.7	179.9
31 December 2012	16.6	17.7	231.3
31 December 2013	18.9	17.9	296.6
31 December 2014	13.9	17.7	363.8

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

III. RETENTION RISKS

Risks associated with succession planning, staff retention and key man risks are mitigated through a combination of resource planning processes and controls, including:

- the identification of key personnel with appropriate succession plans;
- identification of key team profit generators and function holders with targeted retention packages;
- documented recruitment procedures, position descriptions and employment contracts; and
- resource monitoring and the provision of appropriate compensation, including equity based compensation which vests over a defined time horizon, and training schemes.

1. GENERAL INFORMATION

The Group is a provider of global specialty insurance and reinsurance products with operations in the United Kingdom, Bermuda and Canada. LHL was incorporated under the laws of Bermuda on 12 October 2005. On 16 March 2009, LHL was added to the official list and its common shares were admitted to trading on the main market of the LSE; previously LHL's shares were listed on AIM, a subsidiary market of the LSE. Since 21 May 2007, LHL's shares have had a secondary listing on the BSX. LHL's registered office is Power House, 7 Par-la-Ville Road, Hamilton HM 11, Bermuda. LHL's head office is at Level 29, 20 Fenchurch Street, London, EC3M 3BY, United Kingdom.

The consolidated financial statements for the year ended 31 December 2014 include the Group's subsidiary companies, the Group's interest in associates, and the Group's share of syndicate assets and liabilities and income and expenses. A full listing of the Group's related parties can be found in note 27.

2. SEGMENTAL REPORTING

Management and the Board of Directors review the Group's business primarily by its five principal segments: Property, Energy, Marine, Aviation and Lloyd's. These segments are therefore deemed to be the Group's operating segments for the purposes of segment reporting. Further sub-classes of business are underwritten within each operating segment. The nature of these individual sub-classes is discussed further in the risk disclosures section on pages 104 to 107. Operating segment performance is measured by the net underwriting profit or loss and the combined ratio.

All amounts reported are transactions with external parties and associates. There are no inter-segmental transactions and there are no significant insurance or reinsurance contracts that insure or reinsure risks in Bermuda, the Group's country of domicile. Results included in the Lloyd's segment are from the date of completion of the Cathedral acquisition.

2. SEGMENTAL REPORTING CONTINUED

REVENUE AND EXPENSE BY OPERATING SEGMENT

For the year ended 31 December 2014	Property $m	Energy $m	Marine $m	Aviation $m	Lloyd's $m	Total $m
Gross premium written by geographical region						
Worldwide offshore	0.1	220.2	67.0	0.1	–	287.4
Europe	92.3	12.5	–	–	116.9	221.7
U.S. and Canada	33.4	3.7	–	53.1	82.3	172.5
Far East	34.6	0.9	–	–	24.1	59.6
Middle East	33.8	(0.1)	–	–	9.0	42.7
Worldwide, including the U.S. and Canada[1]	14.4	0.4	–	–	8.4	23.2
Worldwide, excluding the U.S. and Canada[2]	8.0	0.5	–	–	1.0	9.5
Rest of world	46.4	1.3	0.7	–	42.6	91.0
Total	263.0	239.4	67.7	53.2	284.3	907.6
Outwards reinsurance premiums	(34.3)	(47.8)	(9.7)	(8.1)	(64.9)	(164.8)
Change in unearned premiums	(9.9)	(22.5)	(0.3)	4.7	(9.0)	(37.0)
Change in unearned premiums ceded	2.7	0.6	–	2.8	3.7	9.8
Net premiums earned	221.5	169.7	57.7	52.6	214.1	715.6
Insurance losses and loss adjustment expenses	(12.0)	(55.2)	(27.6)	(32.9)	(110.2)	(237.9)
Insurance losses and loss adjustment expenses recoverable	(9.6)	13.3	–	–	7.7	11.4
Insurance acquisition expenses	(26.7)	(53.1)	(17.9)	(9.7)	(47.7)	(155.1)
Insurance acquisition expenses ceded	0.5	0.7	0.2	0.1	0.2	1.7
Net underwriting profit	173.7	75.4	12.4	10.1	64.1	335.7
Net unallocated income and expenses						(109.2)
Profit before tax						226.5
Net loss ratio	9.8%	24.7%	47.8%	62.5%	47.9%	31.7%
Net acquisition cost ratio	11.8%	30.9%	30.7%	18.3%	22.2%	21.4%
Expense ratio	–	–	–	–	–	15.6%
Combined ratio	21.6%	55.6%	78.5%	80.8%	70.1%	68.7%

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

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

REVENUE AND EXPENSE BY OPERATING SEGMENT

For the year ended 31 December 2013	Property $m	Energy $m	Marine $m	Aviation $m	Lloyd's $m	Total $m
Gross premium written by geographical region						
Worldwide offshore	–	191.9	61.3	0.1	–	253.3
Europe	36.4	0.4	0.1	–	1.5	38.4
U.S. and Canada	84.9	6.5	–	–	10.1	101.5
Far East	39.1	0.3	–	–	0.5	39.9
Middle East	16.5	0.2	–	–	–	16.7
Worldwide, including the U.S. and Canada[1]	85.4	7.2	0.9	48.8	8.7	151.0
Worldwide, excluding the U.S. and Canada[2]	18.7	0.4	–	–	0.3	19.4
Rest of world	52.4	3.0	0.7	–	3.4	59.5
Total	333.4	209.9	63.0	48.9	24.5	679.7
Outwards reinsurance premiums	(66.9)	(38.5)	(11.2)	(3.8)	(1.7)	(122.1)
Change in unearned premiums	(39.9)	27.8	9.9	(0.4)	26.9	24.3
Change in unearned premiums ceded	(7.8)	3.9	–	–	(9.9)	(13.8)
Net premiums earned	218.8	203.1	61.7	44.7	39.8	568.1
Insurance losses and loss adjustment expenses	(47.1)	(63.2)	(99.2)	(20.0)	(20.5)	(250.0)
Insurance losses and loss adjustment expenses recoverable	16.9	9.3	34.2	–	1.5	61.9
Insurance acquisition expenses	(37.8)	(56.9)	(21.7)	(10.1)	(8.6)	(135.1)
Insurance acquisition expenses ceded	8.4	0.7	0.2	–	–	9.3
Net underwriting profit	159.2	93.0	(24.8)	14.6	12.2	254.2
Net unallocated income and expenses						(36.1)
Profit before tax						218.1
Net loss ratio	13.8%	26.5%	105.3%	44.7%	47.7%	33.1%
Net acquisition cost ratio	13.4%	27.7%	34.8%	22.6%	21.6%	22.1%
Expense ratio	–	–	–	–	–	15.0%
Combined ratio	27.2%	54.2%	140.1%	67.3%	69.3%	70.2%

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

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

3. INVESTMENT RETURN

The total investment return for the Group is as follows:

For the year ended 31 December 2014	Net investment income and net other investment income $m	Net realised gains (losses) and impairments $m	Net change in unrealised gains /losses $m	Total investment return excluding foreign exchange $m	Foreign exchange gains (losses) $m	Total investment return including foreign exchange $m
Fixed income securities – AFS	**27.7**	**2.7**	**(1.8)**	**28.6**	**(9.5)**	**19.1**
Fixed income securities – at FVTPL	**1.6**	**–**	**–**	**1.6**	**–**	**1.6**
Equity securities – AFS	**0.5**	**(0.4)**	**(0.4)**	**(0.3)**	**–**	**(0.3)**
Hedge funds – at FVTPL	**2.1**	**–**	**–**	**2.1**	**–**	**2.1**
Other investments	**(2.3)**	**(8.2)**	**–**	**(10.5)**	**1.9**	**(8.6)**
Cash and cash equivalents	**0.4**	**–**	**–**	**0.4**	**(0.6)**	**(0.2)**
Total investment return	**30.0**	**(5.9)**	**(2.2)**	**21.9**	**(8.2)**	**13.7**

For the year ended 31 December 2013	Net investment income and net other investment income $m	Net realised gains (losses) and impairments $m	Net change in unrealised gains /losses $m	Total investment return excluding foreign exchange $m	Foreign exchange gains (losses) $m	Total investment return including foreign exchange $m
Fixed income securities – AFS	24.5	7.6	(33.8)	(1.7)	(3.1)	(4.8)
Fixed income securities – at FVTPL	(0.4)	–	–	(0.4)	–	(0.4)
Equity securities – AFS	0.1	–	0.5	0.6	–	0.6
Other investments	1.8	5.0	–	6.8	2.6	9.4
Cash and cash equivalents	0.8	–	–	0.8	(0.1)	0.7
Total investment return	26.8	12.6	(33.3)	6.1	(0.6)	5.5

Net realised gains (losses) and impairments includes impairment losses of $0.1 million (2013 – $nil) recognised on fixed income securities and $0.2 million (2013 – $nil) recognised on equity securities held by the Group.

Refer to page 116 in the risk disclosures section for the estimated fair values of the Group's derivative instruments. Realised gains and losses on futures and options contracts are included in net realised gains (losses) and impairments. The net impact of TBAs is $nil for all reporting periods.

Included in investment income is $5.7 million (2013 – $5.5 million) of investment management, accounting and custodian fees.

4. NET INSURANCE ACQUISITION EXPENSES

	2014 $m	2013 $m
Insurance acquisition expenses	**177.6**	132.4
Amortisation of value of in-force business acquired	**15.0**	8.5
Changes in deferred insurance acquisition expenses	**(30.8)**	(5.8)
Insurance acquisition expenses ceded	**(8.3)**	(8.7)
Changes in deferred insurance acquisition expenses ceded	**(0.1)**	(0.6)
Total net insurance acquisition expenses	**153.4**	125.8

A portion of the amortisation expense relating to the value of in-force business acquired has been allocated to insurance acquisition expenses, in line with the run-off profile of that business.

5. RESULTS OF OPERATING ACTIVITIES

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

	2014 $m	2013 $m
Depreciation on owned assets	**2.1**	1.4
Operating lease charges	**3.8**	2.4
Amortisation of value of in-force business	**8.4**	4.7
Auditors' remuneration		
– Group audit fees	**1.7**	1.3
– Other services	**0.3**	0.3
Total	**16.3**	10.1

During 2014, EY provided non-audit services in relation to taxation services, capital management projects, Cathedral group restructuring and services pursuant to the KCML subscription and shareholders' agreement. All fees paid to the Group's auditors for non-audit services are approved by the Group's Audit Committee.

In addition to the auditors' remuneration above, $0.5 million of fees were paid to the Group's auditors during the year ended 31 December 2013 in relation to their work performed in their role as Reporting Accountant for LHL's share issuance on 7 August 2013. The share issuance is discussed further in note 23. These fees are included in the Group's consolidated balance sheet as a deduction to share premium.

6. EMPLOYEE BENEFITS

	2014 $m	2013 $m
Wages and salaries	**27.4**	19.8
Pension costs	**3.0**	1.8
Bonus and other benefits	**23.7**	21.1
Total cash compensation	**54.1**	42.7
RSS – ordinary	**12.6**	13.9
RSS – bonus deferral	**3.2**	2.8
RSS – Cathedral acquisition grant	**7.5**	–
Total equity based compensation	**23.3**	16.7
Total employee benefits	**77.4**	59.4

EQUITY BASED COMPENSATION

The Group's primary equity based compensation scheme is its RSS. Previously the Group also issued options to employees pursuant to an LTIP, which has been closed to further issues, and also authorised and issued warrants at its formation in 2005 and 2006. Further details of the warrants can be found in note 24.

6. EMPLOYEE BENEFITS CONTINUED

RSS

On 22 December 2010, LHL's shareholders, in a Special General Meeting, voted in favour of the LHL Board's proposal to modify the existing RSS awards programme to a nil-cost options programme. The modification introduced an exercise period of ten years from the grant date for all outstanding and future RSS grants. Previously, all awards were automatically converted to shares on the vesting date.

The fair value of any TSR component of the nil-cost options is estimated using a stochastic model. For all other components the Black-Scholes model is used to estimate the fair value.

