IMPORTANT INFORMATION ABOUT SYNDICATE REPORTS AND ACCOUNTS

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XL Catlin Syndicate 2003

For The Year Ended 31 December 2016

XL CATLIN

MAKE YOUR WORLD GO

CONTENTS

XL CATLIN SYNDICATE 2003
SYNDICATE INFORMATION

MANAGING AGENT

Managing agent	Catlin Underwriting Agencies Limited ("CUAL")	
Directors	S Catlin	(Non executive)
	P Jardine	
	P Greensmith	
	R Glauber	(Non executive)
	P Wilson	(Non executive)
	J Harris	
	P Bradbrook	
	B Joseph	(Non executive)
	J Gale	
	A McMellin	
Company secretary	M L Rees	
Registered number	01815126	
Registered office	20 Gracechurch Street London EC3V 0BG	

SYNDICATE:

Active underwriter	P Greensmith J Gale
Independent auditors	PricewaterhouseCoopers LLP Chartered Accountants and Statutory Auditors 7 More London Riverside London SE1 2RT

FINANCIAL HIGHLIGHTS

	2016	2015
Syndicate capacity (£m)	**1,438.2**	*1,521.9*
Gross premiums written ($m)	**2,955.2**	*2,939.2*
Net premium written ($m)	**2,097.0**	*1,975.7*
Earned premiums, net of reinsurance ($m)	**2,092.7**	*2,065.6*
Underwriting result ($m)	**9.4**	*25.1*
Profit for the financial year ($m)	**131.6**	*53.8*
Claims ratio	**59.6%**	*56.7%*
Expense ratio	**39.9%**	*42.1%*
Combined ratio	**99.5%**	*98.8%*
Investment return	**2.7%**	*1.7%*

STRATEGIC REPORT OF THE DIRECTORS OF THE MANAGING AGENT FOR THE YEAR ENDED 31 DECEMBER 2016

The directors of Catlin Underwriting Agencies Limited ("CUAL"), the managing agent, present their strategic report and audited financial statements for the year ended 31 December 2016.

Principal activities

The principal activity of Syndicate 2003 ("the Syndicate") is to underwrite general insurance and reinsurance business within the Lloyd's of London market. The main lines of business are Accident and Health, Aviation, Casualty, Marine and Offshore Energy, Equine, Specie, Crisis Management, Political Risks, Property and Construction.

The result for the year is a profit of $131.6m (2015: profit of $53.8m), as set out on pages 9 and 10.

The underwriting result (net earned premiums minus net claims incurred and net operating expenses) for 2016 is $9.4m against $25.1m in 2015. The underwriting performance in 2016 was driven by challenging market conditions affecting nearly all lines of business with ongoing "soft" market conditions, low rating environment and capacity in the market. In 2016 a large number of catastrophe losses occurred as compared to 2015 where the syndicate benefited from very low levels of attritional losses and claims for natural catastrophes.

There has been an increase in the investment performance with a total investment return of $97.6m (2015: $62.0m).

Results and performance

The gross written premium for the Syndicate increased to $2,955.2m from $2,939.2m. The marginal increase in the premium is largely due to the changes made to the underwriting structure of the new group in creating the operating model post acquisition in 2015. All business, previously underwritten by Syndicate 1209, is now being written by the Syndicate in 2016. This increase in premium has been offset by a reduction in the Syndicate's US Reinsurance business previously written into Syndicate 2003 by the US offices. Increased business for new initiatives such as the Aon Client Treaty placement to the Syndicate are offset by reduced volumes due to the competitive market for many lines of business and continued softening on rates. Whilst the Syndicate's primary source of premium income is the London market, it continues to pursue underwriting opportunities through the XL Catlin Group's international offices. Analysis of the Syndicate's business written by class of business is set out in note 4: segmental analysis, in the notes to the financial statements.

In 2016, the Syndicate has continued its arrangements to purchase whole account quota share reinsurance from four existing Special Purpose Arrangements (SPAs) and Syndicate 2088, as well as one existing whole account quota share reinsurer, as part of an overall group strategic initiative to manage capital.

The four SPAs and Syndicate 2088 provided a 13.92% whole account quota share in total for the 2016 underwriting year as compared to 14.25% for 2015 underwriting year as a result of a reduction with Syndicate 2088. The whole account quota share reinsurer continued to provide 0.92% quota share for 2016 as in 2015 underwriting year.

Overall our combined ratio has increased from 98.8% to 99.5% which is driven by some significant losses observed on events such as Alberta Wildfires, Hurricane Matthew and the New Zealand Earthquake during 2016.

Investment returns has increased from 1.7% in 2015 to 2.7% in 2016. This improved performance was primarily due to a new investment in the European Equity fund during 2016 and strong performance from the special situations portfolio.

STRATEGIC REPORT OF THE DIRECTORS OF THE MANAGING AGENT (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

Strategy and future outlook

CUAL's strategy is to leverage the inherent strengths of the Lloyd's market to write a portfolio of business which achieves or outperforms our capital provider's target returns over the underwriting cycle. We aim to differentiate ourselves through offering underwriting excellence in specialised areas of insurance. Our objective is to support our underwriters with a flexible underwriting environment, superior analytics, efficient claims handling and a robust Enterprise Risk Management framework.

For 2017 underwriting year, the Syndicate will not continue its whole account quota share purchase with three of the SPAs but will continue its relationships with these reinsurance counterparties through other arrangements and maintain a whole account quota share with one SPA and Syndicate 2088.

The 2014 and prior years of account have Reinsurance to Close ("RITC") into the Syndicate's 2015 year of account for an RITC premium of $2,053m.

The Syndicate purchases a Whole Account Stop Loss reinsurance contract from another group entity, namely XL Insurance (Bermuda) Limited which has assumed benefits and liabilities for the preceding whole account stop loss contract from Catlin Re Switzerland Limited via a novation agreement effective 1 January 2017.

Depending upon prevailing market conditions, premium income levels are under continuous review as the Syndicate aims to develop its relationships with distributors and generate new business through the group's international offices whilst continuing to meet the needs of its clients. The Syndicate will continue to selectively focus on growth opportunities with the emphasis on bottom line profitability.

Managed syndicates and underwriting arrangements

CUAL, the managing agent of the Syndicate, is a company registered in England and Wales. CUAL is a wholly-owned subsidiary of its ultimate parent XL Group Ltd., a company registered in Bermuda. Copies of the financial statements of both CUAL and XL Group Ltd. are available from 20 Gracechurch Street, London, EC3V 0BG.

The Syndicate is wholly-aligned with capital provided by XL Catlin through a subsidiary.

Stamp capacity of the Syndicate

The stamp capacity for the 2017 underwriting year is £1,625m.

This report was approved by the Board and signed on its behalf by:

P Bradbrook
Director
21 March 2017

REPORT OF THE DIRECTORS OF THE MANAGING AGENT FOR THE YEAR ENDED 31 DECEMBER 2016

The directors of the managing agent present their report together with the audited annual accounts for the year ended 31 December 2016.

The annual accounts are prepared using the annual basis of accounting as required by Regulation 5 of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("the 2008 Regulations"), as well as in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102") and Financial Reporting Standard 103, "Insurance Contracts" ("FRS 103").

The managing agent has received, in writing, agreement from Catlin Syndicate Limited, the sole member of Syndicate 2003, that no underwriting year accounts need to be prepared in respect of Syndicate 2003. This is in accordance with Section 4, Paragraph 1b of Statutory Instrument 2004 No 3219.

Profit distribution and solvency

Profits will continue to be distributed by reference to the results of individual underwriting years. Under Lloyd's accounting rules, the Syndicate's 2014 year of account was closed at the end of 2016 with a return equal to 17.0% of capacity.

The member's balance as at 31 December 2016 is $225.3m (2015: $242.4m).

Directors

The directors of CUAL who held office during the year and up to the date of signing the annual accounts were:

S Catlin	(Non executive)	
P Jardine		
P Greensmith		
R Glauber	(Non executive)	
P Wilson	(Non executive)	
J Harris		
P Bradbrook		
B Joseph	(Non executive)	Appointed 8 September 2016
C Ighodaro	(Non executive)	Appointed 12 January 2017
G Bruce-Smythe		Resigned 13 February 2016
S Long		Resigned 13 February 2016
O Whelan		Resigned 13 February 2016
R Cowdell	(Non executive)	Resigned 16 April 2016
N Robertson		Resigned 31 July 2016
A McMellin		Resigned 1 January 2017
J Gale		Resigned 1 January 2017

Financial instruments and risk management

Information on the use of financial instruments by the Syndicate and its management of financial risk and in particular its exposure to interest rate risk, equity price risk, currency risk, credit risk and liquidity risk is disclosed in note 2 to the financial statements.

REPORT OF THE DIRECTORS OF THE MANAGING AGENT (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

Statement of managing agent's responsibilities

The directors of the managing agent are responsible for preparing the Syndicate annual accounts in accordance with applicable law and United Kingdom accounting standards including Financial Reporting Standard 102 - "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"), Financial Reporting Standard 103 - "Insurance Contracts" ("FRS 103"), both issued by the Financial Reporting Council.

The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("the Regulations") require the managing agent to prepare syndicate annual accounts for the Syndicate at 31 December each year. The directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Syndicate and of the profit or loss of the Syndicate for that period.

In preparing these Syndicate annual accounts, the directors of the managing agent are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the basis that the Syndicate will continue to write future business unless it is inappropriate to presume that there will be future years of account of the Syndicate.

The directors of the managing agent are responsible for keeping adequate accounting records that are sufficient to show and explain the Syndicate's transactions and disclose with reasonable accuracy at any time, the financial position of the Syndicate and enable it to ensure that the Syndicate's annual accounts comply with the Regulations and the relevant provisions of the Companies Act 2006. It is also responsible for safeguarding the assets of the Syndicate and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

Statement of disclosure of information to the auditors

Each of the persons who are directors at the date of this report confirms that:

- so far as each director is aware, there is no relevant audit information for which the syndicate's auditors are unaware; and
- each director has taken all the steps that he ought to have taken in his duty as a director in order to make himself aware of any relevant audit information and to establish that the syndicate's auditor is aware of that information.

