VALIDUS HOLDINGS LTD
Form 10-Q
August 02, 2017
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017

Commission file number 001-33606

VALIDUS HOLDINGS, LTD.
(Exact name of registrant as specified in its charter)

BERMUDA	98-0501001
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

29 Richmond Road, Pembroke, Bermuda HM 08
(Address of principal executive offices and zip code)
(441) 278-9000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	(Do not check if a smaller reporting company)	
		Smaller reporting company	o
		Emerging growth company	o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No x

As of July 31, 2017 there were 79,465,860 outstanding Common Shares, $0.175 par value per share, of the registrant.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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Validus Holdings, Ltd.
Consolidated Balance Sheets
As at June 30, 2017 (unaudited) and December 31, 2016
(Expressed in thousands of U.S. dollars, except share and per share information)

	June 30, 2017 (unaudited)	December 31, 2016
Assets		
Fixed maturity investments trading, at fair value (amortized cost: 2017—$5,424,562; 2016—$5,584,599)	$5,418,643	$5,543,030
Short-term investments trading, at fair value (amortized cost: 2017—$2,871,126; 2016—$2,796,358)	2,871,353	2,796,170
Other investments, at fair value (cost: 2017—$416,996; 2016—$380,130)	448,618	405,712
Investments in investment affiliates, equity method (cost: 2017—$72,532; 2016—$84,840)	103,377	100,431
Cash and cash equivalents	800,405	419,976
Restricted cash	195,039	70,956
Total investments and cash	9,837,435	9,336,275
Premiums receivable	1,940,637	725,390
Deferred acquisition costs	302,857	209,227
Prepaid reinsurance premiums	335,837	77,996
Securities lending collateral	2,514	9,779
Loss reserves recoverable	600,207	430,421
Paid losses recoverable	35,675	35,247
Income taxes recoverable	4,763	4,870
Deferred tax asset	52,655	43,529
Receivable for investments sold	20,519	3,901
Intangible assets	175,518	115,592
Goodwill	227,701	196,758
Accrued investment income	26,968	26,488
Other assets	387,860	134,282
Total assets	$13,951,146	$11,349,755
Liabilities		
Reserve for losses and loss expenses	$3,305,191	$2,995,195
Unearned premiums	1,970,896	1,076,049
Reinsurance balances payable	461,261	54,781
Securities lending payable	2,980	10,245
Deferred tax liability	4,012	3,331
Payable for investments purchased	92,077	29,447
Accounts payable and accrued expenses	385,958	587,648
Notes payable to AlphaCat investors	1,066,159	278,202
Senior notes payable	245,463	245,362
Debentures payable	538,400	537,226
Total liabilities	8,072,397	5,817,486
Commitments and contingent liabilities		
Redeemable noncontrolling interests	1,251,660	1,528,001
Shareholders' equity		
Preferred shares (Issued and Outstanding: 2017—16,000; 2016—6,000)	400,000	150,000
Common shares (Issued: 2017—161,934,355; 2016—161,279,976; Outstanding: 2017—79,518,581; 2016—79,132,252)	28,339	28,224

Treasury shares (2017—82,415,774; 2016—82,147,724)	(14,423)	(14,376)
Additional paid-in capital	807,321	821,023
Accumulated other comprehensive loss	(19,924)	(23,216)
Retained earnings	3,010,118	2,876,636
Total shareholders’ equity available to Validus	4,211,431	3,838,291
Noncontrolling interests	415,658	165,977
Total shareholders’ equity	4,627,089	4,004,268
Total liabilities, noncontrolling interests and shareholders’ equity	$13,951,146	$11,349,755

The accompanying notes are an integral part of these unaudited consolidated financial statements.