The following table lists the assumptions used in the stochastic model for the RSS awards granted during the years ended 31 December 2014 and 2013:

Assumptions	2014	2013
Dividend yield	**0.0%**	0.0%
Expected volatility[1]	**22.0%**	23.2%
Risk-free interest rate[2]	**1.0%**	0.40%
Expected average life of options	**3 years**	3 years
Share price	**$12.16**	$13.79

(1) The expected volatility of LHL and comparator companies' share prices are calculated based on the movement in the share prices over a period prior to the grant date, equal in length to the expected life of the award.

(2) The risk-free interest rate is consistent with 3 year UK government bond yields on the date of grant.

The calculation of the equity based compensation expense assumes forfeitures due to employee turnover of 10.0 per cent per annum prior to vesting, with subsequent adjustments to reflect actual experience.

RSS – ORDINARY

The ordinary RSS options vest after a three-year period and are dependent on certain performance criteria. A maximum of 75.0 per cent of the ordinary RSS options will vest only on the achievement of an LHL RoE in excess of a required amount. A maximum of 25.0 per cent of the ordinary RSS options will vest only on the achievement of an LHL TSR in excess of the 75th percentile of the TSR of a predefined comparator group. For all RSS options issued in 2012 and earlier the performance criteria was split as 50.0 per cent relating to RoE and 50.0 per cent relating to TSR. An amount equivalent to the dividends paid between the grant date and the exercise date accrues and is paid at the time of exercise, pro-rata according to the number of RSS options that vest.

	Number of employee restricted stock	Number of non-employee restricted stock	Total number of restricted stock
Outstanding as at 31 December 2012	4,914,823	561,327	5,476,150
Granted	1,236,971	–	1,236,971
Exercised	(1,443,649)	(150,975)	(1,594,624)
Forfeited	(369,810)	–	(369,810)
Lapsed	(17,574)	(1,525)	(19,099)
Outstanding as at 31 December 2013	4,320,761	408,827	4,729,588
Granted	**1,157,761**	**–**	**1,157,761**
Exercised[1]	**(1,894,668)**	**(186,994)**	**(2,081,662)**
Forfeited	**(166,857)**	**–**	**(166,857)**
Lapsed[1]	**(262,781)**	**–**	**(262,781)**
Outstanding as at 31 December 2014	**3,154,216**	**221,833**	**3,376,049**
Exercisable as at 31 December 2014	**1,316,281**	**221,833**	**1,538,114**

(1) Richard Brindle, the Group's former CEO, retired on 30 April 2014. He was treated as a good leaver and in line with RSS plan rules his outstanding unvested performance awards were tested for performance at cessation. Based on the agreed upon vesting conditions 406,129 awards vested and 262,781 lapsed. Mr Brindle exercised these awards plus an additional 138,086 vested awards and opted to receive payment in cash. These vested awards have been treated as cash-settled under IFRS 2.

	2014			2013		
	Employee restricted stock	**Non-employee restricted stock**	**Total restricted stock**	Employee restricted stock	Non-employee restricted stock	Total restricted stock
Weighted average remaining contractual life	**7.9 years**	**6.8 years**	**7.9 years**	7.9 years	7.5 years	7.9 years
Weighted average fair value at date of grant during the year	**$12.25**	**–**	**$12.25**	$11.80	–	$11.80
Weighted average share price at date of exercise during the year	**$11.35**	**$10.66**	**$11.29**	$12.80	$12.44	$12.76

RSS – BONUS DEFERRAL

The bonus deferral RSS options vesting periods range from one to three years from the date of grant and do not have associated performance criteria for vesting. An amount equivalent to the dividends paid between the grant date and the exercise date accrues and is paid at the time of exercise.

	Number of employee restricted stock	Number of non-employee restricted stock	Total number of restricted stock
Outstanding as at 31 December 2012	657,343	103,639	760,982
Granted	179,633	7,664	187,297
Exercised	(470,410)	(86,382)	(556,792)
Forfeited	(11,345)	–	(11,345)
Outstanding as at 31 December 2013	355,221	24,921	380,142
Granted	**278,608**	**–**	**278,608**
Exercised[1]	**(266,228)**	**(11,183)**	**(277,411)**
Forfeited	**(3,991)**	**–**	**(3,991)**
Outstanding as at 31 December 2014	**363,610**	**13,738**	**377,348**
Exercisable as at 31 December 2014	**74,079**	**–**	**74,079**

(1) Richard Brindle, the Group's former CEO, retired on 30 April 2014. He was treated as a good leaver and in line with RSS plan rules his 132,643 outstanding bonus deferral awards vested in full at cessation. Mr Brindle exercised these awards plus an additional 40,568 vested awards and opted to receive payment in cash. These vested awards have been treated as cash-settled under IFRS 2.

	2014			2013		
	Employee restricted stock	**Non-employee restricted stock**	**Total restricted stock**	Employee restricted stock	Non-employee restricted stock	Total restricted stock
Weighted average remaining contractual life	**8.4 years**	**7.6 years**	**8.4 years**	8.4 years	8.5 years	8.4 years
Weighted average fair value at date of grant during the year	**$12.14**	**–**	**$12.14**	$13.84	$12.71	$13.85
Weighted average share price at date of exercise during the year	**$11.40**	**$11.08**	**$11.39**	$12.59	$12.48	$12.57

6. EMPLOYEE BENEFITS CONTINUED

RSS – CATHEDRAL ACQUISITION

The Cathedral acquisition RSS options vesting periods range from three to five years and are dependent on certain performance criteria. A maximum of 75.0 per cent of the Cathedral acquisition RSS options will vest only on the achievement of a Cathedral combined ratio below a required amount. A maximum of 25.0 per cent of the Cathedral acquisition RSS options will vest only on the achievement of an LHL RoE in excess of a required amount. An amount equivalent to the dividends paid between the grant date and the exercise date accrues and is paid at the time of exercise. The awards are not exercisable as at 31 December 2014.

	Total number of restricted stock
Outstanding as at 31 December 2012	–
Granted	**2,307,157**
Outstanding as at 31 December 2014 and 2013	**2,307,157**

	Total restricted stock
Weighted average remaining contractual life	**8.9 years**
Weighted average fair value at date of grant	**$13.01**

LTIP

The LTIP plan was closed on 4 January 2008. 25.0 per cent of LTIP options vested on each of the first, second, third and fourth anniversary of the grant date. There were no associated performance criteria. All outstanding LTIP options were exercised during 2013.

	Number	Weighted average exercise price
Outstanding as at 31 December 2013 and 2012	133,836	$0.98
Exercised	(133,836)	$0.80
Outstanding and exercisable as at 31 December 2014 and 2013	**–**	**–**

	2014	2013
Weighted average remaining contractual life	**–**	–
Weighted average share price at date of exercise during the year	**–**	$13.23

As approved by the Remuneration Committee on 18 November 2009, all option exercise prices were automatically adjusted on the dividend record date to neutralise the devaluing impact of dividends payments.

MANAGEMENT TEAM ORDINARY WARRANTS

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

	Number	Weighted average exercise price
Outstanding as at 31 December 2013 and 2012	6,184,399	$4.64
Exercised	(5,625,217)	$4.63
Outstanding and exercisable as at 31 December 2014	**559,182**	**$4.72**

	2014	2013
Weighted average remaining contractual life	**1.0 year**	2.0 years
Weighted average share price at date of exercise during the year	**$10.55**	–

MANAGEMENT TEAM PERFORMANCE WARRANTS

Performance warrants were all fully vested by 31 December 2009. All performance warrants will expire ten years from the date of issue. Vesting was dependent on achieving certain performance criteria. The fair value of all warrants granted was $2.62 per warrant. The exercise price of warrants was automatically adjusted for dividends declared prior to their vesting dates.

Performance warrants granted and outstanding are:

	Number	Weighted average exercise price
Outstanding as at 31 December 2013 and 2012	859,445	$3.62
Exercised	(741,965)	$3.62
Outstanding and exercisable as at 31 December 2014	**117,480**	**$3.62**

	2014	2013
Weighted average remaining contractual life	**1.0 year**	2.0 years
Weighted average share price at date of exercise during the year	**$11.07**	–

Refer to note 24 for further disclosure on non-management warrants outstanding.

7. FINANCING COSTS

	2014 $m	2013 $m
Interest expense on long-term debt	**15.5**	13.2
Net losses (gains) on interest rate swaps	**7.4**	(5.2)
Other financing costs	**0.9**	0.9
Total	**23.8**	8.9

Refer to note 22 for details of long-term debt and financing arrangements.

8. TAX CHARGE

BERMUDA

LHL, LICL and LUK have received an undertaking from the Bermuda government exempting them from all Bermuda local income, withholding and capital gains taxes until 28 March 2035. At the present time no such taxes are levied in Bermuda.

UNITED KINGDOM

LHL and its UK subsidiaries are subject to normal UK corporation tax on all their taxable profits.

Tax charge	2014 $m	2013 $m
Corporation tax charge (credit) for the period	**0.4**	(2.6)
Adjustments in respect of prior period corporation tax	**0.2**	(1.1)
Deferred tax (credit) charge for the period	**(2.9)**	3.8
Tax rate change adjustment	**(0.8)**	(2.9)
Adjustments in respect of prior period deferred tax	**–**	(1.0)
Total tax credit	**(3.1)**	(3.8)

Tax reconciliation	2014 $m	2013 $m
Profit before tax	**226.5**	218.1
UK corporation tax at 21.5% (2013 – 23.3%)	**48.7**	50.7
Non-taxable income	**(59.8)**	(51.0)
Adjustments in respect of prior period	**0.2**	(2.1)
Differences related to equity based compensation	**(8.5)**	0.1
Other expense permanent differences	**2.2**	1.4
Tax rate change adjustment	**(0.8)**	(2.9)
Unused tax losses not recognised for deferred tax	**14.9**	–
Total tax credit	**(3.1)**	(3.8)

Due to the different taxpaying jurisdictions throughout the Group, the current tax charge as a percentage of the Group's profit before tax is 0.3 per cent (2013 – negative 1.7 per cent).

A corporation tax credit of $nil (2013 – $1.1 million) was recognised in other reserves which relates to tax deductions for equity based compensation award exercises in excess of the cumulative expense at the reporting date. Refer to note 16 for further details of tax credits included in other reserves.

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

The UK corporation tax rate as at 31 December 2014 was 21.0 per cent (effective from 1 April 2014). Until 1 April 2014 the UK corporation tax rate of 23.0 per cent applied. On 17 July 2013 reductions to 21.0 per cent from 1 April 2014 and to 20.0 per cent from 1 April 2015 were enacted. These rates have been reflected in the closing deferred tax position on the balance sheet.

9. CASH AND CASH EQUIVALENTS

	2014 $m	2013 $m
Cash at bank and in hand	**210.6**	297.2
Cash equivalents	**92.9**	105.8
Total cash and cash equivalents	**303.5**	403.0

Cash equivalents have an original maturity of three months or less. The carrying amount of these assets approximates their fair value. Refer to note 22 for the cash and cash equivalent balances on deposit as collateral.