Approved by the Board of Catlin Underwriting Agencies Limited and signed on its behalf by:

M L Rees
Company Secretary
21 March 2017

INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF SYNDICATE 2003

REPORT ON THE SYNDICATE ANNUAL ACCOUNTS

Our opinion

In our opinion, Syndicate 2003's syndicate annual accounts (the "Syndicate annual accounts"):

- give a true and fair view of the state of the Syndicate's affairs as at 31 December 2016 and of its profit/loss and cash flows for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008.

What we have audited

The syndicate annual accounts for the year ended 31 December 2016, included within the Syndicate annual accounts (the "Annual Report"), comprise:

- the statement of profit or loss for the year then ended;
- the statement of financial position as at 31 December 2016;
- the statement of changes in member's balances;
- the statement of cash flows; and
- the notes to the Syndicate annual accounts, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the Syndicate annual accounts is United Kingdom Accounting Standards, comprising FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland", and applicable law (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the Managing Agent has made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinion on matter prescribed by The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008

In our opinion the information given in the Managing Agent's Report for the financial year for which the Syndicate annual accounts are prepared is consistent with the Syndicate annual accounts.

Other matter on which we are required to report by exception

Under The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- the Managing Agent in respect of the Syndicate has not kept adequate accounting records; or
- the Syndicate annual accounts are not in agreement with the accounting records.

We have no exceptions to report arising from this responsibility.

INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF SYNDICATE 2003 (CONTINUED)

RESPONSIBILITIES FOR THE SYNDICATE ANNUAL ACCOUNTS AND THE AUDIT

Our responsibilities and those of the Managing Agent

As explained more fully in the Statement of Managing Agent's Responsibilities set out on page 6, the Managing Agent is responsible for the preparation of the Syndicate annual accounts and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Syndicate annual accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the syndicate's members as a body in accordance with part 2 of The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of syndicate annual accounts involves

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the syndicate annual accounts sufficient to give reasonable assurance that the Syndicate annual accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Syndicate's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the managing agent; and
- the overall presentation of the Syndicate annual accounts.

We primarily focus our work in these areas by assessing the Managing Agent's judgements against available evidence, forming our own judgements, and evaluating the disclosures in the Syndicate annual accounts.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited syndicate annual accounts 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.

MNichols

Matthew Nichols (Senior Statutory Auditor)
For and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

STATEMENT OF PROFIT OR LOSS
FOR THE YEAR ENDED 31 DECEMBER 2016

TECHNICAL ACCOUNT - GENERAL BUSINESS	Note	2016 $000's	2015 $000's
Earned premium, net of reinsurance			
Gross premiums written	4	2,955,197	2,939,199
Outward reinsurance premiums		(858,225)	(963,476)
Net premiums written		2,096,972	1,975,723
Change in the gross provision for unearned premiums		17,165	48,083
Change in the provision for unearned premiums, reinsurers' share		(21,455)	41,828
Change in the net provision for unearned premiums		(4,290)	89,911
Earned premiums, net of reinsurance		2,092,682	2,065,634
Allocated investment return transferred from the non-technical account	10	93,482	60,061
Total technical income		2,186,164	2,125,695
Claims incurred, net of reinsurance			
Claims paid			
Gross amount		(1,389,873)	(1,423,319)
Reinsurers' share		327,895	338,288
		(1,061,978)	(1,085,031)
Change in the provision for claims			
Gross amount		(260,508)	(88,212)
Reinsurers' share		75,825	1,908
		(184,683)	(86,304)
Claims incurred, net of reinsurance		(1,246,661)	(1,171,335)
Net operating expenses	7	(836,588)	(869,249)
Balance on the technical account for general business		102,915	85,111

STATEMENT OF PROFIT OR LOSS
FOR THE YEAR ENDED 31 DECEMBER 2016

NON-TECHNICAL ACCOUNT	Note	**2016 $000's**	*2015 $000's*
Balance on the technical account for general business		**102,915**	*85,111*
Investment income	10	**81,422**	*116,119*
Unrealised gains on investments	10	**33,082**	—
Investment expenses and charges	10	**(15,190)**	*(43,320)*
Unrealised losses on investments	10	**(1,710)**	*(10,849)*
		97,604	*61,950*
Allocated investment return transferred to the technical account for general business	10	**(93,482)**	*(60,061)*
Foreign exchange gains /(losses)		**24,527**	*(33,162)*
Profit for the financial year		**131,564**	*53,838*

STATEMENT OF FINANCIAL POSITION - ASSETS
AS AT 31 DECEMBER 2016

	Note	**2016 $000's**	*2015 $000's*
Investments			
Other financial investments	11	**3,133,794**	*3,055,957*
Deposits with ceding undertakings		**918**	*851*
Reinsurers' share of technical provisions			
Provision for unearned premiums	12	**453,811**	*490,497*
Claims outstanding	12	**856,887**	*790,706*
		1,310,698	*1,281,203*
Debtors– amounts falling due within one year			
Debtors arising out of direct insurance operations	14	**1,171,513**	*1,177,105*
Debtors arising out of reinsurance operations		**268,927**	*166,301*
Other debtors	15	**118,635**	*51,400*
		1,559,075	*1,394,806*
Debtors– amounts falling due within one year			
Debtors arising out of direct insurance operations	14	**541**	*687*
Debtors arising out of reinsurance operations		**129,099**	*140,625*
Other debtors	16	**54,944**	*54,038*
		184,584	*195,350*
Other assets			
Cash at bank and in hand		**203,817**	*177,397*
Overseas deposits	17	**398,544**	*375,686*
		602,361	*553,083*
Prepayments and accrued income			
Accrued interest		**18,481**	*21,358*
Deferred acquisition costs		**315,223**	*362,274*
Other prepayments and accrued income		**9,620**	*7,998*
		343,324	*391,630*
TOTAL ASSETS		**7,134,754**	*6,872,880*

STATEMENT OF FINANCIAL POSITION - CAPITAL AND LIABILITIES AS AT 31 DECEMBER 2016

	Note	2016 $000's	2015 $000's
Capital and reserves			
Member's balances		**225,288**	*242,380*
Technical provisions			
Provision for unearned premiums	12	**1,437,125**	*1,515,320*
Claims outstanding	12	**4,143,479**	*3,953,344*
		5,580,604	*5,468,664*
Deposits received from reinsurers		**2,636**	*2,636*
Creditors – amounts falling due within one year			
Creditors arising out of direct insurance operations	18	**6,330**	*18,588*
Creditors arising out of reinsurance operations		**427,373**	*380,431*
Amounts owed to dredit institutuions		**589**	—
Other creditors	19	**219,484**	*121,027*
		653,776	*520,046*
Creditors – amounts falling due after one year			
Creditors arising out of direct insurance operations	18	**4,606**	*160*
Creditors arising out of reinsurance operations		**581,309**	*547,541*
Other creditors	20	**5,147**	*4,021*
		591,062	*551,722*
Accruals and deferred income		**81,388**	*87,432*
TOTAL LIABILITIES		**7,134,754**	*6,872,880*

The notes on pages 15 to 44 form part of these financial statements.

The Syndicate financial statements were approved by the Board of Directors of Catlin Underwriting Agencies Limited and were signed on its behalf by:

P. Bradbrook
Director
21 March 2017

STATEMENT OF CHANGES IN MEMBER'S BALANCES FOR THE YEAR ENDED 31 DECEMBER 2016

	Balance attributable to underwriting $000's	Fund in Syndicate $000's	Total Member's Balances $000's
Balance as at 1 January 2015	**215,610**	**175,989**	**391,599**
Profit for the financial year	51,949	1,889	**53,838**
Profit distribution – 2012 year of account	(203,057)	—	**(203,057)**
Transfer of Funds in Syndicate	(17,160)	17,160	—
Balance as at 31 December 2015	**47,342**	**195,038**	**242,380**
Balance as at 1 January 2016	**47,342**	**195,038**	**242,380**
Adjustments made to opening reserve	10,184	—	**10,184**
Profit for the financial year	127,442	4,122	**131,564**
Profit distribution – 2013 year of account	(158,840)	—	**(158,840)**
Balance as at 31 December 2016	**26,128**	**199,160**	**225,288**

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016 $000's	2015 $000's
Reconciliation of profit to net cash flow from operating activities			
Operating result		**131,564**	*53,838*
Increase/(decrease) in gross technical provisions		**111,941**	*(127,368)*
Increase in reinsurers' share of gross technical provisions		**(29,495)**	*(13,263)*
Increase in debtors		**(105,197)**	*(25,019)*
Decrease in creditors		**166,437**	*28,553*
Investment return		**(97,604)**	*(61,950)*
Net cash inflow/(outflow) generated from operating activities		**177,646**	*(145,209)*
Cash flow from investing activities:			
Purchase of equity and debt instruments		**(2,090,152)**	*(6,304,236)*
Sale of equity and debt instruments		**1,505,521**	*6,515,762*
Purchase of derivatives		**—**	*(18,604)*
Sale of derivatives		**—**	*24,876*
Investment income received		**97,604**	*61,950*
Foreign exchange		**513,648**	*127,806*
Deposits with ceding undertakings made		**(68)**	*81*
		26,553	*407,635*
Cash flows from financing activities:			
Distribution of closed year's profit		**(158,840)**	*(203,057)*
Net increase in cash and cash equivalents		**45,359**	*59,369*
Cash and cash equivalents at the beginning of the year		**553,083**	*542,799*
Foreign exchange on cash and cash equivalents		**3,330**	*(49,085)*
Cash and cash equivalents at end of the year		**601,772**	*553,083*
Cash at bank and in hand		**203,817**	*177,397*
Overseas deposits		**398,544**	*375,686*
Overdrafts		**(589)**	*—*
Cash and cash equivalents at end of the year		**601,772**	*553,083*

Overseas deposits and Funds in Syndicate included in cash and cash equivalents are not readily available for use by Syndicate 2003. See note 22 for further detail on these assets.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES

A Basis of preparation

The financial statements have been prepared in accordance with applicable UK accounting standards including Financial Reporting Standard 102 - "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"), Financial Reporting Standard 103 - "Insurance Contracts" ("FRS 103"), both issued by the Financial Reporting Council and in compliance with The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 ("S12008/410") relating to insurance companies and other requirements of the Companies Act 2006.