Validus Holdings, Ltd.
Consolidated Statements of Income and Comprehensive Income
For the Three and Six Months Ended June 30, 2017 and 2016 (unaudited)
(Expressed in thousands of U.S. dollars, except share and per share information)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(unaudited)		(unaudited)	
Revenues				
Gross premiums written	$792,902	$764,042	$1,983,759	$1,936,833
Reinsurance premiums ceded	(56,222)	(36,229)	(256,328)	(204,064)
Net premiums written	736,680	727,813	1,727,431	1,732,769
Change in unearned premiums	(105,653)	(154,090)	(521,028)	(587,778)
Net premiums earned	631,027	573,723	1,206,403	1,144,991
Net investment income	44,241	39,257	84,455	68,718
Net realized gains on investments	2,274	2,724	1,110	2,140
Change in net unrealized gains on investments	16,321	31,428	29,669	78,872
Income (loss) from investment affiliates	9,466	(589)	14,654	(4,702)
Other insurance related income and other income	1,339	824	2,669	2,237
Foreign exchange (losses) gains	(7,329)	6,286	(5,760)	12,531
Total revenues	697,339	653,653	1,333,200	1,304,787
Expenses				
Losses and loss expenses	296,149	307,130	565,734	531,577
Policy acquisition costs	117,268	107,966	228,896	215,159
General and administrative expenses	96,349	89,688	184,273	175,896
Share compensation expenses	11,146	10,727	20,637	21,964
Finance expenses	14,209	14,166	28,152	29,369
Transaction expenses	4,427	—	4,427	—
Total expenses	539,548	529,677	1,032,119	973,965
Income before taxes, loss from operating affiliate and (income) attributable to AlphaCat investors	157,791	123,976	301,081	330,822
Tax benefit (expense)	987	(1,706)	4,536	412
Loss from operating affiliate	—	—	—	(23)
(Income) attributable to AlphaCat investors	(11,830)	(6,114)	(19,333)	(10,714)
Net income	$146,948	$116,156	$286,284	$320,497
Net (income) attributable to noncontrolling interests	(43,650)	(21,193)	(86,222)	(58,724)
Net income available to Validus	103,298	94,963	200,062	261,773
Dividends on preferred shares	(2,203)	—	(4,406)	—
Net income available to Validus common shareholders	$101,095	$94,963	$195,656	$261,773
Comprehensive income				
Net income	$146,948	$116,156	$286,284	$320,497
Other comprehensive income (loss)				
Change in foreign currency translation adjustments	1,489	(3,287)	2,086	(5,315)
Change in minimum pension liability, net of tax	1,184	479	1,252	396
Change in fair value of cash flow hedge	(144)	64	(46)	(694)
Other comprehensive income (loss), net of tax	2,529	(2,744)	3,292	(5,613)
Comprehensive (income) attributable to noncontrolling interests	(43,650)	(21,193)	(86,222)	(58,724)
Comprehensive income available to Validus	$105,827	$92,219	$203,354	$256,160

Earnings per common share				
Basic earnings per share available to Validus common shareholders	$1.28	$1.16	$2.47	$3.18
Earnings per diluted share available to Validus common shareholders	$1.25	$1.14	$2.42	$3.12
Cash dividends declared per common share	$0.38	$0.35	$0.76	$0.70
Weighted average number of common shares and common share equivalents outstanding:				
Basic	79,270,561	81,950,833	79,202,116	82,386,047
Diluted	80,872,451	83,373,003	80,861,998	83,785,659

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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Validus Holdings, Ltd.
Consolidated Statements of Shareholders' Equity
For the Six Months Ended June 30, 2017 and 2016 (unaudited)
(Expressed in thousands of U.S. dollars)

	Six Months Ended June 30,	
	2017	2016
	(unaudited)	
Preferred shares		
Balance, beginning of period	$150,000	$—
Preferred shares issued	250,000	150,000
Balance, end of period	$400,000	$150,000
Common shares		
Balance, beginning of period	$28,224	$28,100
Common shares issued, net	115	119
Balance, end of period	$28,339	$28,219
Treasury shares		
Balance, beginning of period	$(14,376)	$(13,592)
Repurchase of common shares	(47)	(492)
Balance, end of period	$(14,423)	$(14,084)
Additional paid-in capital		
Balance, beginning of period	$821,023	$1,002,980
Offering expenses on preferred shares	(8,314)	(5,148)
Common shares redeemed, net	(12,076)	(7,504)
Repurchase of common shares	(13,949)	(128,591)
Share compensation expenses	20,637	21,964
Balance, end of period	$807,321	$883,701
Accumulated other comprehensive loss		
Balance, beginning of period	$(23,216)	$(12,569)
Other comprehensive income (loss)	3,292	(5,613)
Balance, end of period	$(19,924)	$(18,182)
Retained earnings		
Balance, beginning of period	$2,876,636	$2,634,056
Net income	286,284	320,497
Net (income) attributable to noncontrolling interests	(86,222)	(58,724)
Dividends on preferred shares	(4,406)	—
Dividends on common shares	(62,174)	(59,227)
Balance, end of period	$3,010,118	$2,836,602
Total shareholders' equity available to Validus	$4,211,431	$3,866,256
Noncontrolling interests	$415,658	$212,154
Total shareholders' equity	$4,627,089	$4,078,410