10. INVESTMENTS

As at 31 December 2014	Cost or amortised cost $m	Gross unrealised gain $m	Gross unrealised loss $m	Estimated fair value $m
Fixed income securities – AFS				
– Short-term investments	**30.4**	**–**	**–**	**30.4**
– Fixed income funds	**17.1**	**0.5**	**(2.2)**	**15.4**
– U.S. treasuries	**363.0**	**1.0**	**(1.0)**	**363.0**
– Other government bonds	**88.5**	**0.8**	**(5.3)**	**84.0**
– U.S. municipal bonds	**28.6**	**0.4**	**(0.1)**	**28.9**
– U.S. government agency debt	**17.3**	**0.3**	**(0.1)**	**17.5**
– Asset backed securities	**185.1**	**0.3**	**(1.3)**	**184.1**
– U.S. government agency mortgage backed securities	**165.9**	**2.8**	**(0.7)**	**168.0**
– Non-agency mortgage backed securities	**20.9**	**0.3**	**(0.4)**	**20.8**
– Agency commercial mortgage backed securities	**2.4**	**–**	**–**	**2.4**
– Non-agency commercial mortgage backed securities	**39.0**	**0.6**	**–**	**39.6**
– Bank loans	**131.2**	**0.1**	**(3.4)**	**127.9**
– Corporate bonds	**707.0**	**3.4**	**(5.3)**	**705.1**
Total fixed income securities – AFS	**1,796.4**	**10.5**	**(19.8)**	**1,787.1**
Fixed income securities – at FVTPL	**30.0**	**1.2**	**–**	**31.2**
Equity securities – AFS	**15.8**	**2.0**	**(2.0)**	**15.8**
Hedge funds – at FVTPL	**150.0**	**4.3**	**(2.2)**	**152.1**
Other investments	**–**	**0.7**	**–**	**0.7**
Total investments	**1,992.2**	**18.7**	**(24.0)**	**1,986.9**

10. INVESTMENTS CONTINUED

As at 31 December 2013	Cost or amortised cost $m	Gross unrealised gain $m	Gross unrealised loss $m	Estimated fair value $m
Fixed income securities – AFS				
– Short-term investments	231.0	0.1	(0.1)	231.0
– Fixed income funds	26.4	0.4	(0.5)	26.3
– U.S. treasuries	218.5	0.1	(1.3)	217.3
– Other government bonds	111.1	0.8	(4.0)	107.9
– U.S. municipal bonds	21.3	0.3	(0.2)	21.4
– U.S. government agency debt	99.0	–	(0.8)	98.2
– Asset backed securities	150.4	1.1	(0.1)	151.4
– U.S. government agency mortgage backed securities	252.5	3.5	(4.0)	252.0
– Non-agency mortgage backed securities	8.7	0.1	–	8.8
– Agency commercial mortgage backed securities	4.1	0.1	–	4.2
– Non-agency commercial mortgage backed securities	36.9	1.0	–	37.9
– Bank loans	107.3	0.6	(0.1)	107.8
– Corporate bonds	698.0	6.0	(2.1)	701.9
Total fixed income securities – AFS	1,965.2	14.1	(13.2)	1,966.1
Fixed income securities – at FVTPL	30.0	–	(0.4)	29.6
Equity securities – AFS	15.1	0.8	(0.3)	15.6
Other investments	2.6	3.5	(1.4)	4.7
Total investments	2,012.9	18.4	(15.3)	2,016.0

Accumulated other comprehensive income is in relation to the Group's AFS fixed income and equity securities and is as follows:

	2014 $m	2013 $m
Gross unrealised gains	**12.5**	14.9
Gross unrealised losses	**(21.8)**	(13.5)
Net foreign exchange losses on fixed income – AFS	**10.3**	1.8
Tax provision	**(0.2)**	(0.3)
Accumulated other comprehensive income	**0.8**	2.9

Fixed income maturities are presented in the risk disclosures section on page 121. Refer to note 22 for the investment balances in trusts in favour of ceding companies and on deposit as collateral.

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

LEVEL (I)

Level (i) investments are securities with quoted prices in active markets. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. The Group determines securities classified as level (i) to include highly liquid U.S. treasuries, certain highly liquid short-term investments and quoted equity securities.

LEVEL (II)

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

- broker-dealer quotes;
- pricing models or matrix pricing;
- present values;
- future cash flows;
- yield curves;
- interest rates;
- prepayment speeds; and
- default rates.

Other similar quoted instruments or market transactions may be used.

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

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

10. INVESTMENTS CONTINUED

LEVEL (III)

Level (iii) investments are securities for which valuation techniques are not based on observable market data. The Group classifies hedge funds as Level (iii) assets as the valuation technique incorporates both observable and unobservable inputs.

The estimated fair values of the Group's hedge funds are determined using a combination of the most recent NAVs provided by each fund's independent administrator and the estimated performance provided by each hedge fund manager. Independent administrators provide monthly reported NAVs with up to a one-month delay in valuation. The most recent NAV available for each hedge fund is adjusted for the estimated performance, as provided by the fund manager, between the NAV date and the reporting date. Estimated fair values incorporating these performance estimates have not been significantly different from subsequent NAVs. Given the Group's knowledge of the underlying investments and the size of the Group's investment therein, we would not anticipate any material variance between estimated valuations.

The Group determines the estimated fair value of each individual security utilising the highest level inputs available. Prices for the Group's investment portfolio are provided by a third-party investment accounting firm whose pricing processes and the controls thereon are subject to an annual audit on both the operation, and the effectiveness, of those controls. The audit reports are available to clients of the firm and the report is reviewed annually by management. In accordance with their pricing policy, various recognised reputable pricing sources are used including index providers, broker-dealers and pricing vendors. The pricing sources use bid prices where available, otherwise indicative prices are quoted based on observable market trade data. The prices provided are compared to the investment managers' and custodian's pricing. The Group has not made any adjustments to any pricing provided by independent pricing services or its third-party investment managers for either year ending 31 December.

The Group determines whether transfers have occurred between levels of the fair value hierarchy by re-assessing the categorisation at the end of each reporting period based on the lowest level input that is significant to the fair value measurement as a whole.

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

As at 31 December 2014	Level (i) $m	Level (ii) $m	Level (iii) $m	Total $m
Fixed income securities – AFS				
– Short-term investments	30.3	0.1	–	30.4
– Fixed income funds	–	15.4	–	15.4
– U.S. treasuries	363.0	–	–	363.0
– Other government bonds	–	84.0	–	84.0
– U.S. municipal bonds	–	28.9	–	28.9
– U.S. government agency debt	–	17.5	–	17.5
– Asset backed securities	–	184.1	–	184.1
– U.S. government agency mortgage backed securities	–	168.0	–	168.0
– Non-agency mortgage backed securities	–	20.8	–	20.8
– Agency commercial mortgage backed securities	–	2.4	–	2.4
– Non-agency commercial mortgage backed securities	–	39.6	–	39.6
– Bank loans	–	127.9	–	127.9
– Corporate bonds	–	705.1	–	705.1
Total fixed income securities – AFS	**393.3**	**1,393.8**	**–**	**1,787.1**
Fixed income securities – at FVTPL	–	31.2	–	31.2
Equity securities – AFS	–	15.8	–	15.8
Hedge funds – at FVTPL	–	–	152.1	152.1
Other investments	–	0.7	–	0.7
Total investments	**393.3**	**1,441.5**	**152.1**	**1,986.9**

As at 31 December 2013	Level (i) $m	Level (ii) $m	Level (iii) $m	Total $m
Fixed income securities – AFS				
– Short-term investments	153.5	77.5	–	231.0
– Fixed income funds	–	26.3	–	26.3
– U.S. treasuries	217.3	–	–	217.3
– Other government bonds	–	107.9	–	107.9
– U.S. municipal bonds	–	21.4	–	21.4
– U.S. government agency debt	–	98.2	–	98.2
– Asset backed securities	–	151.4	–	151.4
– U.S. government agency mortgage backed securities	–	252.0	–	252.0
– Non-agency mortgage backed securities	–	8.8	–	8.8
– Agency commercial mortgage backed securities	–	4.2	–	4.2
– Non-agency commercial mortgage backed securities	–	37.9	–	37.9
– Bank loans	–	107.8	–	107.8
– Corporate bonds	–	701.9	–	701.9
Total fixed income securities – AFS	370.8	1,595.3	–	1,966.1
Fixed income securities – at FVTPL	–	29.6	–	29.6
Equity securities – AFS	15.6	–	–	15.6
Other investments	–	4.7	–	4.7
Total investments	386.4	1,629.6	–	2,016.0

There have been no transfers between Levels (i) and (ii), therefore no reconciliations have been presented.

The table below analyses the movements in assets classified as Level (iii) investments during the year ended 31 December 2014:

	2014 $m
As at 31 December 2013	**–**
Purchases	**150.0**
Total net gains recognised in other investment income in profit or loss	**2.1**
As at 31 December 2014	**152.1**

During the year ended 31 December 2014, the Group recognised $4.3 million of unrealised gains in other investment income in profit or loss for Level (iii) investments held at the reporting date. During the year ended 31 December 2013, the Group did not hold any Level (iii) investments.

11. INTERESTS IN STRUCTURED ENTITIES

A. CONSOLIDATED STRUCTURED ENTITIES

The Group's only consolidated structured entity is the EBT. The Group provides capital contributions to the EBT to enable it to meet its obligations to employees under the equity based compensation plans. The Group has a contractual agreement which may require it to provide financial support to the EBT.

B. UNCONSOLIDATED STRUCTURED ENTITIES IN WHICH THE GROUP HAS AN INTEREST

As part of its investment activities, the Group invests in unconsolidated structured entities. As at December 2014, the Group's total interest in unconsolidated structured entities was $619.7 million. The Group does not sponsor any of the unconsolidated structured entities.

11. INTERESTS IN STRUCTURED ENTITIES CONTINUED

As at 31 December 2014, a summary of the Group's interest in unconsolidated structured entities is as follows:

As at 31 December 2014	Investments $m	Interest in associates $m	Total $m
Fixed income securities			
– Asset backed securities	**184.1**	**–**	**184.1**
– U.S. government agency mortgage backed securities	**168.0**	**–**	**168.0**
– Non-agency mortgage backed securities	**20.8**	**–**	**20.8**
– Agency commercial mortgage backed securities	**2.4**	**–**	**2.4**
– Non-agency commercial mortgage backed securities	**39.6**	**–**	**39.6**
Total fixed income securities	**414.9**	**–**	**414.9**
Investment funds			
– Hedge funds	**152.1**	**–**	**152.1**
Total investment funds	**152.1**	**–**	**152.1**
Specialised investment vehicles			
– KHL (see note 17)	**–**	**52.7**	**52.7**
Total	**567.0**	**52.7**	**619.7**

The fixed income securities structured entities are created to meet specific investment needs of borrowers and investors which cannot be met from standardised financial instruments available in the capital markets. As such, they provide liquidity to the borrowers in these markets and provide investors with an opportunity to diversify risk away from standard fixed income securities. Whilst individual securities may differ in structure, the principles of the instruments are broadly the same and it is appropriate to aggregate the investments into the categories detailed above.

The risk that the Group faces in respect of the investments in structured entities is similar to the risk it faces in respect of other financial investments held on the balance sheet in that fair value is determined by market supply and demand. This is in turn driven by investor evaluation of the credit risk of the structure and changes in term structure of interest rates which change investors expectation of the cash flows associated with the instrument and, therefore, its value in the market. Risk management disclosure for these financial instruments and other investments is provided on pages 111 to 123. The total assets of these entities are not considered meaningful for the purpose of understanding the related risks and therefore have not been presented.

The maximum exposure to loss in respect of these structured entities would be the carrying value of the instruments that the Group holds as at 31 December 2014. Generally, default rates would have to increase substantially from their current level before the Group would suffer a loss and this assessment is made prior to investing and continually through the holding period for the security.

The Group has not provided any other financial or other support in relation to any other to that described above as at the reporting date, and there are no intentions to provide support in relation to any other unconsolidated structured entities in the foreseeable future.

12. REINSURANCE ASSETS AND LIABILITIES

	Unearned premiums ceded $m	Amounts payable to reinsurers $m	Other receivables $m	Total $m
As at 31 December 2012	11.5	(30.6)	4.5	(14.6)
Acquired in the Cathedral acquisition	17.2	(22.0)	13.7	8.9
Net deferral for prior years[1]	(23.3)	–	–	(23.3)
Net deferral for current year	9.5	–	–	9.5
Other	–	21.7	(7.4)	14.3
As at 31 December 2013	14.9	(30.9)	10.8	(5.2)
Net deferral for prior years	**(14.9)**	**–**	**–**	**(14.9)**
Net deferral for current year	**24.7**	**–**	**–**	**24.7**
Other	**–**	**(3.3)**	**(5.5)**	**(8.8)**
As at 31 December 2014	**24.7**	**(34.2)**	**5.3**	**(4.2)**

(1) Includes movement in deferral for reinsurance assets and liabilities acquired in the acquisition of Cathedral.