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the previous years presented, unless otherwise stated.

The preparation of these financial statements required the management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses. The actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in this statement of accounting policies and specifically in the following notes:

Note 11: financial assets and liabilities (valuations based on models and unobservable inputs); and
Note 12: insurance liabilities and reinsurance assets (estimates for losses incurred but not reported).

Capital supporting the business of the Syndicate, referred to as Funds at Lloyd's ("FAL") is, in part, held in separate trust funds administered by Lloyd's in addition to amounts held within the Syndicate Premium Trust Funds. The amounts held by the Corporate Member outside the Syndicate Premium Trust Funds are available to meet the underwriting obligations of the Syndicate, if required. However, these funds are not included in the Syndicate's balance sheet because they are not owned by the Syndicate. The Lloyd's central fund arrangements are available in the event that an individual member's funds are exhausted.

Separate underwriting year accounts for the 2014 underwriting year have not been prepared, as the Syndicate has taken advantage of the exemption under paragraph 6 of the Regulations.

B Basis of accounting

The financial statements have been prepared on a going concern basis, under the annual accrual basis whereby the incurred cost of claims, commission and related expenses are charged against the earned proportion of premiums, net of reinsurance, as follows:

(a) Premiums written

Premiums written comprise premiums on contracts incepted during the financial year, together with adjustments made in the year to premiums written in prior accounting periods. They also include estimates for pipeline premiums, representing amounts due to the Syndicate not yet notified.

Premiums are shown gross of brokerage payable and exclude taxes and duties levied on them.

Contracts with duration of greater than one year and payable in annual instalments, generally, only the initial annual instalment is included as premiums written at policy inception due to the ability of the (re)insured to commute or cancel coverage during the term of the policy. The remaining annual instalments are included as premiums written at each successive anniversary date within the term.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

B Basis of accounting (continued)

(b) Unearned premiums

Written premium is earned according to the risk profile of the policy. Unearned premiums represent the proportion of premiums written in the year that relate to the unexpired terms of the policies in force at the balance sheet date, calculated on the basis of established earnings patterns or time apportionment as appropriate.

(c) Acquisition costs

Acquisition costs, comprising commission and other internal and external costs related to the acquisition of new business and renewing existing contracts. The proportion of acquisition costs in respect of unearned premiums is deferred at the reporting date and recognised in periods when the related premiums are earned.

(d) Ceded Reinsurance

Contracts entered into by the group with reinsurers under which the group is compensated for losses on contracts issued by the group that meet the definition of an insurance contract. Insurance contracts entered into by the group under which the contract holder is another insurer (inwards reinsurance) are included with insurance contracts.

Any benefits to which the group is entitled under its reinsurance contracts held are recognised as reinsurance assets. These assets consist of balances due from reinsurers and include reinsurers' share of provisions for claims. These balances are based on calculated amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the period and the current security rating of the reinsurer involved.

Insurance contracts are those contracts that transfer significant insurance risk.

Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due. The group assesses its reinsurance assets for impairment. If there is objective evidence of impairment, then the carrying amount is reduced to its recoverable amount and the impairment loss is recognised in the statement of profit or loss.

(e) Claims incurred

Claims incurred comprise claims and settlement expenses (both internal and external) paid in the year and the movement in provision for outstanding claims and settlement expenses, including an allowance for the cost of claims incurred by the balance sheet date but not reported until after the year-end. Claims incurred are reduced by anticipated salvage and other recoveries.

(f) Claims provisions and related recoveries

The outstanding claims comprise amounts set aside for claims notified and claims incurred but not yet reported ("IBNR").

Notified claims are estimated on a case by case basis. In estimating the cost of these the Syndicate has regard to the claim circumstance as reported, any information available from loss adjusters and information on the cost of settling claims with similar characteristics in a previous period. Large claims impacting each relevant business class are generally assessed separately, being measured on a case by case basis or projected separately in order to allow for the possible distortion of the development and incidence of these large claims.

The amount included in respect of IBNR is based on statistical techniques of estimation applied by the Syndicate's actuaries. These techniques generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions. Classes of business where claims are typically reported relatively quickly after the claim event tend to display lower levels of volatility.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

B Basis of accounting (continued)

(f) Claims provisions and related recoveries (continued)

The provision for claims includes amounts in respect of internal and external claims handling costs.

For general insurance contracts that are of a duration greater than one year incepting prior to this date the full estimate of gross premiums written was recognised at inception.

The reinsurers' share of provisions for claims is based on calculated amounts of outstanding claims and projections for IBNR having regard to the reinsurance programme in place for the class of business and the claims experience for the year. It is net of estimated irrecoverable amounts having regard to the current security rating of the reinsurance companies involved. The Syndicate uses a number of statistical techniques to assist in making the above estimates.

The two most critical assumptions with regards to claims provisions are that the past is a reasonable predictor of the likely level of claims development and that the rating and other models used for current business are fair reflections of the likely level of ultimate claims to be incurred.

Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in Syndicate processes which might accelerate or slow down the development and/or recording of paid or incurred claims compared with the statistics from previous periods;
- changes in the legal environment;
- the effects of inflation;
- changes in the mix of business;
- the impact of large losses; and
- movements in industry benchmarks.

The directors of CUAL consider that the provisions for gross claims and related reinsurance recoveries are fairly stated on the basis of the information currently available to them. However, ultimate liability will vary as a result of subsequent information and events and this may result in significant adjustments to the amounts provided. Adjustments to the amounts of claims provisions established in prior years are reflected in the financial statements for the period in which the adjustments are made. The methods used, and the estimate made, are reviewed regularly.

The Syndicate discounts unpaid loss reserves arising from US Workers' Compensation business and on Periodic Payment Orders related to bodily injury claims in the UK Motor book.

Both of these payments are considered to have duration of greater than four years from the balance sheet date. The discounting rates and mean estimated terms used for both the Workers Compensation and UK Motor book are 3.75% over 22 years and 2.0% over 40 years, respectively.

	Undiscounted reserves		**Discount credit**	
	2016	*2015*	**2016**	*2015*
	$000's	*$000's*	**$000's**	*$000's*
Workers Compensation	**333,831**	*324,074*	**107,448**	*110,782*
UK Motor book	**53,812**	*55,295*	**29,928**	*28,620*

The Syndicate utilises tabular reserving for US workers' compensation unpaid losses that are considered fixed and determinable, and discount such losses using an interest rate of 3.75%. The interest rate approximates the implied return on the market-based assets supporting the expected cash-flows of our liabilities. The tabular reserving methodology results in applying uniform and consistent criteria for establishing expected future indemnity and medical payments and the use of mortality tables to determine expected payment periods.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

B Basis of accounting (continued)

(f) Claims provisions and related recoveries (continued)

The allowance for Periodic Payment Orders (“PPOs”) relates to bodily injury claims in the UK and includes the unpaid losses for claims already settled and notified as PPOs at 31 December 2016, as well as the unpaid losses for claims to be settled in the future. The future care element of the unpaid losses was discounted using an interest rate of 2%. The interest rate approximates the implied return on the market-based assets supporting the expected cash-flows of our liabilities. Reserves recorded within this report have considered the impacts of the “Ogden Rate” change advised on the 27 February 2017.

The amount of any salvage and subrogation recoveries is separately identified and where material, reported as an asset.

Provision is made at the year-end for the estimated cost of claims incurred but not settled at the Balance Sheet date, including the cost of claims incurred but not yet reported to the Syndicate. The estimated cost of claims includes expenses to be incurred in settling claims. The Syndicate takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established. Any differences between provisions and subsequent settlements are dealt with in the general business technical account of later years.

(g) Unexpired risks provision

A provision for unexpired risks is made where claims and related expenses, likely to arise after the end of the financial period in respect of contracts concluded before that date, are expected to exceed the unearned premiums after the deduction of any acquisition costs deferred. The expected claims relate to policies in force at the year-end, having regard to events that occur prior to the balance sheet date.

Unexpired risk surpluses and deficits are offset when business risk classes are managed together and a provision is made only when an aggregate deficit arises.

(h) Reinsurance to close (RITC)

Each Lloyd's Syndicate underwriting account is normally closed at the end of the third year by means of reinsurance into the following year, which reinsures all future liabilities for the closed year and all previous years in return for a premium which is approved by the managing agent. The payment of a reinsurance to close premium does not eliminate the liability of the closed year for outstanding claims. If the reinsuring Syndicate was unable to meet its obligations, and other elements of Lloyd's chain of security were to fail, then the closed underwriting account would have to settle the outstanding claims.

The directors consider that the likelihood of such a failure of the reinsurance to close is extremely remote, and consequently the reinsurance to close has been deemed to settle liabilities outstanding at the closure of an underwriting account.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

B Basis of accounting (continued)

(i) Financial assets at fair value through the statement of profit or loss

All financial assets are designated as fair value through the statement of profit or loss upon initial recognition because they are managed and their performance is evaluated on a fair value basis. Purchases and sales are recognised on the trade date, which is the date the group commits to purchase or sell the asset, net of transaction costs. These investments are subsequently carried at fair value. Any gains and losses arising from changes in fair value are recognised in the statement of profit or loss in the period in which they arise.

The Syndicate has designated hedge funds, equity funds, equity securities and money market funds at fair value through the statement of profit or loss.

Designated debt securities and other fixed income securities at fair value through the statement of profit or loss. The fair value is based on the quoted market prices provided by either independent pricing services, or, when such prices are not available, by reference to broker or underwriter bid indications.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re measured at their fair value. Changes in the fair value are recognised immediately in the statement of profit or loss. Fair values are obtained from independent pricing services which provide quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

C Pension costs

Catlin Holdings Limited, a fellow group company, operates a defined contribution scheme. Pension contributions relating to staff working on the affairs of the syndicate are charged to the Syndicate and included within net operating expenses.