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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Validus Holdings, Ltd.
Consolidated Statements of Cash Flows
For the Six Months Ended June 30, 2017 and 2016 (unaudited)
(Expressed in thousands of U.S. dollars)

	Six Months Ended June 30,	
	2017	2016
	(unaudited)	
Cash flows provided by (used in) operating activities		
Net income	$286,284	$320,497
Adjustments to reconcile net income to cash provided by (used in) operating activities:		
Share compensation expenses	20,637	21,964
Loss on deconsolidation of AlphaCat ILS fund	402	—
Amortization of discount on senior notes	54	54
(Income) loss from investment affiliates	(14,654)	4,702
Net realized and change in net unrealized gains on investments	(30,779)	(81,012)
Amortization of intangible assets	3,995	2,832
Loss from operating affiliate	—	23
Foreign exchange gains included in net income	(9,686)	(6,289)
Amortization of premium on fixed maturity investments	7,012	8,710
Change in:		
Premiums receivable	(648,195)	(719,070)
Deferred acquisition costs	(97,746)	(102,211)
Prepaid reinsurance premiums	(30,684)	(67,575)
Loss reserves recoverable	(113,508)	(95,429)
Paid losses recoverable	17,500	(4,571)
Reserve for losses and loss expenses	199,985	147,305
Unearned premiums	488,198	655,353
Reinsurance balances payable	111,488	18,610
Other operational balance sheet items, net	(137,618)	(34,450)
Net cash provided by operating activities	52,685	69,443
Cash flows provided by (used in) investing activities		
Proceeds on sales of fixed maturity investments	1,632,371	1,376,077
Proceeds on maturities of fixed maturity investments	247,394	184,413
Purchases of fixed maturity investments	(1,682,609)	(1,537,606)
Purchases of short-term investments, net	(88,623)	(428,040)
Purchases of other investments, net	(33,870)	(19,796)
Decrease (increase) in securities lending collateral	7,265	(5,361)
Redemption from operating affiliates	—	369
Distributions from (investments in) investment affiliates, net	11,708	(16,307)
Increase in restricted cash	(124,083)	(22,752)
Purchase of subsidiary, net of cash acquired	(183,923)	—
Net cash used in investing activities	(214,370)	(469,003)
Cash flows provided by (used in) financing activities		
Net proceeds on issuance of notes payable to AlphaCat investors	269,645	294,748
Net proceeds on issuance of preferred shares	241,686	144,852
Redemption of common shares, net	(11,961)	(7,385)

Purchases of common shares under share repurchase program	(13,996)	(129,083)
Dividends paid on preferred shares	(4,406)	—
Dividends paid on common shares	(63,286)	(59,961)
(Decrease) increase in securities lending payable	(7,265)	5,361
Third party investment in redeemable noncontrolling interests	210,200	381,250
Third party redemption of redeemable noncontrolling interests	(79,334)	(10,800)
Third party investment in noncontrolling interests	258,300	171,674
Third party distributions of noncontrolling interests	(96,125)	(127,103)
Third party subscriptions deployed in AlphaCat Funds and Sidecars	(171,952)	(411,336)
Net cash provided by financing activities	531,506	252,217
Effect of foreign currency rate changes on cash and cash equivalents	10,608	(6,968)
Net increase (decrease) in cash and cash equivalents	380,429	(154,311)
Cash and cash equivalents - beginning of period	419,976	723,109
Cash and cash equivalents - end of period	$800,405	$568,798
Supplemental disclosure of cash flow information:		
Taxes paid during the period	$568	$3,837
Interest paid during the period	$27,186	$27,552

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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Validus Holdings, Ltd.
Notes to the Consolidated Financial Statements (unaudited)
(Expressed in thousands of U.S. dollars, except share and per share information)

1. Basis of preparation and consolidation

These unaudited Consolidated Financial Statements (the "Consolidated Financial Statements") have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 in Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In addition, the year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by U.S. GAAP. This Quarterly Report on Form 10-Q should be read in conjunction with the financial statements and related notes included in Validus Holdings, Ltd.'s (the "Company") Annual Report on Form 10-K for the year ended December 31, 2016, as filed with the U.S. Securities and Exchange Commission (the "SEC").