13. LOSSES AND LOSS ADJUSTMENT EXPENSES

	Losses and loss adjustment expenses $m	Reinsurance recoveries $m	Net losses and loss adjustment expenses $m
As at 31 December 2012	537.4	(73.0)	464.4
Assumed in the Cathedral acquisition	331.5	(107.3)	224.2
Net incurred losses for:			
Prior years	41.9	(57.8)	(15.9)
Current year	208.1	(4.1)	204.0
Exchange adjustments	(13.6)	(0.7)	(14.3)
Incurred losses and loss adjustment expenses	236.4	(62.6)	173.8
Net paid losses for:			
Prior years	200.3	(59.8)	140.5
Current year	51.6	(0.1)	51.5
Paid losses and loss adjustment expenses	251.9	(59.9)	192.0
As at 31 December 2013	853.4	(183.0)	670.4
Net incurred losses for:			
Prior years	**(40.8)**	**6.4**	**(34.4)**
Current year	**278.7**	**(17.8)**	**260.9**
Exchange adjustments	**(11.8)**	**0.8**	**(11.0)**
Incurred losses and loss adjustment expenses	**226.1**	**(10.6)**	**215.5**
Net paid losses for:			
Prior years	**265.8**	**(76.4)**	**189.4**
Current year	**61.1**	**(4.8)**	**56.3**
Paid losses and loss adjustment expenses	**326.9**	**(81.2)**	**245.7**
As at 31 December 2014	**752.6**	**(112.4)**	**640.2**

Further information on the calculation of loss reserves and the risks associated with them is provided in the risk disclosures section from page 108. The risks associated with general insurance contracts are complex and do not readily lend themselves to meaningful sensitivity analysis. The impact of an unreported event could lead to a significant increase in the Group's loss reserves. The Group believes that the loss reserves established are adequate, however a 20.0 per cent increase in estimated losses would lead to a $150.5 million (2013 – $170.7 million) increase in gross loss reserves. There was no change to the Group's reserving methodology during the year. The split of losses and loss adjustment expenses between notified outstanding losses, additional case reserves assessed by management and IBNR is shown below:

	2014		2013	
As at 31 December	**$m**	**%**	$m	%
Outstanding losses	**369.3**	**49.1**	501.1	58.7
Additional case reserves	**159.7**	**21.2**	115.0	13.5
Losses incurred but not reported	**223.6**	**29.7**	237.3	27.8
Total	**752.6**	**100.0**	853.4	100.0

The Group's reserve for unpaid losses and loss adjustment expenses as at 31 December 2014 and 2013 had an estimated duration of approximately two years.

13. LOSSES AND LOSS ADJUSTMENT EXPENSES CONTINUED

CLAIMS DEVELOPMENT

The development of insurance liabilities is indicative of the Group's ability to estimate the ultimate value of its insurance liabilities. The Group began writing insurance and reinsurance business in December 2005. With the acquisition of Cathedral, the Group has assumed loss reserves relating to 2001 and subsequent years.

Accident year	2006 and prior $m	2007 $m	2008 $m	2009 $m	2010 $m	2011 $m	2012 $m	2013 $m	2014 $m	Total $m
Group gross losses[1]										
Estimate of ultimate liability[2]										
At end of accident year	39.1	154.8	444.6	163.3	297.4	397.0	250.3	280.0	274.8	
One year later	34.7	131.2	417.4	107.8	209.4	371.9	350.4	259.8		
Two years later	32.0	103.5	377.5	73.1	204.2	447.0	338.8			
Three years later	27.6	94.8	345.1	66.0	235.8	450.4				
Four years later	27.2	83.5	340.8	89.1	229.4					
Five years later	24.4	81.0	355.6	81.7						
Six years later	24.0	87.6	350.9							
Seven years later	60.6	87.8								
Eight years later	58.6									
Current estimate of cumulative liability	**58.6**	**87.8**	**350.9**	**81.7**	**229.4**	**450.4**	**338.8**	**259.8**	**274.8**	**2,132.2**
Payments made	**(26.0)**	**(78.9)**	**(337.6)**	**(57.0)**	**(188.6)**	**(262.1)**	**(233.3)**	**(135.0)**	**(61.1)**	**(1,379.6)**
Total Group gross liability	**32.6**	**8.9**	**13.3**	**24.7**	**40.8**	**188.3**	**105.5**	**124.8**	**213.7**	**752.6**

(1) Balances at 31 December 2013 include the addition of losses assumed in the Cathedral acquisition on 7 November 2013.

(2) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2014.

Accident year	2006 and prior $m	2007 $m	2008 $m	2009 $m	2010 $m	2011 $m	2012 $m	2013 $m	2014 $m	Total $m
Reinsurance[1]										
Estimate of ultimate recovery[2]										
At end of accident year	–	3.6	40.7	1.6	33.8	56.2	48.9	9.9	17.8	
One year later	–	6.2	47.1	1.3	23.6	52.6	121.8	8.9		
Two years later	–	4.0	43.1	0.7	24.1	92.4	122.0			
Three years later	–	3.5	40.9	0.7	33.5	88.9				
Four years later	–	3.3	38.1	10.0	34.4					
Five years later	–	3.1	40.7	7.0						
Six years later	–	4.0	39.8							
Seven years later	25.1	4.1								
Eight years later	25.1									
Current estimate of cumulative recovery	**25.1**	**4.1**	**39.8**	**7.0**	**34.4**	**88.9**	**122.0**	**8.9**	**17.8**	**348.0**
Payments made	**(2.3)**	**(3.5)**	**(38.7)**	**(1.9)**	**(28.0)**	**(42.2)**	**(110.6)**	**(3.6)**	**(4.8)**	**(235.6)**
Total Group gross recovery	**22.8**	**0.6**	**1.1**	**5.1**	**6.4**	**46.7**	**11.4**	**5.3**	**13.0**	**112.4**

(1) Balances at 31 December 2013 include the addition of losses assumed in the Cathedral acquisition on 7 November 2013.

(2) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2014.

Accident year	2006 and prior $m	2007 $m	2008 $m	2009 $m	2010 $m	2011 $m	2012 $m	2013 $m	2014 $m	Total $m
Net Group losses[1]										
Estimate of ultimate liability[2]										
At end of accident year	39.1	151.2	403.9	161.7	263.6	340.8	201.4	270.1	257.0	
One year later	34.7	125.0	370.3	106.5	185.8	319.3	228.6	250.9		
Two years later	32.0	99.5	334.4	72.4	180.1	354.6	216.8			
Three years later	27.6	91.3	304.2	65.3	202.3	361.5				
Four years later	27.2	80.2	302.7	79.1	195.0					
Five years later	24.4	77.9	314.9	74.7						
Six years later	24.0	83.6	311.1							
Seven years later	35.5	83.7								
Eight years later	33.5									
Current estimate of cumulative liability	**33.5**	**83.7**	**311.1**	**74.7**	**195.0**	**361.5**	**216.8**	**250.9**	**257.0**	**1,784.2**
Payments made	**(23.7)**	**(75.4)**	**(298.9)**	**(55.1)**	**(160.6)**	**(219.9)**	**(122.7)**	**(131.4)**	**(56.3)**	**(1,144.0)**
Total Group net liability	**9.8**	**8.3**	**12.2**	**19.6**	**34.4**	**141.6**	**94.1**	**119.5**	**200.7**	**640.2**

(1) Balances at 31 December 2013 include the addition of losses assumed in the Cathedral acquisition on 7 November 2013.

(2) Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2014.

The inherent uncertainty in reserving gives rise to favourable or adverse development on the established reserves. The total favourable development on net losses and loss adjustment expenses, excluding the impact of foreign exchange revaluations, was as follows:

	2014 $m	2013 $m
2006 accident year and prior	**1.8**	(0.7)
2007 accident year	**(0.3)**	(0.9)
2008 accident year	**3.6**	(4.1)
2009 accident year	**4.3**	2.0
2010 accident year	**5.7**	1.4
2011 accident year	**(6.1)**	(4.1)
2012 accident year	**11.1**	22.3
2013 accident year	**14.3**	–
Total favourable development	**34.4**	15.9

The favourable prior year development in 2014 arose primarily from IBNR releases due to lower than expected reported losses and releases on settlement of outstanding losses, offset by adverse development on prior accident year mid-sized marine and energy claims. The favourable prior year development in 2013 arose primarily from IBNR releases due to fewer than expected reported losses, a benefit from the settlement on our North East ILW in relation to Sandy and releases on the settlement of outstanding losses. This favourable development was offset to an extent by unfavourable development of $33.5 million after reinsurance on the Costa Concordia marine loss.

13. LOSSES AND LOSS ADJUSTMENT EXPENSES CONTINUED

During 2012 the Group was impacted by significant losses in relation to the total loss of the Costa Concordia. Management's current best estimate of the ultimate net loss in relation to this event is $100.7 million. The 90th percentile of the loss distribution for this estimate is $103.3 million with the 95th percentile being $104.2 million. Significant uncertainty exists on the eventual ultimate loss in relation to this event.

During 2012 the Group was also impacted by significant losses in relation to Sandy. Management's current best estimate of the ultimate net loss in relation to this event is $24.7 million. The 90th percentile of the loss distribution for this estimate is $48.7 million with the 95th percentile being $50.6 million. Significant uncertainty exists on the eventual ultimate loss.

The Group's estimated ultimate net losses, after reinstatement premiums, for these significant events are as follows:

	Sandy $m	Costa Concordia $m
Net ultimate losses as at 31 December 2012	44.5	59.2
Assumed in the Cathedral acquisition	6.8	–
Change in insurance losses and loss adjustment expenses	3.4	67.7
Change in insurance losses and loss adjustment expenses recoverable	(23.6)	(34.2)
Change in reinstatement premium	(0.4)	4.4
Net ultimate losses as at 31 December 2013	30.7	97.1
Change in insurance losses and loss adjustment expenses	**(6.3)**	**3.9**
Change in insurance losses and loss adjustment expenses recoverable	**–**	**–**
Change in reinstatement premium	**0.3**	**(0.3)**
Net ultimate losses as at 31 December 2014	**24.7**	**100.7**

14. INSURANCE, REINSURANCE AND OTHER RECEIVABLES

All receivables are considered current other than $71.3 million (2013 – $52.1 million) of inwards premiums receivable related to multi-year contracts. The carrying value approximates fair value due to the short-term nature of the receivables. There are no significant concentrations of credit risk within the Group's receivables.

15. DEFERRED ACQUISITION COSTS AND DEFERRED ACQUISITION COSTS CEDED

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

	Incurred $m	Ceded $m	Net $m
As at 31 December 2012	68.0	(0.8)	67.2
Net deferral during the year	132.4	(8.7)	123.7
(Expense) income for the year	(126.6)	9.3	(117.3)
As at 31 December 2013	73.8	(0.2)	73.6
Net deferral during the year	**177.6**	**(8.3)**	**169.3**
(Expense) income for the year	**(146.8)**	**8.4**	**(138.4)**
As at 31 December 2014	**104.6**	**(0.1)**	**104.5**

16. PROVISION FOR DEFERRED TAX

	2014 $m	2013 $m
Equity based compensation	**3.2**	8.5
Claims equalisation reserves	**(15.1)**	(16.7)
Syndicate underwriting profits	**(13.3)**	(11.2)
Syndicate participation rights	**(16.0)**	(16.4)
Other temporary differences	**(0.2)**	(5.1)
Tax losses carried forward	**2.7**	2.2
Net deferred tax liability	**(38.7)**	(38.7)

A deferred tax charge of $4.4 million (2013 – $0.5 million credit) was recognised in other reserves which relates to deferred tax credits for unexercised equity based compensation awards where the estimated market value is in excess of the cumulative expense at the reporting date.

Deferred tax assets are recognised to the extent that realising the related tax benefit through future taxable profits is likely. It is anticipated that sufficient taxable profits will be available within the Group in 2015 and subsequent years to utilise the deferred tax assets recognised when the underlying temporary differences reverse.

A deferred tax asset of $18.7 million (2013 – $3.2 million) has not been recognised in relation to unused tax losses carried forward in LHL, as at present the related tax benefit is not expected to be realised through future taxable profits.