D Investment return

Investment return comprises all investment income, realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses, charges and interest. Net gains or losses arising from changes in the fair value of financial assets are recognised through the statement of profit or loss within ‘Unrealised gains on investments’ or ‘Unrealised losses on investments’ in the period in which they arise. Investment return is recorded in the non-technical account within the statement of profit or loss. Dividends are recognised on the date on which the shares go and include the imputed tax credits. Interest income is accrued up to the balance sheet date.

a. *Realised gains and losses*
   Realised gains and losses on investments carried at market value are calculated as the difference between sale proceeds and purchase price.

b. *Unrealised gains and losses*
   Unrealised gains and losses on investments represent the difference between their valuation at the balance sheet date and their purchase price or, where acquired in previous years, their valuation at the last balance sheet date, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

c. *Investment expenses, charges or interest*
   There are accounted for as incurred on an accruals basis.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

E Foreign currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Syndicate operates (the functional currency). The Syndicate's financial statements are presented in thousands of US dollars, which is the Syndicate's functional currency. Foreign currency transactions in pound sterling, Canadian dollars, Euros and Australian dollars are translated at the rate of exchange ruling at the dates of the transactions or at an appropriate average rate.

All assets and liabilities arising from insurance contracts should be treated as monetary items. At each period end foreign currency monetary items are re-translated into US dollars at the rate of exchange at the balance sheet date. For this purpose all assets and liabilities arising from insurance contracts (including unearned premiums, deferred acquisition costs and unexpired risks provisions) are monetary items. Non-monetary items measured at historical cost are translated using the exchange rate at the date of the transaction and non-monetary items measured at fair value are measured using the exchange rate when fair value was determined.

Foreign exchange gains and losses resulting from the settlement of transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the non-technical account.

F Taxation

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct income tax from trading income. UK basic rate income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax. No provision has been made for any United States Federal Income Tax payable on underwriting results or investment earnings. Any payments on account made by the Syndicate during the year have been included in the balance sheet under the heading "other debtors".

G Investments and Overseas Deposits

Investments and overseas deposits are stated at current value at the balance sheet date. For this purpose listed investments are stated at bid value and deposits with credit institutions are stated at cost. All other financial instruments are designated as at fair value through profit and loss. In line with normal Lloyd's market practice, the Syndicate writes business in certain jurisdictions that require the deposit of cash and investments in locally held trust funds therefore preventing the free transfer of cash between currencies and locations.

H Equity method investments

Investments over which the Syndicate exercises significant influence by not a controlling interest are carried at cost adjusted for the Syndicate's share of earnings or losses and distributions.

The Syndicate has elected to apply the valuation basis for these investments as established by the alternative accounting rules in SI 410 2008. This permits valuation to be determined on any appropriate basis. Amounts relating to these investments are reported within shares and other variable yield securities in note 11.

I Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Syndicate has designated at fair value through the statement of profit or loss. Loans and receivables are carried at amortised cost less any impairment losses.

Receivables arising from insurance contracts are also classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables. This basis of valuation is viewed by the directors as having prudent regard to the likely realisable value.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

1 ACCOUNTING POLICIES (continued)

J Cash and cash equivalents

Cash and cash equivalents consist of cash held at bank, cash in hand, deposits held at call with banks, cash held in Lloyd's trust accounts and other short term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. These investments have less than three months maturity from the date of acquisition. Cash and cash equivalents are measured at fair value through the statement of profit or loss. Bank overdrafts,where applicable, are held within the current liabilities as amounts due to credit institutions.

Overseas deposits are considered as cash and cash equivalents within the statement of cash flows.

K Financial liabilities

Creditors are recognised initially at fair value, net of directly attributable transaction costs. Creditors are subsequently stated at amortised cost determined according to the effective interest rate method.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 RISK MANAGEMENT

Financial risk management objectives

The Syndicate is exposed to a range of financial risks through its financial assets, insurance liabilities and reinsurance assets. In particular, the key financial risk is that the proceeds from financial assets are not sufficient to fund the obligations arising from insurance policies as they fall due. The most important components of this financial risk are insurance risk (including reinsurance risk), market risk (including interest rate risk, equity price risk and currency risk), credit risk and liquidity risk.

These risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements. The risks that the Syndicate primarily faces due to the nature of its investments and liabilities are interest rate, equity price risk and currency risk.

The Syndicate's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the syndicate's financial performance. It manages these positions within a risk management framework ("the framework") that has been developed to ensure that investment proceeds and returns are in excess of obligations under insurance contracts. The Syndicate produces regular reports that are circulated to the management of the Managing Agency. The principal technique of the Syndicate's framework is to match assets and liabilities from insurance contracts by reference to the type of benefits payable to contract holders. The Syndicate's framework is also integrated with the management of the financial risks associated with the syndicate's other financial assets and liabilities not directly associated with insurance liabilities.

The notes that follow explain how financial risks are managed using the categories utilised in the Syndicate's framework.

(a) Insurance risk

Insurance risk arises from the Syndicate's general insurance business and refers to the risk of loss or of adverse change in the value of insurance liabilities due to inadequate pricing and reserving assumptions. Examples of such risks include unexpected losses arising from fluctuations in the timing, frequency and severity of claims compared to expectations and inadequate reinsurance protection. The Syndicate's underwriting and reinsurance strategies are set within the context of the overall XL Catlin strategies, approved by the Board and communicated clearly throughout the business through policy statements and guidelines.

Capital resource sensitivities

The capital position is sensitive to market conditions due to changes in the value of the assets, and to assumptions and experience in respect of the value of the liabilities. The most significant risks to the Syndicate are as follows:

Event risk

The risk that individual risk losses or catastrophes lead to claims that are higher than anticipated in plans and pricing.

Pricing risk

The risk that the level of expected loss is understated in the pricing process.

Reinsurance risk

Reinsurance risk to the syndicate occurs where reinsurance contracts put in place to reduce gross insurance risk do not perform as anticipated, prove inadequate in terms of the vertical or horizontal limits purchased or result in coverage disputes.

Cycle risk

The risk that business is written in a soft market without full knowledge as to the adequacy of rates, terms and conditions.

Expense risk

The risk that the allowance for expenses and inflation in pricing is inadequate.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 RISK MANAGEMENT (CONTINUED)

(a) Insurance risk (continued)

Underwriting risks are continually monitored through, for example, the established peer review process, underwriting authority limits imposed, round table review and audits, as well as via exception reporting. Formal price monitoring procedures form part of the standard monthly management information. These contribute to the quarterly actuarial review whereby the loss outcome of the underwriting activity is continually and considered by the Reserving actuaries. There is a dedicated Catastrophe and Aggregation management function independent of Underwriting management, whose responsibility is to model aggregate risk and support pricing decisions, providing a key control to the underwriting process.

The Syndicate seeks to maintain a diversified and balanced portfolio of risks in order to reduce the variability of outcomes. Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. In addition, a more diversified portfolio is less likely to be affected by a change in any subset of the portfolio. This is achieved by accepting a spread of business over time, segmented between different classes of business. The Syndicate business forecasts for each class of business reflect this underwriting strategy, and set out the types of business to be written, the geographical regions in which business is to be written and the industry sectors to which the syndicate is prepared to expose itself. These plans are approved and monitored by management and are submitted to Lloyd's. The Syndicate's management also recognises that insurance events are, by their nature, random, and the actual number and size of events during any one year may vary from those estimated using established statistical techniques. To address this, the Syndicate's actuarial team sets out the realistic disaster scenario (RDS) exposure that it is prepared to accept in certain territories to a range of natural and man-made events.

Specific scenarios monitored include:

• Two consecutive Atlantic seaboard windstorms
• Florida windstorm
• Gulf of Mexico windstorm
• European windstorm
• Japanese windstorm
• California earthquake
• New Madrid earthquake
• Japanese earthquake
• UK flood
• Terrorism

The current aggregate position is monitored at the time of underwriting a risk, and reports are produced to highlight the key aggregations to which the Syndicate is exposed. The Syndicate uses a number of modelling tools to monitor aggregation and to simulate catastrophe losses in order to measure the effectiveness of its reinsurance programmes. Stress and scenario tests are also run using these models. The greatest likelihood of significant losses to the Syndicate arises from catastrophe events, such as flood damage, windstorm or earthquake. Where possible the Syndicate's underwriting team measures geographic accumulations and uses their knowledge of the business, historical loss behaviour and commercial catastrophe modelling software. The Syndicate regularly models and monitors known accumulations of risks including natural catastrophes, marine, liability and political events. Upon application of the reinsurance coverage purchased, the key gross and net exposures are calculated on the basis of a 1 in 200 year event.

Loss development tables providing information about historical claims development are included in note 13.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (CONTINUED)

(b) Market risk

Market risk is the impact arising from the uncertainty of asset prices, interest rates, foreign exchange rates, and other factors related to financial markets and investment asset management.

XL Catlin Group imposes restrictions on the external investment managers' investment strategies. Strict limits, by trust fund, are set for types of assets held, concentration limits and average investment grade ratings. Investments are typically investment grade bonds and investment grade asset backed securities. Guidelines and benchmarks are set annually and approved by the board.

The performance of the investment managers is monitored constantly by XL Catlin Group investment specialists and reported monthly to CUAL management and reviewed quarterly by the CUAL Board of directors. The Syndicate aims to manage exchange rate exposure in US dollar terms and asset and liabilities are duration matched. As at 31 December 2016, more than 90% of the Syndicate's investments are rated A or above. The Syndicate does not use hedge accounting.

(i) Interest rate risk

Interest rate risk arises primarily from investments in fixed interest securities. In addition to the extent that claims inflation is correlated to interest rates, liabilities to policyholders are exposed to interest rate risk.

The Syndicate monitors interest rate risk on a monthly basis by calculating the impact of changes in interest rate on the value of investments and the net present value of liabilities against a risk appetite that has been agreed with the Board.

The sensitivity analysis for interest rate risk illustrates how changes in the fair value of future cash flows of an interest bearing financial asset will fluctuate because of changes in market interest rates at the reporting date.