The Company consolidates in these Consolidated Financial Statements the results of operations and financial position of all voting interest entities ("VOE") in which the Company has a controlling financial interest and all variable interest entities ("VIE") in which the Company is considered to be the primary beneficiary. The consolidation assessment, including the determination as to whether an entity qualifies as a VIE or VOE, depends on the facts and circumstances surrounding each entity.

In the opinion of management, these unaudited Consolidated Financial Statements reflect all adjustments (including normal recurring adjustments) considered necessary for a fair statement of the Company's financial position and results of operations as at the end of and for the periods presented. All significant intercompany accounts and transactions have been eliminated. The results of operations for any interim period are not necessarily indicative of the results for a full year.

The preparation of these financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. While management believes that the amounts included in the Consolidated Financial Statements reflect its best estimates and assumptions, actual results could differ materially from those estimates. The Company's principal estimates include:

- reserve for losses and loss expenses;
- premium estimates for business written on a line slip or proportional basis;
- the valuation of goodwill and intangible assets;
- reinsurance recoverable balances including the provision for uncollectible amounts; and
- investment valuation of financial assets.

The term "ASC" used in these notes refers to Accounting Standard Codification issued by the United States Financial Accounting Standards Board (the "FASB").

2. Recent accounting pronouncements

Recently issued accounting standards not yet adopted

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718)." This ASU is directed at reducing diversity in practice when applying the accounting guidance to a change in the terms or conditions of a share-based payment award. The ASU is effective for fiscal periods beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The Company has evaluated the impact of this guidance and it will not have a material impact on the Company's Consolidated Financial Statements. The Company plans to adopt this guidance on January 1, 2018.

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3. Business combination

On May 1, 2017, Western World Insurance Group, Inc. (“Western World”), a wholly owned subsidiary of the Company acquired all of the outstanding capital stock of Crop Risk Services (“CRS”) for an aggregate purchase price of $185,576 in cash. CRS is a primary crop insurance managing general agent (“MGA”) based in Decatur, Illinois with 1,170 agents across 36 states. CRS does not have insurance licenses of its own, but acts solely as an MGA in that it can produce business for any properly licensed entity on a commission basis. Concurrent with closing of the transaction, Stratford Insurance Company (“Stratford”), a wholly–owned subsidiary of Western World, was granted the required license to write crop insurance in the United States and executed several agreements to transfer the related agriculture book of business to Stratford.

The CRS acquisition was undertaken to complement the Company’s existing agricultural business and expand the Company’s presence in U.S. primary specialty lines.

For segmental reporting purposes, the results of CRS’ operations, including the related agricultural book of business have been included within the Western World segment in the Consolidated Financial Statements from the date of acquisition.

On closing, the Company recorded intangible assets totaling $63,921 for Distribution Channels, Brand Name and Technology. Distribution Channels and Brand Name were estimated to have finite useful economic lives of ten years on acquisition and are being amortized on a straight line basis over such period. Technology was estimated to have a finite useful economic life of two years on acquisition and is being amortized on a straight line basis over such a period.

The purchase price was allocated to the acquired assets and liabilities of CRS based on estimated fair values on May 1, 2017, the date the transaction closed, as detailed below. The Company recognized goodwill of $30,943 primarily attributable to CRS’s assembled workforce and synergies expected to result upon the integration of CRS and its related book of business into the Company’s operations. The estimates of fair values for tangible assets acquired and liabilities assumed were determined by management based on various market and income analyses. The Company estimated the fair values of intangible assets acquired based on variations of the income and cost approaches. Significant judgment was required to arrive at these estimates of fair value and changes to assumptions used could have led to materially different results.

The purchase of CRS was a taxable transaction and as such, goodwill and intangibles recorded at closing will be deductible for income tax purposes. The Company has recognized and recorded a deferred tax asset of $6,443 which results from the excess of tax-deductible goodwill over book goodwill as recognized in the purchase price allocation.