All deferred tax assets and liabilities are classified as non-current.

17. INVESTMENT IN ASSOCIATES

KHL

The Group holds a 10.0 per cent interest in the preference shares of each segregated account of KHL, a company incorporated in Bermuda. KHL's operating subsidiary, KRL, is authorised by the BMA as a Special Purpose Insurer. KRL commenced writing insurance business on 1 January 2014. As at 31 December 2014, the carrying value of the Group's investment in KHL was $52.7 million (31 December 2013 – $20.1 million). The Group's share of comprehensive income for KHL for the period was $4.7 million (31 December 2013 – $nil). Key financial information for KHL is as follows:

	2014 $m	2013[1] $m
Assets	**551.2**	201.2
Liabilities	**24.6**	–
Shareholders' equity	**526.6**	201.2
Gross premium earned	**79.8**	–
Comprehensive income	**47.0**	–

(1) From the date of incorporation, 4 June 2013.

The Group has the power to participate in operational and financial policy decisions of KHL and KRL through the provision of essential technical information by KCML and has therefore classified its investment in KHL as an investment in associate.

Refer to note 27 for details of transactions between the Group, KHL, KRL and KCML.

During the year ended 31 December 2014, AHL, ARL, SHL and SRL were placed in member's voluntary liquidation. As at 31 December 2014, remaining assets and liabilities in AHL, ARL, SHL and SRL were negligible. As at 31 December 2014, the carrying value of the Group's investment in AHL is $nil (31 December 2013 – $32.4 million). As at 31 December 2014, the carrying value of the Group's investment in SHL is $nil (31 December 2013 – $12.2 million). The Group's share of comprehensive income for AHL for the year ended was $1.1 million (31 December 2013 – $6.6 million). The Group's share of comprehensive income for SHL for the year ended was $0.1 million (31 December 2013 – $2.6 million).

Refer to note 27 for details of transactions between the Group, AHL, ARL, SHL and SRL.

18. PROPERTY, PLANT AND EQUIPMENT

	2014 $m	2013 $m
Cost	**19.3**	14.3
Accumulated depreciation	**(10.2)**	(11.5)
Net book value	**9.1**	2.8

19. INTANGIBLE ASSETS

	Value of in-force business $m	Syndicate participation rights $m	Goodwill $m	Total $m
Net book value at 1 January 2013	–	–	–	–
Acquired in the Cathedral acquisition	36.6	82.6	71.2	190.4
Amortisation charge for the year through insurance acquisition expenses	(8.5)	–	–	(8.5)
Amortisation charge for the year through other operating expenses	(4.7)	–	–	(4.7)
Net book value at 31 December 2013	23.4	82.6	71.2	177.2
Amortisation charge for the year through insurance acquisition expenses	**(15.0)**	**–**	**–**	**(15.0)**
Amortisation charge for the year through other operating expenses	**(8.4)**	**–**	**–**	**(8.4)**
Net book value at 31 December 2014	**–**	**82.6**	**71.2**	**153.8**

Syndicate participation rights and goodwill are deemed to have indefinite life as they are expected to have value in use that does not diminish over the course of time. Consequently, the carrying value is not amortised but tested annually for impairment. The value of in-force business was amortised over the remaining life of the acquired insurance contracts, which was approximately one year.

For the purpose of impairment testing, intangible assets are allocated to the Group's CGUs, in accordance with the manner in which management operates and monitors the business. The syndicate participation rights and goodwill have therefore been allocated to the Lloyd's CGU.

When testing for impairment, the recoverable amount of the Lloyd's CGU is determined based on value in use. Value in use is calculated using projected cash flows based on the financial projections of the CGU. These are approved by management and cover a 3 year period. The most significant assumptions used to derive the projected cash flows include an assessment of business prospects, projected loss ratios, outwards reinsurance expenditure and investment returns. A discount rate of 8.0 per cent has been used to discount the projected post tax cash flows, which reflects a combination of factors including the Group's expected cost of equity and cost of borrowing. The growth rate used to extrapolate the cash flows of the unit beyond the 3 year period is 2.0 per cent based on historical growth rates and management's best estimate of future growth rates.

The results of this exercise indicate that the recoverable amount exceeds the intangible asset's carrying value for both the syndicate participation rights and goodwill and would not be sensitive to any reasonably possible changes in assumptions. Therefore no impairment has been recognised during the year ended 31 December 2014 (2013 – $nil).

20. INSURANCE LIABILITIES

	Unearned premiums $m	Other payables $m	Total $m
As at 31 December 2012	343.3	23.5	366.8
Acquired in the Cathedral acquisition	123.1	6.3	129.4
Net deferral for prior years[1]	(275.9)	–	(275.9)
Net deferral for current year	251.6	–	251.6
Other	–	(0.9)	(0.9)
As at 31 December 2013	442.1	28.9	471.0
Net deferral for prior years	**(330.5)**	**–**	**(330.5)**
Net deferral for current year	**367.5**	**–**	**367.5**
Other	**–**	**11.9**	**11.9**
As at 31 December 2014	**479.1**	**40.8**	**519.9**

(1) Includes movement in deferral for insurance liabilities acquired in the Cathedral acquisition.

21. INSURANCE, REINSURANCE AND OTHER PAYABLES

	2014 $m	2013 $m
Other payables	**81.2**	78.5
Accrued interest payable	**2.3**	2.2
Total other payables	**83.5**	80.7
Insurance contracts – other payables	**40.8**	28.9
Amounts payable to reinsurers	**34.2**	30.9
Total payables	**158.5**	140.5

Other payables include unsettled investment trades, accrued interest and other accruals. Insurance payables relate to amounts due to policyholders for profit commission, return premiums and claims payable. All payables are considered current. The carrying value approximates fair value due to the short-term nature of the payables.

22. LONG-TERM DEBT AND FINANCING ARRANGEMENTS

LONG-TERM DEBT

On 5 October 2012, the Group issued U.S. $130.0 million 5.70 per cent senior unsecured notes due 2022 pursuant to a private offering to U.S. Qualified Institutional Buyers. Interest on the principal is payable semi-annually. The notes were listed and admitted to trading on the LSE on 16 October 2012.

On 15 December 2005, the Group issued $97.0 million and €24.0 million in aggregate principal amount of floating rate subordinated loan notes. The U.S. dollar subordinated loan notes are repayable on 15 December 2035. Interest on the principal is based on a set margin, 3.70 per cent, above the three month LIBOR rate and is payable quarterly. The loan notes were issued via a trust company. The Euro subordinated loan notes are repayable on 15 June 2035. Interest on the principal is based on a set margin, 3.70 per cent, above the EURIBOR rate and is payable quarterly. On 21 October 2011, the Cayman Islands Stock Exchange admitted to the official list the Group's U.S. dollar and Euro subordinated loan notes due 2035.

In 2013, the Group assumed loan notes, issued by CCHL and listed on the ISE, as part of the Cathedral acquisition. The loan notes acquired are set out as follows:

- €12.0 million floating rate subordinated loan note issued on 18 November 2004 and repayable in September 2034, paying interest quarterly based on a set margin, 3.75 per cent, above three month EURIBOR;
- $10.0 million floating rate subordinated note loan issued on 26 November 2004 and repayable in September 2034, paying interest quarterly based on a set margin, 3.75 per cent, above three month LIBOR;
- $25.0 million floating rate subordinated loan note issued on 13 May 2005 and repayable in June 2035, paying interest quarterly based on a set margin, 3.25 per cent, above three month LIBOR; and
- $25.0 million floating rate subordinated loan note issued on 18 November 2005 and repayable in December 2035, paying interest quarterly based on a set margin, 3.25 per cent, above three month LIBOR.

22. LONG-TERM DEBT AND FINANCING ARRANGEMENTS CONTINUED

The Group has the option to redeem its senior unsecured notes and all of its subordinated loan notes, in whole or in part, prior to the respective maturity dates.

The carrying values of the notes are shown below:

As at 31 December	2014 $m	2013 $m
Long-term debt $130.0 million	**130.0**	130.0
Long-term debt $97.0 million	**97.0**	97.0
Long-term debt €24.0 million	**29.2**	33.0
Long-term debt €12.0 million	**13.0**	14.9
Long-term debt $10.0 million	**10.0**	10.0
Long-term debt $25.0 million	**23.7**	23.7
Long-term debt $25.0 million	**23.7**	23.7
Carrying value	**326.6**	**332.3**

The Group is exposed to cash flow interest rate risk and currency risk on its long-term debt. Further information is provided in the risk disclosures section on page 118.

The fair value of the long-term debt is estimated as $347.2 million (2013 – $341.2 million). The fair value measurement is classified within Level (ii) of the fair value hierarchy. The fair value is estimated by reference to similar financial instruments quoted in active markets.

The interest accrued on the long-term debt was $2.3 million (2013 – $2.2 million) at the balance sheet date and is included in other payables.

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

INTEREST RATE SWAPS

The Group hedges a portion of its floating rate borrowings using interest rate swaps to transfer floating to fixed rate. These instruments are held at estimated fair value. Refer to the risk disclosures section from page 117 for further details. The Group has the right to net settle these instruments.

The net fair value position owed by the Group on the swap agreements is a $4.9 million liability. Further information is provided on pages 115 and 117. The Group has the right to net settle these instruments. Cash settlements are completed on a quarterly basis and the total of the next cash settlement in the first quarter of 2015 on these instruments is $0.7 million. The net impact from cash settlement and changes in estimated fair value is included in financing costs.

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

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

LETTERS OF CREDIT

As both LICL and LUK are non-admitted insurers or reinsurers throughout the U.S., the terms of certain contracts require them to provide LOCs to policyholders as collateral. LHL and LICL have the following facilities in place as at 31 December 2014:

(i) a $350.0 million syndicated collateralised credit facility with a $75.0 million loan sub-limit that has been in place since 5 April 2012 and will expire on 5 April 2017. There was no outstanding debt under this facility as at 31 December 2014 and 2013; and

(ii) a $50.0 million bi-lateral uncommitted LOC facility with Citibank Europe PLC.

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

The terms of the $350.0 million LOC facility include standard default and cross-default provisions which require certain covenants to be adhered to. These include the following:

(i) an A.M. Best financial strength rating of at least B++; and

(ii) a maximum debt to capital ratio of 30.0 per cent, where the subordinated loan notes are excluded from this calculation.

As at all reporting dates the Group was in compliance with all covenants under these facilities. The $50.0 million bi-lateral uncommitted LOC facility does not contain default provisions or covenants.

The following LOCs have been issued:

As at 31 December	2014 $m	2013 $m
Issued to third parties	**31.8**	20.1

LOCs are required to be fully collateralised.

SYNDICATE BANK FACILITIES

As at 31 December 2014, Syndicate 2010 had in place an $80.0 million catastrophe facility with Barclays Bank plc. The facility is available to assist in paying claims and the gross funding of catastrophes for Syndicate 2010. Up to $50.0 million can be utilised by way of an LOC to assist Syndicate 2010's gross funding requirements.

As at 31 December 2014, Syndicate 3010 had in place a $40.0 million catastrophe facility with Barclays Bank plc. The facility is available to assist in paying claims and the gross funding of catastrophes for Syndicate 3010. Up to $20.0 million can be utilised by way of an LOC to assist gross funding requirements of Syndicate 3010.

There are no balances outstanding under either of the syndicate bank facilities as at 31 December 2014 or 2013. The syndicate bank facilities are not available to the Group other than through its participation on the syndicates it supports.

TRUSTS AND RESTRICTED BALANCES

The Group has several trust arrangements in place in favour of policyholders and ceding companies in order to comply with the security requirements of certain reinsurance contracts and/or the regulatory requirements of certain jurisdictions.

In 2012, LICL entered into an MBRT to collateralise its reinsurance liabilities associated with U.S. domiciled clients. As at 31 December 2014, LICL had been granted authorised or trusteed reinsurer status in all States (31 December 2013 – 45 States). The MBRT is subject to the rules and regulations of the aforementioned States and the respective deed of trust. These rules and regulations include minimum capital funding requirements, investment guidelines, capital distribution restrictions and regulatory reporting requirements.