Sensitivity analysis

Changes in interest yields, with all other variables constant, would result in changes in the capital value of debt securities and borrowings as well as subsequent interests receipts and payments. This would affect reported profits and net assets as indicated in the table below:

	Impact on profit after tax		**Impact on net assets**	
	2016	*2015*	**2016**	*2015*
	$m	*$m*	**$m**	*$m*
50 basic points increase	**(48.0)**	*(47.8)*	**(48.0)**	*(47.8)*
50 basic points decrease	**48.0**	*47.8*	**48.0**	*47.8*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (CONTINUED)

(b) Market risk (continued)

(ii) Equity price risk

The Syndicate is exposed to equity securities price risk as a result of its holdings in equity investments, classified as financial assets at fair value through statement of profit or loss. Exposures to individual companies and to equity shares in aggregate are monitored in order to ensure compliance with the relevant regulatory limits for solvency purposes.

The Syndicate has a defined investment policy which sets limits on the syndicate's exposure to equities both in aggregate terms and by geography, industry and counterparty. This policy of diversification is used to manage the syndicate's price risk arising from its investments in equity securities.

As at 31 December 2016 the Syndicate had $81.4m of equity investments of which 83% were listed securities (2015: $82.3m and 72% respectively).

	Impact on profit after tax		Impact on net assets	
	2016	*2015*	**2016**	*2015*
	$m	*$m*	**$m**	*$m*
5% increase in stock market prices	**11.1**	*12.0*	**11.1**	*12.0*
5% decrease in stock market prices	**(11.1)**	*(12.0)*	**(11.1)**	*(12.0)*

(iii) Currency risk

The Syndicate manages its foreign exchange risk against its functional currency. Foreign exchange arises when future commercial transactions or recognised assets and liabilities are denominated in a currency that is not the Syndicate's functional currency.

The Syndicate is primarily exposed to currency risk in respect of liabilities under policies of insurance denominated in currencies other than US Dollars. The most significant currencies to which the Syndicate is exposed are Pounds Sterling, Canadian Dollar and Euro. The Syndicate seeks to mitigate the risk by matching the estimated foreign currency denominated liabilities with assets denominated in the same currency.

Sensitivity analysis

Fluctuations in the Syndicate's trading currencies against the US dollar would result in a change to profit after tax and net assets value.

The table below gives an indication of the impact on profit after tax and net assets of a percentage change in the relative strength of the US dollar against the value of the Euro, the Canadian dollar and the Sterling, simultaneously. The analysis is based on current information.

	Impact on profit after tax		Impact on net assets	
Changes to Sterling, Canadian dollar and Euros relative to US dollar	**2016** **$000's**	*2015* *$000's*	**2016** **$000's**	*2015* *$000's*
USD weakens 10% against other currencies	**13,156**	*6,230*	**19,312**	*18,614*
USD weakens 5% against other currencies	**6,578**	*3,115*	**9,656**	*9,307*
USD strengthens 5% against other currencies	**(6,265)**	*(2,967)*	**(9,196)**	*(8,864)*
USD strengthens 10% against other currencies	**(11,960)**	*(5,664)*	**(17,557)**	*(16,922)*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (CONTINUED)

(b) Market risk (continued)

(iii) Currency risk (continued)

2016

	GBP	USD	EUR	CAD	AUD	OTH	TOTAL
	$000's	$000's	$000's	$000's	$000's	$000's	$000's
Financial investments	202,608	2,376,429	237,477	314,893	—	2,387	3,133,794
Overseas deposits	—	47,035	—	79,444	189,028	83,037	398,544
Reinsurers' share of technical provisions	112,853	1,025,049	84,365	88,431	—	—	1,310,698
Insurance and Reinsurance receivables	70,518	1,344,125	97,240	58,197	—	—	1,570,080
Cash and cash equivalents	12,788	172,601	9,083	9,345	—	—	203,817
Other assets	46,571	379,261	30,047	61,942	—	—	517,821
Total assets	445,338	5,344,500	458,212	612,252	189,028	85,424	7,134,754
Technical provisions	514,091	4,270,350	419,069	377,094	—	—	5,580,604
Insurance and reinsurance payables	109,970	765,041	80,327	64,280	—	—	1,019,618
Other creditors	19,201	276,943	9,151	3,949	—	—	309,244
Total Liabilities	643,262	5,312,334	508,547	445,323	—	—	6,909,466

2015

	GBP	USD	EUR	CAD	AUD	OTH	TOTAL
	$000's	$000's	$000's	$000's	$000's	$000's	$000's
Financial investments	264,489	2,227,699	289,233	271,506	1,079	1,951	3,055,957
Overseas deposits	—	43,280	—	65,044	195,336	72,026	375,686
Reinsurers' share of technical provisions	95,872	1,041,317	73,827	70,187	—	—	1,281,203
Insurance and Reinsurance receivables	122,308	1,215,833	98,818	47,759	—	—	1,484,718
Cash and cash equivalents	2,821	158,319	7,884	761	357	7,255	177,397
Other assets	115,987	275,544	53,584	52,804	—	—	497,919
Total assets	601,477	4,961,992	523,346	508,061	196,772	81,232	6,872,880
Technical provisions	649,706	4,119,434	378,893	320,631	—	—	5,468,664
Insurance and reinsurance payables	109,335	705,538	83,789	48,057	—	1	946,720
Other creditors	128,622	80,785	1,277	4,432	—	—	215,116
Total Liabilities	887,663	4,905,757	463,959	373,120	—	1	6,630,500

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (continued)

(c) Credit risk

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. Key areas where the Syndicate is exposed to credit risk are:

- reinsurers' share of insurance liabilities;
- amounts due from reinsurers in respect of claims already paid;
- amounts due from insurance contract holders;
- amounts due from insurance intermediaries;
- amounts due from issuers of debt securities; and
- counterparty risk with respect to derivative transactions.

The Syndicate manages the levels of credit risk it accepts by placing limits on its exposure to a single counterparty, or groups of counterparties, and monitoring its exposure to regions, countries and industries. Such risks are subject to regular review.

Changes to the limits on the level of credit risk by category and territory are approved annually by the managing agency Board of Directors. Reinsurance is used to manage insurance risk. This does not, however, discharge the Syndicate's liability as primary insurer. If a reinsurer fails to pay a claim, the syndicate remains liable for the payment to the policyholder. The creditworthiness of reinsurers is considered on an ongoing basis by reviewing their financial strength prior to finalisation of any contract. In addition, management assesses the creditworthiness of all reinsurers and intermediaries by reviewing credit grades provided by rating agencies and other publicly available financial information. The recent payment history of reinsurers is also used to update the reinsurance purchasing strategy. In certain circumstances, deposits from reinsurers are also held as collateral.

The table below provides information on the credit quality of financial assets of the Syndicate that are neither past due nor impaired:

2016	AAA	AA	A	BBB or below	Not rated	Total
	$000's	$000's	$000's	$000's	$000's	$000's
Debt securities and other fixed income securities	1,029,004	843,209	588,579	80,955	—	2,541,747
Deposits with ceding undertakings	—	—	—	—	918	918
Cash and cash equivalents	—	—	—	—	203,817	203,817
Overseas deposits as investments	206,141	60,052	36,292	15,834	80,225	398,544
Reinsurance debtors	—	32,108	161,579	87	133	193,907
Reinsurers' share of claims outstanding	—	—	837,748	7,090	12,049	856,887
Other debtors	—	—	—	—	1,174,832	1,174,832
Shares and other variable yield securities and units in unit trusts	—	—	—	—	505,417	505,417
Derivative assets	—	—	—	—	—	—
Other investments	—	13,579	1,007	72,044	—	86,630
Insurance debtors	—	—	—	—	1,172,055	1,172,055
Total	1,235,145	948,948	1,625,205	176,010	3,149,446	7,134,754

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (continued)

(c) Credit risk (continued)

2015	*AAA*	*AA*	*A*	*BBB or below*	*Not rated*	*Total*
	$000's	*$000's*	*$000's*	*$000's*	*$000's*	*$000's*
Debt securities and other fixed income securities	*1,570,743*	*535,928*	*448,255*	*109,658*	*35,707*	*2,700,291*
Deposits with ceding undertakings	—	—	—	—	*851*	*851*
Cash and cash equivalents	—	—	—	—	*177,397*	*177,397*
Overseas deposits	*211,796*	*85,201*	*36,480*	*41,277*	*932*	*375,686*
Reinsurance debtors	*43,185*	*55,228*	—	*60*	*33*	*98,506*
Reinsurers' share of claims outstanding	—	*295,533*	*493,063*	*2,004*	*105*	*790,705*
Other debtors	—	—	*1,196*	—	*1,194,792*	*1,195,988*
Shares and other variable yield securities and units in unit trusts	*979*	—	—	—	*274,214*	*275,193*
Derivative assets	—	—	—	—	*38*	*38*
Other investments	—	—	—	—	*80,433*	*80,433*
Insurance debtors	—	—	—	—	*1,177,792*	*1,177,792*
Total	*1,826,703*	*971,890*	*978,994*	*152,999*	*2,942,294*	*6,872,880*

The concentration of credit risk is substantially unchanged compared to prior year. There were no material unapproved breaches of credit limits during the year. The Syndicate maintains strict control limits on open derivative positions, by both amount and term. The amount subject to credit risk at any one time is limited to the current fair value of derivative financial assets.

The Syndicate has insurance and reinsurance debtors that are past due but not considered to be impaired. The syndicate does not currently hold any impaired assets (2015: no impaired assets held).

2016	**Up to three months**	**Three to six months**	**Six months to one year**	**Greater than one year**	**Total**
	$000's	**$000's**	**$000's**	**$000's**	**$000's**
Insurance debtors	**15,403**	**13,196**	**2,767**	**541**	**31,907**
Reinsurance debtors	**166**	**993**	**—**	**(1,223)**	**(64)**
Total	**15,569**	**14,189**	**2,767**	**(682)**	**31,843**

2015	*Up to three months*	*Three to six months*	*Six months to one year*	*Greater than one year*	*Total*
	$000's	*$000's*	*$000's*	*$000's*	*$000's*
Insurance debtors	*22,013*	*6,501*	*413*	*2,861*	*31,788*
Reinsurance debtors	*533*	*173*	*-*	*(956)*	*(250)*
Total	*22,546*	*6,674*	*413*	*1,905*	*31,538*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (continued)

(d) Liquidity risk

Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The primary liquidity risk of the syndicate is the obligation to pay claims as they fall due. The projected settlement of these liabilities is modelled, on a regular basis, using actuarial techniques. The Syndicate manages this risk by maintaining sufficient liquid assets to meet expected cash flow requirements.