Validus Holdings, Ltd.
Notes to the Consolidated Financial Statements (unaudited)
(Expressed in thousands of U.S. dollars, except share and per share information)

The fair value of net assets acquired, including GAAP adjustments, are summarized as follows:

Total purchase price		$185,576
Assets acquired		
Cash and cash equivalents	$1,653	
Premiums receivable	564,453	
Prepaid reinsurance premiums	227,157	
Other assets	157,146	
Assets acquired		950,409
Liabilities acquired		
Reinsurance balances payable	$294,201	
Unearned premiums	406,649	
Net loss reserves	42,575	
Other liabilities	122,715	
Liabilities acquired		866,140
Excess purchase price		$101,307
Goodwill and other intangible assets acquired		
Intangible asset - Distribution channels	$52,898	
Intangible asset - Brand name	9,568	
Intangible asset - Technology	1,455	
Total intangible assets	63,921	
Goodwill	30,943	
Deferred tax arising on Goodwill	6,443	
Total goodwill and intangible assets		$101,307

The Company also incurred transaction expenses related to the CRS acquisition of $4,427. Transaction expenses included legal, financial advisory and audit related services.

(Expressed in thousands of U.S. dollars, except share and per share information)

The following tables reconcile the carrying amount of goodwill and intangible assets from December 31, 2016 to June 30, 2017:

	Goodwill Six Months Ended June 30, 2017		
	Talbot	Western World	Total
Balance at December 31, 2016	20,393	176,365	196,758
Additions	—	30,943	30,943
Balance at June 30, 2017	20,393	207,308	227,701

	Intangible assets Six Months Ended June 30, 2017		
	Talbot	Western World	Total
Balance at December 31, 2016	93,924	21,668	115,592
Additions	—	63,921	63,921
Amortization	(2,081)	(1,914)	(3,995)
Balance at June 30, 2017	91,843	83,675	175,518

	Intangible assets Six Months Ended June 30, 2017		
	With a Finite Life	With an Indefinite Life	Total
Balance at December 31, 2016	11,424	104,168	115,592
Additions	63,921	—	63,921
Amortization	(3,995)	—	(3,995)
Balance at June 30, 2017	71,350	104,168	175,518

Operating results of CRS have been included in the Consolidated Financial Statements from the May 1, 2017 acquisition date.

The following selected unaudited information has been provided to present a summary of the results of CRS that have been included in the Consolidated Financial Statements for the three and six months ended June 30, 2017.

	From Acquisition Date to June 30, 2017
Net premiums written	6,988
Net premiums earned	50,044
Total underwriting deductions	44,780
Underwriting income, before general and administrative expenses	5,264

Validus Holdings, Ltd.
Notes to the Consolidated Financial Statements (unaudited)
(Expressed in thousands of U.S. dollars, except share and per share information)

4. Investments
Managed investments represent assets governed by the Company’s investment policy statement (“IPS”) whereas, non-managed investments represent assets held in support of consolidated AlphaCat VIEs which are not governed by the Company’s IPS. Refer to Note 6, “Variable interest entities,” for further details.

The Company classifies its fixed maturity and short-term investments as trading and accounts for its other investments in accordance with ASC Topic 825 “Financial Instruments.” As such, all investments are carried at fair value with interest and dividend income and realized and unrealized gains and losses included in net income for the period.

The amortized cost (or cost) and fair value of the Company’s investments as at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017		December 31, 2016	
	Amortized Cost or Cost	Fair Value	Amortized Cost or Cost	Fair Value
Managed investments				
U.S. government and government agency	$649,214	$646,436	$809,392	$804,126
Non-U.S. government and government agency	293,002	292,504	245,651	240,791
U.S. states, municipalities and political subdivisions	227,047	227,949	271,742	271,830
Agency residential mortgage-backed securities	786,784	783,006	684,490	679,595
Non-agency residential mortgage-backed securities	26,745	26,683	15,858	15,477
U.S. corporate	1,378,884	1,386,484	1,540,036	1,534,508
Non-U.S. corporate	380,317	379,480	418,520	410,227
Bank loans	560,446	552,901	579,121	570,399
Asset-backed securities	500,679	502,056	528,563	526,814
Commercial mortgage-backed securities	317,732	316,190	333,740	330,932
Total fixed maturities	5,120,850	5,113,689	5,427,113	5,384,699
Short-term investments	255,289	255,516	228,574	228,386
Other investments				
Fund of hedge funds	—	—	1,457	955
Hedge funds	11,292	18,303	11,292	17,381
Private equity investments	79,871	100,391	66,383	82,627
Fixed income investment funds	266,041	268,110	247,967	249,275
Overseas deposits	57,874	57,874	50,106	50,106
Mutual funds	1,918	3,940	2,925	5,368
Total other investments	416,996	448,618	380,130	405,712
Investments in investment affiliates [a]	72,532	103,377	84,840	100,431
Total managed investments	$5,865,667	$5,921,200	$6,120,657	$6,119,228
Non-managed investments				
Catastrophe bonds	$303,712	$304,954	$157,486	$158,331
Short-term investments	2,615,837	2,615,837	2,567,784	2,567,784
Total non-managed investments	2,919,549	2,920,791	2,725,270	2,726,115
Total investments	$8,785,216	$8,841,991	$8,845,927	$8,845,343