As at and for the years ended 31 December 2014 and 2013, the Group was in compliance with all covenants under its trust facilities.

22. LONG-TERM DEBT AND FINANCING ARRANGEMENTS CONTINUED

The Group is required to hold a portion of its assets as FAL to support the underwriting capacity of Syndicate 2010 and Syndicate 3010. FAL are restricted in their use and are only drawn down to pay cash calls to syndicates supported by the Group. FAL requirements are formally assessed twice a year and any funds surplus to requirements may be released at that time. See note 30 for more information regarding FAL requirements.

In addition to the FAL, certain cash and investments held by Syndicate 2010 and Syndicate 3010 are only available for paying claims and expenses of the syndicate to their policyholders. See note 30 for more information regarding capital requirements for Syndicate 2010 and Syndicate 3010.

The following cash and cash equivalents and investment balances were held in trust, other collateral accounts in favour of third parties or are otherwise restricted:

	2014			2013		
As at 31 December	Cash and cash equivalents $m	Fixed income securities $m	Equity securities $m	Cash and cash equivalents $m	Fixed income securities $m	Equity securities $m
MBRT accounts	**0.3**	**31.3**	**–**	1.0	20.0	–
In various other trust accounts for policyholders	**0.7**	**22.9**	**–**	3.8	9.7	–
In favour of LOCs	**8.0**	**25.3**	**–**	6.3	20.0	–
In favour of derivative contracts	**1.5**	**1.7**	**–**	0.7	0.8	–
FAL	**6.9**	**167.5**	**15.8**	14.2	152.6	14.9
Syndicate accounts	**6.9**	**89.6**	**–**	16.4	123.9	–
Total	**24.3**	**338.3**	**15.8**	42.4	327.0	14.9

23. SHARE CAPITAL

Authorised ordinary shares of $0.50 each	Number	$m
As at 31 December 2014 and 2013	3,000,000,000	1,500.0

Allocated, called up and fully paid	Number	$m
As at 31 December 2012	168,602,427	84.3
Shares issued	16,843,382	8.4
As at 31 December 2013	185,445,809	92.7
Shares issued	**6,666,789**	**3.4**
As at 31 December 2014	**192,112,598**	**96.1**

Own shares	Number held in treasury	$m	Number held in trust	$m	Total number of own shares	$m
As at 31 December 2012	5,810,583	40.7	1,320,486	16.4	7,131,069	57.1
Shares distributed	(435,120)	(3.0)	(2,276,285)	(30.1)	(2,711,405)	(33.1)
Shares donated to trust	(1,862,138)	(13.1)	1,862,138	25.9	–	12.8
As at 31 December 2013	3,513,325	24.6	906,339	12.2	4,419,664	36.8
Shares distributed	**(666,434)**	**(5.0)**	**(1,643,647)**	**(21.6)**	**(2,310,081)**	**(26.6)**
Shares repurchased	**2,498,433**	**25.0**	**–**	**–**	**2,498,433**	**25.0**
Shares donated to trust	**(2,394,377)**	**(16.8)**	**2,394,377**	**24.9**	**–**	**8.1**
As at 31 December 2014	**2,950,947**	**27.8**	**1,657,069**	**15.5**	**4,608,016**	**43.3**

The number of common shares in issue with voting rights (allocated share capital less shares held in treasury) as at 31 December 2014 was 189,161,651 (31 December 2013 – 181,932,484).

On 7 August 2013, LHL issued 16,843,382 new common shares. As a result of these shares being issued, a total of $203.5 million was raised, $8.4 million of which was included in share capital and $195.1 million of which was included in share premium, net of $5.3 million of offering expenses.

During 2014, the Group issued new common shares to satisfy the cashless exercises of warrants as follows:

Shares issued	Number of shares issued	$m
23 May 2014	**2,077,605**	**1.1**
13 June 2014	**1,759,974**	**0.9**
3 July 2014	**2,829,210**	**1.4**
Total	**6,666,789**	**3.4**

Of the shares issued on 23 May 2014 and 13 June 2014, per the table above 3,837,579 were issued to satisfy Richard Brindle's warrant exercises (refer to note 27 for further information on related party transactions).

SHARE REPURCHASES

At the AGM held on 30 April 2014, the Group's shareholders approved a renewal of the Repurchase Programme authorising the repurchase of a maximum of 18,544,580 shares, with such authority to expire on the conclusion of the 2015 AGM or, if earlier, fifteen months from the date the resolution approving the Repurchase Programme was passed.

Shares have been repurchased by the Group under share repurchase authorisation as follows:

Own shares	Number of shares cancelled	Number of shares transferred to treasury shares	Weighted average share price	$m
As at 31 December 2012	27,541,552	5,810,583	£4.30	244.5
Shares distributed	–	(435,120)	£4.30	(3.0)
Shares donated to trust	–	(1,862,138)	£4.27	(13.1)
As at 31 December 2013	27,541,552	3,513,325	£4.31	228.4
Repurchased	**–**	**2,498,433**	**£6.27**	**25.0**
Shares distributed	**–**	**(666,434)**	**£4.77**	**(5.0)**
Shares donated to trust	**–**	**(2,394,377)**	**£4.61**	**(16.8)**
As at 31 December 2014	**27,541,552**	**2,950,947**	**£4.43**	**231.6**

At the balance sheet date $nil (31 December 2013 – $nil) remained to be settled.

In 2014, the trustees of the EBT acquired nil shares (2013 – nil) in accordance with the terms of the trust and distributed 1,643,647 (2013 – 2,276,285). There were no unsettled balances in relation to EBT purchases at either balance sheet date.

DIVIDENDS

The Board of Directors have authorised the following dividends:

Type	Per share amount	Record date	Payment date	$m
Final	$0.10	22 Mar 2013	17 Apr 2013	19.2
Special	$1.05	22 Mar 2013	17 Apr 2013	201.4
Interim	$0.05	23 Aug 2013	25 Sep 2013	10.5
Special	$0.45	29 Nov 2013	20 Dec 2013	94.5
Final	$0.10	21 Mar 2014	16 Apr 2014	21.1
Special	$0.20	21 Mar 2014	16 Apr 2014	42.1
Interim	$0.05	29 Aug 2014	24 Sep 2014	10.4
Special	$1.20	28 Nov 2014	19 Dec 2014	247.4

24. OTHER RESERVES

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

	Number of Founder warrants	Number of Lancashire Foundation warrants	Number of ordinary warrants
Outstanding at 31 December 2012	19,803,572	648,143	2,350,000
Exercised	(728,785)	–	–
Outstanding and exercisable as at 31 December 2013	19,074,787	648,143	2,350,000
Exercised	**(4,042,108)**	**–**	**–**
Outstanding and exercisable as at 31 December 2014	**15,032,679**	**648,143**	**2,350,000**
Weighted average exercise price as at 31 December 2014	**$5.00**	**$4.73**	**$5.00**

	2014	2013
Weighted average remaining contractual life	**1.0 year**	2.0 years
Weighted average share price at date of exercise during the year	**$11.25**	$12.17

The fair value of all warrants granted was $2.62 per warrant. The exercise price of the Lancashire Foundation warrants was automatically adjusted for dividends declared prior to the vesting date. Refer to note 6 for further details. This did not apply to the Founder warrants as they were fully vested at the date of grant and exercisable upon issuance.

25. LEASE COMMITMENTS

The Group has payment obligations in respect of operating leases for certain items of office equipment and office space. Operating lease expenses for the year were $3.8 million (2013 – $2.4 million). Future minimum lease payments under non-cancellable operating leases are as follows:

	2014 $m	2013 $m
Due in less than one year	**1.1**	2.9
Due between one and five years	**11.4**	6.9
Due in more than five years	**41.2**	–
Total	**53.7**	9.8

During 2014, the Group entered into a new lease agreement for larger office premises in the UK and assigned the leases in relation to the existing office premises in the UK to a third party who assumed responsibility for payments. Under the terms of the lease assignment the Group retains liability for lease payments in the event that the assignee and the assignee's guarantor fail to meet their obligations under the assignment agreements. The new lease agreement contains a break date of April 2029 and is guaranteed by the Group.

26. EARNINGS PER SHARE

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

	2014 $m	2013 $m
Profit for the year attributable to equity shareholders of LHL	**229.3**	222.5

	2014 Number of shares	2013 Number of shares
Basic weighted average number of shares	**185,558,086**	169,270,681
Dilutive effect of RSS	**2,442,255**	3,431,739
Dilutive effect of warrants	**10,112,990**	17,788,368
Diluted weighted average number of shares	**198,113,331**	190,490,788

Earnings per share	2014	2013
Basic	**$1.24**	$1.31
Diluted	**$1.16**	$1.17

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

27. RELATED PARTY DISCLOSURES

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

Name	Principal Business	Domicile
Subsidiaries[1]		
LICL	General insurance business	Bermuda
SML[2]	Insurance management services	Bermuda
KCML[3]	Insurance management services	Bermuda
Lutine[4]	Non trading	Bermuda
KCMMSL	Support services	United Kingdom
LIHL	Holding company	United Kingdom
LIMSL	Insurance mediation activities	United Kingdom
LISL	Support services	United Kingdom
LUK	General insurance business	United Kingdom
LMSCL	Support services	Canada
CCIL[5]	Holding company	United Kingdom
CCHL	Investment company	United Kingdom
CCL	Holding company	United Kingdom
CCL 1998	Lloyd's corporate member	United Kingdom
CCL 1999	Non trading	United Kingdom
CCL 2000[5]	Holding company	United Kingdom
CCML[5]	Non trading	United Kingdom
CCSL	Support services	United Kingdom
CUL	Lloyd's managing agent	United Kingdom
Associates		
AHL[6]	Holding company	Bermuda
AHL II[7]	Holding company	Bermuda
SHL[8]	Holding company	Bermuda
KHL	Holding company	Bermuda
Other controlled entities		
LHFT	Trust	United States
EBT	Trust	Jersey

(1) Unless otherwise stated, the Group owns 100 per cent of the ordinary share capital and voting rights in its subsidiaries listed.

(2) SML was liquidated on 12 August 2014.

(3) 92.68 per cent owned by the Group.

(4) Lutine was dissolved on 29 May 2014.

(5) The entities were formally placed in members' voluntary liquidation on 11 December 2014.

(6) AHL was liquidated on 15 October 2014.

(7) AHL II was liquidated on 25 November 2014.

(8) SHL was liquidated on 15 October 2014.

27. RELATED PARTY DISCLOSURES CONTINUED

The Group has issued subordinated loan notes via a trust vehicle – LHFT, refer to note 22. The Group effectively has 100.0 per cent of the voting rights in LHFT. These rights are subject to the property trustee's obligations to seek the approval of the holders of LHFT's preferred securities in case of default and other limited circumstances where the property trustee would enforce its rights. While the ability of the Group to influence the actions of LHFT is limited by the trust agreement, LHFT was set up by the Group with the sole purpose of issuing the subordinated loan notes, is in essence controlled by the Group, and is therefore consolidated.

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

The Group has a Loan Facility Agreement (the 'Facility') with RBC Cees Trustee Limited, the trustees of the EBT. The Facility is an interest free revolving credit facility under which the Trustee can request advances on demand, within the terms of the facility, up to a maximum aggregate of $60.0 million. The Facility may only be used by the Trustees for the purpose of achieving the objectives of the EBT. During the year ended 31 December 2014, the Group had made advances of $5.0 million (2013 – $10.7 million) to the EBT under the terms of the Facility.

During the year ended 31 December 2014, the Group donated 2,394,377 (2013 – 1,862,138) treasury shares to the EBT at the prevailing market rate. The total value of the treasury share donation was $24.9 million (2013 – $25.9 million).

LICL holds $346.1 million (2013 – $302.8 million) of cash and cash equivalents and fixed income securities in trust for the benefit of LUK relating to intra-group reinsurance agreements.