The following tables analyse financial liabilities by maturity date:

2016	**Less than one year on demand**	**Between 1 and 3 years**	**Between 3 and 5 years**	**Over 5 years**	**Total**
	$000's	**$000's**	**$000's**	**$000's**	**$000's**
Deposits received from reinsurers	**2,636**	**—**	**—**	**—**	**2,636**
Other creditors	**653,776**	**591,062**	**—**	**—**	**1,244,838**
Claims outstanding	**1,399,667**	**1,172,190**	**532,023**	**1,039,599**	**4,143,479**
Financial liabilities	**2,056,079**	**1,763,252**	**532,023**	**1,039,599**	**5,390,953**

2015	*Less than one year on demand*	*Between 1 and 3 years*	*Between 3 and 5 years*	*Over 5 years*	*Total*
	$000's	*$000's*	*$000's*	*$000's*	*$000's*
Deposits received from reinsurers	*2,636*	*—*	*—*	*—*	*2,636*
Other creditors	*520,042*	*551,721*	*—*	*—*	*1,071,763*
Claims outstanding	*1,340,034*	*1,303,940*	*613,099*	*696,271*	*3,953,344*
Financial liabilities	*1,862,712*	*1,855,661*	*613,099*	*696,271*	*5,027,743*

The nature of insurance is that the requirements of funding cannot be predicted with absolute certainty and therefore the theory of probability is applied on insurance contracts to ascertain the likely provision and the time period when such liabilities will require settlement.

(e) Operational risk

This is the risk of loss resulting from inadequate or failed internal processes and systems, or from external events.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (continued)

(f) Fair value estimation

With the adoption of FRS 102 on fair value hierarchy disclosures, below are the methods and assumptions used by the Syndicate in estimating the fair value of its financial instruments, together with its categorisation:

The categorising of these assets is defined as follows:

Level 1: The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.

Level 3: Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

Fixed maturities and short-term investments
Fair values of fixed maturities and short-term investments are based on the quoted market price of these securities provided by either independent pricing services, or, when such prices are not available, by reference to broker or underwriting bid indications.

The Syndicate's Level 3 fixed maturities include RMBS, CMBS, ABS and corporate securities, for which pricing vendors and broker quotes are the primary source of the valuations. The syndicate compares the price to independent valuations, which may also consist of broker quotes, to assess if the prices received represent a reasonable estimate of the fair value. Although the syndicate does not have access to the specific unobservable inputs that may have been used in the fair value measurements of RMBS, CMBS and ABS, the syndicate would expect that the significant inputs considered are prepayment rates, probability of default, loss severity in the event of default, recovery rates, liquidity premium and reinvestment rates. Significant increases or decreases in any of those inputs in isolation could result in a significantly different fair value measurement. Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

The Syndicate's level 3 investments also include fixed maturities where the prices provided by vendors have been unchanged for 3 months or more.

The fair value of investments in funds is based on the net asset value provided by the funds' administrators. The fair values of holdings in equity and loan instruments are based on the market price of these securities provided by independent pricing services, or, when such prices are not available, by reference to broker or underwriting bid indications provided by administrators and recent transactions, if any.

The Syndicate's Level 3 other invested assets consist of investments in funds with significant redemption restrictions and unquoted private equity and debt, for which manager NAV statements are the primary source of the valuations. Although the Syndicate does not have access to the specific unobservable inputs that may have been used in the fair value measurements, the Syndicate would expect the significant inputs for private equity and debt to be discounted cash flows and valuations of similar sized peers. Significant increases or decreases in any of those inputs in isolation could result in a significantly different fair value measurement.

The Syndicate's level 3 investments also include other invested assets where the prices provided by vendors have been unchanged for 3 months or more.

Derivatives
The fair values of interest rate, foreign exchange, equity market and credit default derivative contracts are based on prices provided by independent pricing services.

Other assets and liabilities
The fair values of cash and cash equivalents, premiums and other receivables, and accounts payable approximate their carrying value due to the immediate or short term maturity of these financial instruments.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

2 MANAGEMENT OF FINANCIAL RISK (continued)

(f) Fair value estimation (continued)

The following tables present the Syndicate's holdings of assets measured at fair value:

2016	**Level 1**	**Level 2**	**Level 3**	**Total**
	\$000's	**\$000's**	**\$000's**	**\$000's**
Assets				
Fair value through Profit and Loss:				
Shares and other variable yield securities and units in unit trusts	**211,705**	**52,168**	**241,544**	**505,417**
Derivative financial instruments	**—**	**—**	**—**	**—**
Debt securities and other fixed income securities	**—**	**2,448,538**	**4,529**	**2,453,067**
Loans and deposits with credit institutions	**—**	**81,538**	**7,142**	**88,680**
Overseas deposits	**112,153**	**286,391**	**—**	**398,544**
Other investments	**—**	**44,432**	**42,198**	**86,630**
	323,858	**2,913,067**	**295,413**	**3,532,338**

The Syndicate also holds investments in associates and joint ventures held at cost adjusted for the Syndicate's share of earnings or losses and distributions worth \$71.9m (2015: \$72.3m).

2015	*Level 1*	*Level 2*	*Level 3*	*Total*
	\$000's	*\$000's*	*\$000's*	*\$000's*
Assets				
Fair value through Profit and Loss:				
Shares and other variable yield securities and units in unit trusts	*59,453*	*69,261*	*146,478*	*275,192*
Derivative financial instruments	*—*	*—*	*38*	*38*
Debt securities and other fixed income securities	*243,679*	*2,334,250*	*67,247*	*2,645,176*
Loans and deposits with credit institutions	*—*	*46,479*	*8,122*	*54,601*
Overseas deposits	*103,903*	*271,783*	*—*	*375,686*
Other investments	*—*	*—*	*62,048*	*62,048*
	407,035	*2,721,773*	*283,933*	*3,412,741*

Fair value estimates included in Level 3 are hedge funds with significant redemption restrictions, collateralised debt obligations ("CDO"), sub-prime securities, Alt A securities and securities rated CCC and below.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

3 MANAGEMENT OF CAPITAL

(a) Capital Framework at Lloyd's

The Society of Lloyd's (Lloyd's) is a regulated undertaking and subject to the supervision of the Prudential Regulatory Authority (PRA) under the Financial Services and Markets Act 2000 and in accordance with Solvency II legislation.

Within this supervisory framework, Lloyd's applies capital requirements at member level and centrally to ensure that Lloyd's complies with Solvency II, and beyond that to meet its own financial strength, licence and ratings objectives.

Although, as described below, Lloyd's capital setting processes use a capital requirement set at syndicate level as a starting point, the requirement to meet Solvency II and Lloyd's capital requirements applies at overall and member level respectively, not at syndicate level. Accordingly the capital requirement in respect of Syndicate 2003 is not disclosed in these financial statements. See notes 21 and 22 for details of the Syndicate's FAL and FIS requirements.

(b) Lloyd's Capital Setting Process

In order to meet Lloyd's requirements, each Syndicate is required to calculate its Solvency Capital Requirement (SCR) for the prospective underwriting year. This amount must be sufficient to cover a 1 in 200 year loss, reflecting uncertainty in the ultimate run-off of underwriting liabilities (SCR 'to ultimate'). The syndicate must also calculate its SCR at the same confidence level but reflecting uncertainty over a one year time horizon (one year SCR) for Lloyd's to use in meeting Solvency II requirements. The SCRs of each Syndicate are subject to review by Lloyd's and approval by the Lloyd's Capital and Planning Group.

A Syndicate may be comprised of one or more underwriting members of Lloyd's. Each member is liable for its own share of underwriting liabilities on the Syndicate(s) on which it participates but not other members' shares. Accordingly, the capital requirement that Lloyd's sets for each member operates on a similar basis. Each member's SCR shall thus be determined by the sum of the member's share of the Syndicate SCR 'to ultimate'. Where a member participates on more than one Syndicate, a credit for diversification is provided to reflect the spread of risk, but consistent with determining an SCR which reflects the capital requirement to cover a 1 in 200 year loss 'to ultimate' for that member. Over and above this, Lloyd's applies a capital uplift to the member's capital requirement, known as the Economic Capital Assessment (ECA). The purpose of this uplift, which is a Lloyd's not a Solvency II requirement, is to meet Lloyd's financial strength, licence and ratings objectives. The capital uplift applied for 2016 was 35% of the member's SCR 'to ultimate'.

(c) Provision of capital by members

Each member may provide capital to meet its ECA either by assets held in trust by Lloyd's specifically for that member (Funds at Lloyd's), held within and managed within a Syndicate (Funds in Syndicate) or as the member's share of the members' balances on each Syndicate on which it participates.