In 2013, members of the Group's senior management team contributed 12.57 per cent of the share capital in KCML. During 2014, LHL and the Group's senior management team purchased shares in KCML from Richard Brindle (see other transactions below). The senior management team shareholding now represents a minority interest of 7.32 per cent. This investment represents the non-controlling interest listed in the Group's consolidated balance sheet.

KEY MANAGEMENT COMPENSATION

Remuneration for key management, the Group's Executive and Non-Executive Directors, was as follows:

For the year ended 31 December	2014 $m	2013 $m
Short-term compensation[1]	**3.3**	8.1
Equity based compensation	**7.5**	6.7
Directors' fees and expenses	**2.2**	2.1
Total	**13.0**	**16.9**

(1) Includes a credit of $2.3 million relating to the decrease in the UK National Insurance contribution provision in respect of Richard Brindle's warrants. This is a result of the reduction in the Group's share price prior to the exercise of his warrants during 2014.

The table above includes short-term compensation of $1.8 million and an equity based compensation charge of $3.5 million relating to the retirement of Richard Brindle, the Group's former CEO. His retirement package also included a cash settlement of RSS awards amounting to $8.2 million. Dividend equivalents that have been accrued on the RSS awards amounted to $1.6 million. The settlement of the RSS awards and the dividend equivalent payment are reflected in contributed surplus within shareholders' equity.

The Directors' fees and expenses includes $0.4 million (2013 – $0.4 million) paid to significant founding shareholders. Non-Executive Directors do not receive any benefits in addition to their agreed fees and expenses and do not participate in any of the Group's incentive, performance or pension plans. Neil McConachie left the Company as an employee on 30 June 2012, relinquishing his executive responsibilities and became a Non-Executive Director effective 1 July 2012. He subsequently relinquished his role as a Non-Executive Director on 30 April 2014. He is able to exercise previously granted RSS awards when they have vested, subject to the performance conditions being met.

TRANSACTIONS WITH LANCASHIRE FOUNDATION

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

Date	$m
23 May 2013	1.4
5 November 2013	2.0

TRANSACTIONS WITH ASSOCIATES

In relation to transactions with ARL, the following amounts were included in the consolidated statement of comprehensive income and the consolidated balance sheet:

As at 31 December	2014 $m	2013 $m
Consolidated statement of comprehensive income		
Outwards reinsurance premiums	**0.6**	47.9
Insurance loss and loss adjustment expenses recoverable	**(6.9)**	9.1
Insurance acquisition expenses ceded	**6.8**	7.1
Consolidated balance sheet		
Reinsurance recoveries	**–**	26.8
Amounts payable to reinsurers	**–**	(5.5)

During 2014, AHL returned $33.5 million of capital to the Group and ARL paid a final profit commission to the Group in the amount of $6.7 million following a commutation of the Group's quota share agreement with ARL.

During 2014, SHL returned $12.2 million of capital to the Group and SRL paid a final profit commission to the Group in the amount of $3.0 million and was placed in to run-off and subsequently liquidated.

During 2014, the Group committed an additional $27.8 million of capital to KHL.

In 2013, KCML entered into an underwriting services agreement with KRL and KHL to provide various services relating to underwriting, actuarial, premium payments and relevant deductions, acquisition expenses and receipt of claims. For the year ended 31 December 2014, the Group recognised $6.2 million (31 December 2013 – $nil) of service fees in other income in relation to this agreement. Contingent profit commission may be payable to KCML on the ultimate performance of KRL.

Refer to note 17 for further details on the Group's investment in associates.

OTHER TRANSACTIONS

On 2 June 2014, Richard Brindle sold his shares in KCML to LHL and certain of the minority shareholders of KCML (being members of the Group's senior management team) for an amount of $1.2 million, of which $1.1 million was received from LHL. The sale was a direct result of the provisions outlined in the subscription and shareholders' agreement of KCML and the valuation was externally determined by a valuation expert.

28. BUSINESS COMBINATIONS

On 7 November 2013, LHL acquired the entire issued share capital of Cathedral together with manager and investor loan notes and preference shares issued by CCIL and CCL respectively. The acquisition has enabled the Group to benefit from direct participation in Lloyd's, the world's leading specialist insurance market.

	Notes	$m
Total consideration paid for the entire issued share capital of Cathedral		**230.4**
Net assets acquired at fair value		**159.2**
Excess of total consideration over net fair value of assets acquired allocated to goodwill	19	**71.2**

Intangible assets recognised on the acquisition of Cathedral relate to syndicate participation rights and the value of in-force business. These are discussed further in note 19. The goodwill recognised arose from the premium paid for strengthening the Group's market position and acquiring a skilled workforce with an existing book of business and long standing business relationships. The goodwill is not deductible for tax purposes.

29. NON-CASH TRANSACTIONS

On 25 June 2014, following shareholder approval on 30 April 2014, LHL transferred $192.2 million from share premium to contributed surplus. During 2014, the Group issued new common shares to satisfy the cashless exercises of warrants in the amount of $3.4 million. Refer to note 23 for further details.

30. STATUTORY REQUIREMENTS AND DIVIDEND RESTRICTIONS

The primary source of capital used by the Group is equity shareholders' funds and borrowings. As a holding company, LHL relies on dividends from its operating entities to provide the cash flow required for debt service and dividends to shareholders. The operating entities' ability to pay dividends and make capital distributions is subject to the legal and regulatory restrictions of the jurisdictions in which they operate.

For LICL and LUK, these regulatory restrictions are based principally on the amount of premiums written and reserves for losses and loss adjustment expenses, subject to overall minimum solvency requirements. LICL and LUK's statutory capital and surplus are different from shareholder's equity due to certain items that are capitalised under IFRS but expensed or have a different valuation basis for regulatory reporting, or are not admitted under insurance regulations.

Annual statutory capital and surplus reported to regulatory authorities by LICL and LUK is as follows:

	2014		2013	
As at 31 December	**LICL $m**	**LUK £m**	LICL $m	LUK £m
Statutory capital and surplus	**1,009.5**	**117.3**	1,210.2	118.9
Minimum required statutory capital and surplus	**233.7**	**23.9**	235.5	23.9

LICL is required to maintain a minimum liquidity ratio, whereby relevant assets, as defined in the regulations, must exceed 75.0 per cent of relevant liabilities. As at 31 December 2014 and 2013 the liquidity ratio was met. LICL is also required to perform various capital calculations under the BMA's regulatory framework. An assessment is made of LICL's capital needs and a target capital amount is determined. The BMA may require a further capital loading on the target capital amount in certain circumstances. The BMA considers that a decrease in capital below the target level represents a regulatory intervention point.

For LUK, various capital calculations are performed and an ICA is presented to the PRA. The PRA then considers the capital calculations and issues an ICG, reflecting the PRA's own view as to the level of capital required. The PRA considers that a decrease in an insurance company's capital below the level of its ICG represents a regulatory intervention point. As the Solvency II regime is adopted by the PRA the capital measures will change, but the principles and restrictions on capital release will remain.

The Group's underwriting capacity as a member of Lloyd's must be supported by providing a deposit in the form of cash, securities or LOCs, which are referred to as FAL. The capital framework at Lloyd's requires each managing agent to calculate the capital requirement for each syndicate they manage, a process known as ICA. Solvency II internal models and the uSCR have been used to determine capital requirements for Syndicate 2010 and Syndicate 3010. The uSCR of each syndicate at Lloyd's is regarded as the minimum regulatory capital requirement for the business. Lloyd's has the discretion to take into account other factors at member level to uplift the calculated uSCR, including the need to maintain the market's overall security rating. Any uplift by Lloyd's is added to the uSCR to produce the ECA.

Lloyd's then uses each syndicate's ECA as a basis for determining member level ECR. For the 2015 calendar year the Group's initial FAL requirement was set at 53.9 per cent (2014 – 61.0 per cent) of underwriting capacity supported. Further adjustments can be made by Lloyd's to allow for open year profits and losses of the syndicates on which the corporate member participates. The Group has sufficient capital to meet its FAL requirement of £149.3 million as at 31 December 2014 (31 December 2013 – £115.1 million).

As at 31 December 2014 and 2013 the capital requirements of all the regulatory jurisdictions were met.

31. SUBSEQUENT EVENTS

DIVIDEND

On 11 February 2015 the Board of Directors declared the payment of an ordinary dividend of $0.10 per common share and a special dividend of $0.50 per share to shareholders of record on 20 March 2015, with a settlement date of 15 April 2015. The ordinary dividend payable will be approximately $20.6 million and the special dividend payable will be approximately $102.8 million. An amount equivalent to the dividend accrues on all RSS options and is paid at the time of exercise, pro-rata according to the number of RSS options that vest.

ANNUAL GENERAL MEETING

The Company's AGM is scheduled for 29 April 2015. Notice of this year's AGM and the form of proxy accompany this Annual Report. If you have any queries regarding the notice or return of the proxy please contact Chris Head, Company Secretary, at Lancashire Holdings Limited, 29th Floor, 20 Fenchurch Street, London EC3M 3BY, United Kingdom, Tel: + 44 (0) 20 7264 4000 and email: chris.head@lancashiregroup.com.

FURTHER INFORMATION

Lancashire Holdings Limited is registered in Bermuda under company number EC 37415 and has its registered office at Power House, 7 Par-la-Ville Road, Hamilton HM 11, Bermuda.

Further information about the Group including this Annual Report, press releases and the Company's share price is available on our website at www.lancashiregroup.com. Please address any enquiries to info@lancashiregroup.com.

NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements in this document include forward-looking statements which reflect the Directors' current views with respect to financial performance, business strategy, plans and objectives of management for future operations (including development plans relating to the Group's products and services). These statements include forward-looking statements both with respect to the Group and the sectors and industries in which the Group operates. Statements containing the words "believes", "anticipates", "plans", "projects", "forecasts", "guidance", "intends", "expects", "estimates", "predicts", "may", "can", "will", "seeks", "should" or, in each case, their negative or comparable terminology and similar statements are of a future or forward-looking nature. All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause the actual results, performance or achievements of the Group to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements.

These factors include, but are not limited to: the Group's ability to integrate its business and personnel, the successful retention and motivation of the Group's key management, the increased regulatory burden facing the Group, the number and type of insurance and reinsurance contracts that the Group writes or the Group may write; the Group's ability to successfully implement its business strategy during "soft" as well as "hard" markets; the premium rates which may be available at the time of such renewals within its targeted business lines; the possible low frequency of large events; potentially unusual loss frequency; the impact that the Group's future operating results, capital position and rating agency and other considerations may have on the execution of any capital management initiatives or dividends; the possibility of greater frequency or severity of claims and loss activity than the Group's underwriting, reserving or investment practices have anticipated; the reliability of, and changes in assumptions to, catastrophe pricing, accumulation and estimated loss models; increased competition from existing alternative capital providers and insurance linked funds and collateralised special purpose insurers and the related demand and supply dynamics as contracts come up for renewal; the effectiveness of its loss limitation methods; the potential loss of key personnel; a decline in the Group's operating subsidiaries' rating with A.M.Best, Standard & Poor's, Moody's or other rating agencies; increased competition on the basis of pricing, capacity, coverage terms or other factors; cyclical downturns of the industry; the impact of a deteriorating credit environment for issuers of fixed income investments; the impact of swings in market interest rates and securities prices; a rating downgrade of, or a market decline in, securities in its investment portfolio; changes in governmental regulations or tax laws in jurisdictions where the Group conducts business; Lancashire or its Bermudian subsidiaries becoming subject to income taxes in the United States or the Bermudian subsidiaries becoming subject to income taxes in the United Kingdom; the inapplicability to the Group of suitable exclusions from the UK CFC regime; any change in the UK government or the UK government policy which impacts the CFC regime or other tax changes; and the negative impact in any material way of the change in tax residence of the Company on its stakeholders. Any estimates relating to loss events involve the exercise of considerable judgement and reflect a combination of ground-up evaluations, information available to date from brokers and insureds, market intelligence, initial and/or tentative loss reports and other sources. Judgements in relation to loss arising from natural catastrophe and man-made events are influenced by complex factors. The Group cautions as to the preliminary nature of the information used to prepare such estimates as subsequently available information may contribute to an increase in these types of losses.

These forward-looking statements speak only as at the date of this document. The Company expressly disclaims any obligation or undertaking (save as required to comply with any legal or regulatory obligations including the rules of the LSE) to disseminate any updates or revisions to any forward-looking statements to reflect any changes in the Group's expectations or circumstances on which any such statement is based. All subsequent written and oral forward-looking statements attributable to the Group or individuals acting on behalf of the Group are expressly qualified in their entirety by this paragraph. Prospective investors should specifically consider the factors identified in this document which could cause actual results to differ before making an investment decision.

ABS
Asset backed securities

ACTIVE UNDERWRITER
The individual at a Lloyd's syndicate with principal authority to accept insurance and reinsurance risk on behalf of the syndicate

ADDITIONAL CASE RESERVES (ACR)
Additional reserves deemed necessary by management

AFS
Available for sale

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

AGM
Annual General Meeting

AHL
Accordion Holdings Limited

AHL II
Accordion Holdings II Limited

AIM
A sub-market of the LSE

AIR
AIR Worldwide

A.M. BEST COMPANY (A.M. BEST)
A.M. Best is a full-service credit rating organisation dedicated to serving the financial services industries, focusing on the insurance sector

ARL (ACCORDION)
Accordion Reinsurance Limited

BAM
Bathwater aggregate model

BEST LANCASHIRE ASSESSMENT OF SOLVENCY OVER TIME (BLAST)
The Group's economic internal capital model

BMA
Bermuda Monetary Authority

BOARD OF DIRECTORS
Unless otherwise stated refers to the LHL Board of Directors

BOOK VALUE PER SHARE (BVS)
Calculated by dividing the value of the total shareholders' equity by the sum of all common voting shares outstanding

BSX
Bermuda Stock Exchange

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

CATHEDRAL; CATHEDRAL GROUP
Refers to CCL and all direct and indirect subsidiaries of CCL

CCHL
Cathedral Capital Holdings Limited

CCIL
Cathedral Capital (Investments) Limited

CCL
Cathedral Capital Limited

CCL 1998
Cathedral Capital (1998) Limited

CCL 1999
Cathedral Capital (1999) Limited

CCL 2000
Cathedral Capital (2000) Limited

CCML
Cathedral Capital Management Limited

CCSL
Cathedral Capital Services Limited

CEDED
To transfer insurance risk from a direct insurer to a reinsurer and/or from a reinsurer to a retrocessionaire

CEO
Chief Executive Officer

CFC
Controlled Foreign Company

CFO
Chief Financial Officer

CGU
Cash generating unit

CMBS
Commercial mortgage backed securities

THE CODE
UK Corporate Governance Code published by the UK Financial Reporting Council

COMBINED RATIO
Ratio, in per cent, of the sum of net insurance losses, net acquisition expenses and other operating expenses to net premiums earned

COVERHOLDER AT LLOYD'S
A coverholder is a company or partnership authorised by a managing agent to enter into a contract or contracts of insurance to be underwritten by the members of a syndicate managed by it in accordance with the terms of a binding authority

CRO
Chief Risk Officer

CUL
Cathedral Underwriting Limited

CUO
Chief Underwriting Officer

DEFERRED ACQUISITION COSTS
Costs incurred for the acquisition or the renewal of insurance policies (e.g. brokerage and premium taxes) which are deferred and amortised over the term of the insurance contracts to which they relate

DILUTED EARNINGS PER SHARE
Calculated by dividing the net profit for the year attributable to shareholders by the weighted average number of common shares outstanding during the year plus the weighted average number of common shares that would be issued on the conversion of all potentially dilutive equity based compensation awards into common shares under the treasury stock method

DIVIDEND YIELD
Calculated by dividing the annual dividends per share by the share price on the last day of the given year

DURATION
Duration is the weighted average maturity of a security's cash flows, where the present values of the cash flows serve as the weights.

The effect of the convexity, or sensitivity, of the portfolio's response to changes in interest rates is also factored in to the calculation

EARNINGS PER SHARE (EPS)
Calculated by dividing net profit for the year attributable to shareholders by the weighted average number of common shares outstanding during the year, excluding treasury shares and shares held by the EBT

EBT
Lancashire Holdings Employee Benefit Trust

ECA
Economic Capital Assessment

ECR
Economic Capital Requirement

EMD
Emerging Market Debt

ERM
Enterprise Risk Management

EURIBOR
The Euro Interbank Offered Rate

EXCESS OF LOSS
Reinsurance or insurance that indemnifies the reinsured or insured against all or a specified portion of losses on an underlying insurance policy in excess of a specified amount

EXPENSE RATIO
Ratio, in per cent, of other operating expenses to net premiums earned

EY
Ernst & Young LLP

FACULTATIVE REINSURANCE
A reinsurance risk that is placed by means of a separately negotiated contract as opposed to one that is ceded under a reinsurance treaty

FAL
Funds at Lloyd's

FCA
Financial Conduct Authority

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

FPSO
Floating production storage and offloading

FSMA
The Financial Services and Markets Act 2000 (as amended from time to time)

FULLY CONVERTED BOOK VALUE PER SHARE (FCBVS)
Calculated by dividing the value of the total shareholders' equity plus the proceeds that would be received from the exercise of all dilutive equity compensation awards, by the sum of all shares, including equity compensation awards assuming all are exercised

FVTPL
Fair value through profit or loss

G10
Belgium, Canada, Germany, France, Italy, Japan, the Netherlands, Sweden, the United Kingdom, and the United States

GROSS PREMIUMS WRITTEN
Amounts payable by the insured, excluding any taxes or duties levied on the premium, including any brokerage and commission deducted by intermediaries

THE GROUP
LHL and its subsidiaries

HMRC
Her Majesty's Revenue & Customs

ICA
Individual capital assessment

ICSA
Institute of Chartered Secretaries and Administrators

ICG
Individual capital guidance

IFRIC
International Financial Reporting Interpretations Committee

IFRS
International Financial Reporting Standard(s)

INCURRED BUT NOT REPORTED (IBNR)
These are anticipated or likely losses that may result from insured events which have taken place, but for which no losses have yet been reported. IBNR also includes a reserve for possible adverse development of previously reported losses

INDUSTRY LOSS WARRANTY (ILW)
A type of reinsurance or derivative contract through which one party will purchase protection based on the total loss arising from an event to the entire insurance industry rather than their own losses.

INTERNAL AUDIT CHARTER
Is a formal written document that sets out the mission, scope, responsibilities, authority, professional standards and the relationship with the external auditors / regulatory bodies of the internal audit function ("internal audit") with the company and its subsidiaries

INTERNATIONAL ACCOUNTING STANDARD(S) (IAS)
Standards, created by the IASB, for the preparation and presentation of financial statements

INTERNATIONAL ACCOUNTING STANDARDS BOARD (IASB)
An international panel of accounting experts responsible for developing IAS and IFRS

IRR
Internal rate of return

IRRC
Investment Risk and Return Committee

ISE
Irish Stock Exchange

KCML
Kinesis Capital Management Limited

KCMMSL
KCM Marketing Services Limited

KHL (KINESIS HOLDINGS)
Kinesis Holdings I Limited

KINESIS
The Group's third party capital management division encompassing KCML, KCMMSL and the management of KHL and KRL

KRL (KINESIS RE)
Kinesis Reinsurance I Limited

LANCASHIRE COMPANIES
Refers to the Group excluding Cathedral and Kinesis

LANCASHIRE FOUNDATION OR FOUNDATION
The Lancashire Foundation is a charity registered in England and Wales

LANCASHIRE UK GROUP OF COMPANIES
Includes LHL, LUK, LIHL, LISL and LIMSL

LHFT
Lancashire Holdings Financing Trust I

LHL
Lancashire Holdings Limited

LIBOR
London Interbank Offered Rate

LICL
Lancashire Insurance Company Limited

LIHL
Lancashire Insurance Holdings (UK) Limited

LIMSL
Lancashire Insurance Marketing Services Limited

LISL
Lancashire Insurance Services Limited

LISTING RULES
The listing rules made by the FCA under part VI of FSMA (as amended from time to time)

LLOYD'S
The Society of Lloyd's

LMSCL
Lancashire Management Services (Canada) Limited

LOC
Letter of credit

LOSSES
Demand by an insured for indemnity under an insurance contract

LSE
London Stock Exchange

LUK
Lancashire Insurance Company (UK) Limited

LUTINE
Lutine Limited

MBRT
Multi-beneficiary reinsurance trust

MBS
Mortgage backed securities

MGA'S
Managing general agents

MOODY'S INVESTORS SERVICES (MOODY'S)
Moody's Corporation is the parent company of Moody's Investors Service, which provides credit ratings and research covering debt instruments and securities, and Moody's Analytics, which offers software, advisory services and research for credit and economic analysis and financial risk management.

NAV
Net asset value

NBS
New Bridge Street (a trading name of Aon Hewitt Limited)

NET ACQUISITION COST RATIO
Ratio, in per cent, of net acquisition expenses to net premiums earned

NET LOSS RATIO
Ratio, in per cent, of net insurance losses to net premiums earned

NET OPERATING PROFIT
Profit before tax excluding realised gains and losses and foreign exchange gains and losses

NET PREMIUMS WRITTEN
Net premiums written is equal to gross premiums written less outwards reinsurance premiums written

ORSA
Own Risk and Solvency Assessment

OTC
Over the counter

PML
Probable maximum loss

PRA
Prudential Regulation Authority

PRO-RATA/PROPORTIONAL
Reinsurance or insurance where the reinsured or insured shares a proportional part of the original premiums and losses of the reinsured or insured

RDS
Realistic Disaster Scenarios

RETROCESSION
The reinsurance of a reinsurance account

RETURN ON EQUITY (RoE)
The IRR of the change in FCBVS in the period plus accrued dividends

RMBS
Residential mortgage backed securities

RMS
Risk Management Solutions

RPI
Renewal Price Index

RRC
Risk and Return Committee

RSS
Restricted share scheme

SATEC
SATEC Underwriting, a privately owned insurance underwriting agency operating at national and international level in specialty classes of business. SATEC Underwriting is a coverholder at Lloyd's

SHARP
Lancashire's in house aggregation system

SHL
Saltire Holdings I Limited

SIDECAR
A specialty reinsurance company designed to provide additional capital to another (re)insurance company. Investors invest in a sidecar to reinsure specific risks for a specific (re)insurance company

SML
Saltire Management Limited

SRL
Saltire Re I Limited

STANDARD & POOR'S (S&P)
Standard & Poor's is a worldwide insurance rating and information agency whose ratings are recognised as an ideal benchmark for assessing the financial strength of insurance related organisations

SYNDICATE 2010
Lloyd's Syndicate 2010, managed by CUL. The group provides capital to support 57.8 per cent of the stamp

SYNDICATE 3010
Lloyd's Syndicate 3010, managed by CUL. The group provides capital to support 100.0 per cent of the stamp

THE SYNDICATES
Syndicate 2010 and 3010

TBAs
Mortgage backed "to be announced" securities

TOTAL SHAREHOLDER RETURN (TSR)
The IRR of the increase in share price in the period, measured in U.S. dollars, adjusted for dividends

TREATY REINSURANCE
A reinsurance contract under which the reinsurer agrees to offer and to accept all risks of a certain size within a defined class

UMCC
Underwriting and Marketing Conference Call

UNEARNED PREMIUMS
The portion of premium income that is attributable to periods after the balance sheet date that is deferred and amortised to future accounting periods

UNL
Ultimate net loss

USCR
Ultimate solvency capital requirement

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

VALUE AT RISK (VAR)
A measure of the risk of loss of a specific portfolio of financial assets

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Paper from responsible sources
FSC® C107262

This report is printed on Heaven 42 and Essential Offset which have been independently certified by the Forest Stewardship Council® and manufactured using materials from sustainable sources.

The inks used are all vegetable oil based.

Designed and produced by Black Sun Plc.

Printed at Principal Colour Ltd. ISO 14001 certified, Alcohol Free and FSC® Chain of Custody certified.

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