Resources available to meet members' and Lloyd's capital requirements are separately identified in the Statement of Changes in Member's Balances.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

4 SEGMENTAL ANALYSIS

Gross premiums written, gross premiums earned, gross claims incurred, gross operating expenses and the reinsurance balances by class of business are as follows:

2016	**Gross Premiums Written**	**Gross Premiums Earned**	**Gross Claims Incurred**	**Gross Operating Expenses**	**Reinsurance Balance**	**Total**
	$000's	**$000's**	**$000's**	**$000's**	**$000's**	**$000's**
Fire and other damage to property	**705,986**	**664,923**	**(381,544)**	**(209,475)**	**(89,357)**	**(15,453)**
Accident and health	**115,509**	**110,901**	**(72,207)**	**(41,159)**	**(11,763)**	**(14,228)**
Third party liability	**271,985**	**271,469**	**(114,918)**	**(92,418)**	**(39,895)**	**24,238**
Marine, aviation and transport	**379,419**	**346,670**	**(193,970)**	**(97,034)**	**(46,212)**	**9,454**
Motor (third party liability)	**41,239**	**41,428**	**(24,173)**	**(16,297)**	**(4,604)**	**(3,646)**
Miscellaneous	**100,718**	**76,161**	**(32,460)**	**(25,599)**	**(9,264)**	**8,838**
	1,614,856	**1,511,552**	**(819,272)**	**(481,982)**	**(201,095)**	**9,203**
Reinsurance	**1,340,341**	**1,460,810**	**(831,109)**	**(414,897)**	**(214,574)**	**230**
Total	**2,955,197**	**2,972,362**	**(1,650,381)**	**(896,879)**	**(415,669)**	**9,433**

2015	*Gross Premiums Written*	*Gross Premiums Earned*	*Gross Claims Incurred*	*Gross Operating Expenses*	*Reinsurance Balance*	*Total*
	$000's	*$000's*	*$000's*	*$000's*	*$000's*	*$000's*
Fire and other damage to property	*595,160*	*587,326*	*(272,277)*	*(195,295)*	*(105,108)*	*14,646*
Accident and health	*120,590*	*108,026*	*(59,983)*	*(52,899)*	*(5,884)*	*(10,740)*
Third party liability	*263,863*	*265,240*	*(120,828)*	*(82,839)*	*(49,430)*	*12,143*
Marine, aviation and transport	*289,734*	*314,004*	*(153,870)*	*(80,775)*	*(74,063)*	*5,296*
Motor (third party liability)	*39,685*	*40,067*	*(19,180)*	*(15,308)*	*(4,850)*	*729*
Miscellaneous	*85,715*	*69,680*	*(16,953)*	*(26,030)*	*(13,285)*	*13,412*
	1,394,747	*1,384,343*	*(643,091)*	*(453,146)*	*(252,620)*	*35,486*
Reinsurance	*1,544,452*	*1,602,939*	*(868,440)*	*(477,290)*	*(267,645)*	*(10,436)*
Total	*2,939,199*	*2,987,282*	*(1,511,531)*	*(930,436)*	*(520,265)*	*25,050*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

4 SEGMENTAL ANALYSIS (continued)

The reinsurance balance represents the charge to the technical account from the aggregate of all items relating to outwards reinsurance.

The Lloyd's insurance market has been treated as one geographical segment. All business is signed and concluded in the UK.

The geographical analysis of gross premiums written by risk location is as follows:

	Attributable to all business		Attributable to direct business	
	2016	*2015*	**2016**	*2015*
	$000's	*$000's*	**$000's**	*$000's*
United Kingdom	**367,893**	*188,109*	**202,748**	*89,264*
Other EU Countries	**330,230**	*243,954*	**181,992**	*115,764*
US	**1,533,718**	*867,064*	**845,244**	*411,450*
Oceania	**187,920**	*243,954*	**103,564**	*115,764*
Other	**535,366**	*1,396,118*	**295,044**	*662,505*
	2,955,127	*2,939,199*	**1,628,592**	*1,394,747*

5 MOVEMENT IN PRIOR YEAR'S PROVISION FOR CLAIMS OUTSTANDING

A favourable run off deviation (prior accident year release) of $167.2m (2015: favourable run off deviation of $12.3m) was experienced during the year in respect of various lines of business. The most significantly releases were within energy ($75.5m), reinsurance ($34.3m), casualty ($26.8m), financial lines ($24.7m) and marine ($21.1m). These were partially offset by increases in accident & health ($15.7m). This is mainly due to a reduction in the ultimate loss estimates.

6 DEFERRED ACQUISITION COSTS

	2016	*2015*
	$000's	*$000's*
On insurance contracts	**315,223**	*362,274*

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

	2016	*2015*
	$000's	*$000's*
At 1 January	**362,274**	*407,823*
Expenses for the acquisition of contracts deferred during the year	**(28,548)**	*(39,190)*
Foreign exchange losses	**(18,503)**	*(6,359)*
At 31 December	**315,223**	*362,274*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

7 NET OPERATING EXPENSES

	2016 $000's	*2015 $000's*
Acquisition costs	**573,119**	*603,809*
Change in deferred acquisition costs	**28,548**	*39,190*
	601,667	*642,999*
Administration expenses	**295,212**	*287,437*
Reinsurance commissions and profit participation	**(60,291)**	*(61,187)*
	836,588	*869,249*

Included within acquisition costs are amounts relating to commissions on direct insurance business of $289.7m (2015: $297.5m).
Administrative expenses include:

	2016 $000's	*2015 $000's*
Audit Services:		
Fees payable to the Syndicate's auditor for the audit of the Syndicate's accounts	**798**	*973*
Non-audit Services:		
Fees payable to the Syndicate's auditor for other services:		
Other services pursuant to legislation, including the audit of the regulatory return	**206**	*251*
	1,004	*1,224*

The auditors' remuneration for the year has been borne by another group company.

8 STAFF NUMBERS AND COSTS

The Syndicate has no direct employees. The employees that provide services to the Syndicate are employed by other XL Catlin Group companies and are recharged to the Syndicate. The expense recharge includes the cost of these employees but it is not possible to ascertain separately the element of the expense recharge that relates directly to staff costs or staff numbers.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

9 DIRECTORS AND ACTIVE UNDERWRITERS' EMOLUMENTS

XL Services UK Ltd. charges the Syndicate the following amounts in respect of aggregate emoluments paid to the directors of Catlin Underwriting Agencies Limited:

	2016 $000's	*2015 $000's*
Aggregate emoluments and other benefits	**2,800**	*4,553*
Pension contributions	**31**	*121*
	2,831	*4,674*

Emoluments of the highest paid director are:

	2016 $000's	*2015 $000's*
Aggregate emoluments and other benefits	1,093	2,148
Pension contributions	10	50
	1,103	2,198

The Active Underwriter received the following aggregate remuneration charged to the Syndicate:

	2016 $000's	*2015 $000's*
Aggregate emoluments and other benefits	**399**	*356*
Pension contributions	**11**	*6*
	410	*362*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

10 INVESTMENT RETURN

	2016 **$000's**	*2015* *$000's*
Investment income		
Income from financial investments	**60,977**	*67,649*
Gains on realisation of investments	**20,445**	*48,470*
	81,422	*116,119*
Net unrealised gains/(losses) on investments	**31,372**	*(10,849)*
Investment expenses and charges		
Investment management expenses	**(7,841)**	*(15,547)*
Losses on the realisation of investments	**(7,349)**	*(27,773)*
	(15,190)	*(43,320)*
Total investment return	**97,604**	*61,950*

Investment return is analysed between:

	2016	*2015*
	$000's	*$000's*
Allocated investment return transferred to the general business technical account	**93,482**	*60,061*
Net investment return included in the non-technical account	**4,122**	*1,889*
Total investment return	**97,604**	*61,950*

Included in the above is a return of $4,122k (2015: $1,889k) of investment income earned on Funds in Syndicate deposited by Catlin Syndicate Limited into the Syndicate's Premium Trust Funds (see note 22).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

11 OTHER FINANCIAL INVESTMENTS

	Market value		Cost	
	2016 $000's	*2015 $000's*	**2016 $000's**	*2015 $000's*
Financial assets				
Fair value through Profit and Loss:				
Shares and other variable yield securities and units in unit trusts	**505,417**	*275,194*	**469,475**	*271,775*
Derivative financial instruments	**—**	*38*	**—**	*8,196*
Debt securities and other fixed income securities	**2,453,067**	*2,645,175*	**2,463,374**	*2,648,853*
Loans and deposits with credit institutions	**88,680**	*55,116*	**88,853**	*59,196*
Other investments	**86,630**	*80,434*	**76,115**	*64,212*
Total financial assets	**3,133,794**	*3,055,957*	**3,097,817**	**3,052,232**

Included in the above are Funds In Syndicate of $157m (2015: $195m) placed by Catlin Syndicate Limited (see note 22).

a) Listed investments

Included in the carrying values above are amounts in respect of listed investments as follows:

	2016 $000's	*2015 $000's*
Shares and other variable yield securities and units in unit trusts	**91,870**	*128,754*
Debt securities and other fixed income securities	**1,700,328**	*2,692,256*
	1,792,198	*2,821,010*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

12 INSURANCE LIABILITIES AND REINSURANCE ASSETS

2016	**Provision for unearned premium $000's**	**Claims Outstanding $000's**
Gross Technical Provisions		
As at 1 January 2016	**1,515,320**	**3,953,344**
Movement in the provision	**(17,165)**	**260,508**
Foreign exchange movements	**(61,030)**	**(70,373)**
As at 31 December 2016	**1,437,125**	**4,143,479**
Reinsurers' share of technical provisions		
As at 1 January 2016	**490,497**	**790,706**
Movement in the provision	**(21,455)**	**75,825**
Foreign exchange movements	**(15,231)**	**(9,644)**
As at 31 December 2016	**453,811**	**856,887**
Net technical provisions		
As at 1 January 2016	**1,024,823**	**3,162,638**
As at 31 December 2016	**983,314**	**3,286,592**

The gross claims reported, the loss adjustment liabilities and the liabilities for claims incurred but not reported are gross of expected recoveries from salvage and subrogation.

2015	*Provision for unearned premium $000's*	*Claims Outstanding $000's*
Gross Technical Provisions		
As at 1 January 2015	*1,610,941*	*3,985,091*
Movement in the provision	*(48,083)*	*88,212*
Foreign exchange movements	*(47,538)*	*(119,959)*
As at 31 December 2015	*1,515,320*	*3,953,344*
Reinsurers' share of technical provisions		
As at 1 January 2015	*462,061*	*805,879*
Movement in the provision	*41,828*	*1,908*
Foreign exchange movements	*(13,392)*	*(17,081)*
As at 31 December 2015	*490,497*	*790,706*
Net technical provisions		
As at 1 January 2015	*1,148,880*	*3,179,212*
As at 31 December 2015	*1,024,823*	*3,162,638*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

13 CLAIMS DEVELOPMENT TRIANGLES

To illustrate the robustness of our reserves, the loss development tables below provide information about historical claims development by the pure underwriting year.

Gross claims development

	2011 & Prior	2012	2013	2014	2015	2016	Total
	$000's	$000's	$000's	$000's	$000's	$000's	$000's
12 months		788,411	702,745	751,028	704,165	844,456	
24 months		1,371,129	1,319,184	1,479,390	1,454,995		
36 months		1,361,571	1,307,218	1,569,833			
48 months		1,393,067	1,291,475				
60 months		1,367,623					
Estimate total losses	**21,234,414**	**1,367,623**	**1,291,475**	**1,569,833**	**1,454,995**	**844,456**	**27,762,796**
Paid claims	**(20,057,284)**	**(1,069,387)**	**(875,057)**	**(911,374)**	**(570,981)**	**(135,234)**	**(23,619,317)**
Gross reserves	**1,177,130**	**298,236**	**416,418**	**658,459**	**884,014**	**709,222**	**4,143,479**

Net claims development

	2011 & Prior	2012	2013	2014	2015	2016	Total
	$000's	$000's	$000's	$000's	$000's	$000's	$000's
12 months		627,100	567,930	568,923	548,055	668,674	
24 months		1,139,970	1,043,207	1,128,558	1,121,970		
36 months		1,131,567	1,044,708	1,191,748			
48 months		1,140,651	1,035,658				
60 months		1,125,672					
Estimate total losses	**12,843,959**	**1,125,672**	**1,035,658**	**1,191,748**	**1,121,970**	**668,674**	**17,987,681**
Paid claims	**(11,866,459)**	**(853,982)**	**(676,140)**	**(730,821)**	**(447,339)**	**(126,348)**	**(14,701,089)**
Net reserves	**977,500**	**271,690**	**359,518**	**460,927**	**674,631**	**542,326**	**3,286,592**

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

14 DEBTORS ARISING OUT OF DIRECT INSURANCE OPERATIONS

	2016 $000's	*2015 $000's*
Due within one year	**1,171,513**	*1,177,105*
Due after one year	**541**	*687*
	1,172,054	*1,177,792*

15 OTHER DEBTORS:

Amounts falling due within one year

	2016 $000's	*2015 $000's*
Amounts owed from group undertakings	**79,907**	*1,196*
Overseas taxation including federal excise tax	**28,526**	*32,968*
Salvage and subrogation recoveries	**—**	*985*
Investment settlements	**531**	*5,448*
Other debtors	**9,671**	*10,803*
	118,635	*51,400*

16 OTHER DEBTORS:

Amounts falling due after one year

	2016 $000's	*2015 $000's*
Salvage and subrogation recoveries	**42,858**	*36,400*
Other debtors	**12,086**	*17,638*
	54,944	*54,038*

17 OVERSEAS DEPOSITS

Overseas deposits include the following trust fund balances:

	2016 $000's	*2015 $000's*
Illinois - USA	**11,205**	*9,604*
South African deposit	**4,616**	*2,907*
Additional Securities Limited	**80,135**	*81,834*
Kentucky trust funds	**10,879**	*10,439*
Australian trust fund	**177,626**	*184,256*
Joint Asset Trust Fund - Australia	**11,181**	*7,208*
Joint Asset Trust Fund - USA	**23,458**	*14,395*
Canadian Margin Fund	**79,444**	*65,043*
	398,544	*375,686*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

18 CREDITORS ARISING OUT OF DIRECT INSURANCE OPERATIONS

	2016 $000's	*2015 $000's*
Due within one year	**6,330**	*18,588*
Due after one year	**4,606**	*160*
	10,936	*18,748*

19 OTHER CREDITORS:

Amounts falling due within one year

	2016 $000's	*2015 $000's*
Amounts owed to group undertakings	**138,006**	*94,791*
Outstanding investment balances	**—**	*8,484*
Other creditors	**81,478**	*17,752*
	219,484	*121,027*

20 OTHER CREDITORS:

Amounts falling due after one year

	2016 $000's	*2015 $000's*
Other creditors	**5,147**	*4,021*
	5,147	*4,021*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED) FOR THE YEAR ENDED 31 DECEMBER 2016

21 FUNDS AT LLOYD'S

Every member is required to hold capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL). As at 31 December 2016, the value of assets supporting FAL for the 2017 year of account is $1,087.3m. These funds are intended primarily to cover circumstances where syndicate assets prove insufficient to meet participating members' underwriting liabilities.

The level of FAL/FIS that Lloyd's requires a member to maintain is determined by Lloyd's based on PRA requirements and resource criteria. This capital requirement is based on a number of factors including the nature and amount of risk to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. Since FAL is not under the management of the managing agent, no amount has been shown in these financial statements by way of such capital resources. However, the managing agent is able to make a call on the member's FAL to meet liquidity requirements or to settle losses.

22 FUNDS IN SYNDICATE

Catlin Syndicate Limited, the sole corporate member of the Syndicate, holds investments in the Syndicate to be used as collateral to support the Syndicate's capital requirements, or Funds at Lloyd's. These investments give the Syndicate the ability to manage these funds under the same Investment Management Agreement as the other funds of the Syndicate that are held in the premium trust funds.

At 31 December 2016, $157m of investments were held as Funds in Syndicate (2015: $195m).

The investments realised a profit of $4.1m for the year to 31 December 2016 (2015: $1.9m). The balance of $157m is included within member's balances on the Syndicate's statement of financial position and is owed exclusively to Catlin Syndicate Limited.

23 ULTIMATE PARENT UNDERTAKING

Catlin Syndicate Limited is the sole member of Syndicate 2003.

Catlin Insurance Company Ltd, a company registered in Bermuda, is the parent undertaking of the smallest group to consolidate the financial statements of Catlin Syndicate Limited. Copies of the Catlin Insurance Company Ltd consolidated financial statements can be obtained from The Secretary, Catlin Insurance Company Ltd, O'Hara House, One Bermudiana Road, Hamilton, Bermuda HM08.

The ultimate parent undertaking and controlling party is XL Group Ltd, a company registered in Bermuda, which is the parent undertaking of the largest group to consolidate the financial statements of Catlin Syndicate Limited. Copies of the XL Group Ltd consolidated financial statements can be obtained from 20 Gracechurch Street, London, EC3V 0BG.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2016

24 RELATED PARTY TRANSACTIONS

Catlin Underwriting Agencies Limited ("CUAL") is the managing agent for Syndicate 2003. Under the standard managing agents' agreement, CUAL receives an annual fee of 1% of stamp capacity. In 2016 this amounted to $20.3m (2015: $23.3m). The balance due to CUAL as at 31 December 2016 was $15.0m (2015: $10.5m).

Catlin Syndicate Limited is the sole member of Syndicate 2003.

The XL Catlin Group wholly owns a number of cover holders which underwrite on behalf of Syndicate 2003 and these are listed below:

Catlin Canada Inc
Catlin Insurance Company Inc US
Catlin Specialty Insurance Company
Catlin Insurance Services Inc
Catlin Underwriting Inc
Catlin France SAS
Catlin Schweiz AG
Catlin Hong Kong Limited
Catlin Guernsey Limited
Catlin Middle East Limited
Catlin Brasil Servicos Tecnicos Ltda
Catlin Australia Pty Limited
Catlin Singapore Pte Limited
Catlin Labuan Limited
Catlin (BB) Ltd
Catlin Ecosse Insurance Limited
Catlin Risk Solutions Limited
Catlin Re Switzerland Ltd
Catlin Europe SE

Commissions and administrative expenses relating to the provision of insurance underwriting by other Group companies are charged to Syndicate 2003 by the respective offices. These amounts are charged to acquisition costs in the statement of profit or loss. The total effect of these on the statement of profit or loss in 2016 totalled $63.0m (2015: $112.3m). The amounts receivable in respect of insurance business and commission payable was $167.4m (2015: $238.1m).

The Syndicate participates in reinsurance contracts with other parts of the Group, including XL Insurance (Bermuda) Limited, which has assumed liability for existing whole account stop loss contract from Catlin Re Switzerland Limited (Bermuda branch) via a novation agreement effective 1 January 2017, and Catlin Insurance Company Ltd. The effect of these contracts on the statement of profit or loss in 2016 is a charge of $63.0m (2015: $95.8m). Amounts relating to these contracts of $147.0m (2015: $80.5m) were payable as at the balance sheet date. Commencing 2012, Syndicate 6112 was created to provide quota share reinsurance cover to Syndicate 2003. The sole corporate member of Syndicate 6112 is Catlin Syndicate 6112 Limited, a group company. The effect of these contracts on the statement of profit or loss 2016 is a charge of $2.5m (2015: credit of $9.2m); the balance payable at the balance sheet date totalled $68.6m (2015: $41.3m).

The Syndicate participated in an intra group reinsurance contract with Catlin Insurance Company (UK) Ltd to normalise the loss ratios across specified lines of business between the two XL Catlin platforms. The effect of this contract on the statement of profit or loss in 2016 was a credit of $17.0m (2015: a credit of $20.3m). Amounts relating to these contracts of $8.1m were receivable (2015: $8.7m payable) as at the balance sheet date. This contract was last renewed for the 2012 year of account, so charges relate wholly to previous years of account.

The Syndicate is serviced in terms of accommodation, staff and other overhead costs by Catlin Holdings Limited and other group companies. The Syndicate is charged its share of these central costs. In 2016 the total recharge from Catlin Holdings Limited and other group companies was $211.0m (2015: $229.6m). At 31 December 2016 the balance receivable from Catlin Holdings Limited and other group companies in relation to this recharge was $2.6m (2015: payable of $5.6m).

At the balance sheet date, Syndicate 2003 had existing reinsurance contracts with several XL Catlin Group companies, with balances recoverable of $0.3m from XL Re Limited (2015: $0.1m) with $1.8m held as collateral (2015: $1.8m), $8.7m from XL Global Reinsurance Company Limited (2015: $8.8m), $18.5k recoverable from Syndicate 1209 (2015: $28.0k) and $0.2m recoverable from XL Re Europe Limited (2015: $0.2m). In turn Syndicate 2003 had a balance of $37.3k payable to Syndicate 1209 in relation to contracts where Syndicate 1209 has ceded business to Syndicate 2003 (2015: $0.1m).