(a) The Company’s investments in investment affiliates have been treated as equity method investments with the corresponding gains and losses recorded in income as “Income (loss) from investment affiliates.”

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Validus Holdings, Ltd.
Notes to the Consolidated Financial Statements (unaudited)
(Expressed in thousands of U.S. dollars, except share and per share information)

(a) Fixed maturity investments

The following table sets forth certain information regarding the investment ratings of the Company's fixed maturity investments as at June 30, 2017 and December 31, 2016.

	June 30, 2017			December 31, 2016		
	Fair Value	% of Total		Fair Value	% of Total	
Managed fixed maturities						
AAA	$2,318,254	42.8	%	$2,405,597	43.4	%
AA	463,060	8.5	%	538,289	9.7	%
A	1,009,366	18.6	%	1,081,949	19.5	%
BBB	703,563	13.0	%	740,861	13.4	%
Total investment grade managed fixed maturities	4,494,243	82.9	%	4,766,696	86.0	%
BB	229,023	4.2	%	213,568	3.9	%
B	176,743	3.3	%	177,737	3.2	%
CCC	11,114	0.2	%	13,371	0.2	%
NR	202,566	3.8	%	213,327	3.8	%
Total non-investment grade fixed maturities	619,446	11.5	%	618,003	11.1	%
Total managed fixed maturities	$5,113,689	94.4	%	$5,384,699	97.1	%
Non-managed fixed maturities						
BB	28,177	0.4	%	29,731	0.6	%
B	2,781	0.1	%	4,524	0.1	%
NR	273,996	5.1	%	124,076	2.2	%
Total non-managed fixed maturities	304,954	5.6	%	158,331	2.9	%
Total fixed maturities	$5,418,643	100.0	%	$5,543,030	100.0	%

(Expressed in thousands of U.S. dollars, except share and per share information)

The amortized cost and fair value amounts for the Company’s fixed maturity investments held at June 30, 2017 and December 31, 2016 are shown below by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

	June 30, 2017		December 31, 2016	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Managed fixed maturities				
Due in one year or less	$497,473	$492,256	$350,733	$346,161
Due after one year through five years	2,464,093	2,461,870	2,954,856	2,933,146
Due after five years through ten years	456,793	459,311	430,365	426,647
Due after ten years	70,551	72,317	128,508	125,927
	3,488,910	3,485,754	3,864,462	3,831,881
Asset-backed and mortgage-backed securities	1,631,940	1,627,935	1,562,651	1,552,818
Total managed fixed maturities	$5,120,850	$5,113,689	$5,427,113	$5,384,699
Non-managed catastrophe bonds				
Due in one year or less	$33,662	$32,441	$43,664	$45,418
Due after one year through five years	263,300	265,735	112,572	111,656
Due after five years through ten years	6,750	6,778	1,250	1,257
Due after ten years	—	—	—	—
Total non-managed fixed maturities	303,712	304,954	157,486	158,331
Total fixed maturities	$5,424,562	$5,418,643	$5,584,599	$5,543,030

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(b) Other investments

The following tables set forth certain information regarding the Company's other investment portfolio as at June 30, 2017 and December 31, 2016:

	June 30, 2017				
	Fair Value	Investments with redemption restrictions	Investments without redemption restrictions	Redemption frequency (a)	Redemption notice period (a)
Hedge funds	18,303	18,303	—		
Private equity investments	100,391	100,391	—		
Fixed income investment funds	268,110	237,986	30,124	Daily	Daily to 2 days
Overseas deposits	57,874	57,874	—		
Mutual funds	3,940	—	3,940	Daily	Daily
Total other investments	$448,618	$ 414,554	$ 34,064		

	December 31, 2016				
	Fair Value	Investments with redemption restrictions	Investments without redemption restrictions	Redemption frequency (a)	Redemption notice period (a)
Fund of hedge funds	$955	$ 955	$ —		
Hedge funds	17,381	17,381	—		
Private equity investments	82,627	82,627	—		
Fixed income investment funds	249,275	218,333	30,942	Daily	2 days
Overseas deposits	50,106	50,106	—		
Mutual funds	5,368	—	5,368	Daily	Daily
Total other investments	$405,712	$ 369,402	$ 36,310		

(a) The redemption frequency and notice periods only apply to investments without redemption restrictions.

Other investments include alternative investments in various funds and pooled investment schemes. These alternative investments employ various investment strategies primarily involving, but not limited to, investments in collateralized obligations, fixed income securities, private equities, distressed debt and equity securities.

Certain securities included in other investments are subject to redemption restrictions and are unable to be redeemed from the funds. Distributions from these funds will be received as the underlying investments of the funds are liquidated. Currently, it is not known to the Company when these underlying assets will be sold by their investment managers; however, it is estimated that the majority of the underlying assets of the investments would liquidate over five to ten years from inception of the funds. In addition, one of the investment funds with a fair value of $192,437 (December 31, 2016: $184,749), has a lock-up period of approximately two years as at June 30, 2017 and may also impose a redemption gate. A lock-up period refers to the initial amount of time an investor is contractually required to remain invested before having the ability to redeem. Typically, the imposition of a gate delays a portion of the requested redemption, with the remaining portion settled in cash shortly after the redemption date. The underlying investments held in the overseas deposit funds are liquid and will generally trade freely in an open market. However, the Company's ability to withdraw from the overseas deposit funds is restricted by an annual and quarterly funding and release process for Lloyd's market participants.

The Company's maximum exposure to any of these alternative investments is limited to the amount invested and any remaining capital commitments. Refer to Note 15, "Commitments and contingencies," for further details. As at June 30, 2017, the Company does not have any plans to sell any of the other investments listed above.

(Expressed in thousands of U.S. dollars, except share and per share information)

(c) Investments in investment affiliates

Included in the Company’s managed investment portfolio as at June 30, 2017 were investments in Aquiline Financial Services Fund II L.P. (“Aquiline II”), Aquiline Financial Services Fund III L.P. (“Aquiline III”) and Aquiline Technology Growth Fund L.P. (“Aquiline Tech”).

Aquiline II and III

For further information regarding Aquiline II and III please refer to Note 7(c), “Investments in investment affiliates,” included within the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. As at June 30, 2017, the Company’s total unfunded investment commitment to Aquiline II and III was $3,229 and $62,031, respectively (December 31, 2016: $2,040 and $62,031).

Aquiline Tech

On March 20, 2017, the Company entered into a Subscription Agreement (the “Subscription Agreement”) with Aquiline Technology Growth GP Ltd, (the “General Partner”) pursuant to which the Company committed and agreed to purchase limited partnership or other comparable limited liability equity interests in Aquiline Tech, a Cayman Islands exempted limited partnership, with a capital commitment in an amount equal to $20,000. The limited partnership interests are governed by the terms of an amended and restated exempted limited partnership agreement. As at June 30, 2017, the unfunded investment commitment to Aquiline Tech was $18,786.

The following table presents a reconciliation of the Company’s beginning and ending investments in investment affiliates for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Investments in investment affiliates, beginning of period	$94,697	$84,135	$100,431	$87,673
Net capital (distributions) contributions	(786)	15,732	(11,708)	16,307
Income (loss) from investment affiliates	9,466	(589)	14,654	(4,702)
Investments in investment affiliates, end of period	$103,377	$99,278	$103,377	$99,278

The following table presents the Company’s investments in investment affiliates as at June 30, 2017 and December 31, 2016:

	June 30, 2017			
	Investment at cost	Voting ownership %	Equity ownership %	Carrying value
Aquiline II	$33,349	—%	8.1 %	$52,010
Aquiline III	37,969	—%	9.0 %	50,153
Aquiline Tech	1,214	—%	16.4 %	1,214
Total investments in investment affiliates	$72,532			$103,377

	December 31, 2016			
	Investment at cost	Voting ownership %	Equity ownership %	Carrying value

Aquiline II	$46,871	—%	8.1	%	$61,999
Aquiline III	37,969	—%	9.0	%	38,432
Total investments in investment affiliates	$84,840				$100,431

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(Expressed in thousands of U.S. dollars, except share and per share information)

(d) Net investment income

Net investment income was derived from the following sources:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Managed investments				
Fixed maturities and short-term investments	$31,312	$30,621	$62,983	$58,638
Other investments	7,571	8,026	14,441	8,898
Cash and cash equivalents and restricted cash	616	380	1,226	1,245
Securities lending income	7	12	20	17
Total gross investment income	39,506	39,039	78,670	68,798
Investment expenses	(1,443)	(2,190)	(4,415)	(4,026)
Total managed net investment income	$38,063	$36,849	$74,255	$64,772
Non managed investments				
Fixed maturities and short-term investments	$4,500	$1,977	$7,560	$3,272
Restricted cash, cash and cash equivalents	1,678	431	2,640	674
Total non-managed net investment income	6,178	2,408	10,200	3,946
Total net investment income	$44,241	$39,257	$84,455	$68,718

Net investment income from other investments includes distributed and undistributed net income from hedge funds, overseas deposits and certain fixed income investment funds.

(e) Net realized and change in net unrealized gains on investments

The following table sets forth an analysis of net realized gains and the change in net unrealized gains on investments:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Managed fixed maturities, short-term and other investments				
Gross realized gains	$5,175	$3,306	$7,865	$6,523
Gross realized (losses)	(2,906)	(786)	(8,488)	(5,089)
Net realized gains (losses) on investments	2,269	2,520	(623)	1,434
Change in net unrealized gains on investments	15,942	30,052	30,291	77,130
Total net realized and change in net unrealized gains on managed investments	$18,211	$32,572	$29,668	$78,564
Non-managed fixed maturities, short-term and other investments				
Gross realized gains	$5	$204	$1,733	$715
Gross realized (losses)	—	—	—	(9)
Net realized gains on investments	5	204	1,733	706
Change in net unrealized gains (losses) on investments	379	1,376	(622)	1,742
Total net realized and change in net unrealized gains on non-managed investments	384	1,580	1,111	2,448
Total net realized and change in net unrealized gains on total investments	$18,595	$34,152	$30,779	$81,012

(f) Pledged cash and investments

As at June 30, 2017, the Company had $5,221,174 (December 31, 2016: $5,173,966) of cash and cash equivalents, restricted cash, short-term investments and fixed maturity investments that were pledged during the normal course of business. Of those, $5,156,173 were held in trust (December 31, 2016: $5,068,092). Pledged assets are generally for the benefit of the Company’s cedants and policyholders, to support AlphaCat’s fully collateralized reinsurance transactions and to facilitate the accreditation of Validus Reinsurance, Ltd., Validus Reinsurance (Switzerland) Ltd. (“Validus Re Swiss”) and Talbot as an alien Insurer/Reinsurer by certain regulators.

In addition, the Company has pledged cash and investments as collateral under the Company’s credit facilities in the total amount of $404,516 (December 31, 2016: $442,184). For further details on the credit facilities, please refer to Note 13, “Debt and financing arrangements.”

5. Fair value measurements

(a) Classification within the fair value hierarchy

Fair value is defined as the price to sell an asset or transfer a liability in an orderly transaction between market participants. Under U.S. GAAP, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The fair value hierarchy prioritizes the inputs, which refer broadly to assumptions market participants would use in pricing an asset or liability, into three levels. It gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The level in the fair value hierarchy within which a fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

The three levels of the fair value hierarchy are described below:

Level 1 - Fair values are measured based on unadjusted quoted prices in active markets for identical assets or liabilities that we have the ability to access.

Level 2 - Fair values are measured based on quoted prices in active markets for similar assets or liabilities, quoted prices for identical assets or liabilities in inactive markets, or for which significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data.

Level 3 - Fair values are measured based on inputs that are unobservable and significant to the overall fair value measurement. The unobservable inputs reflect the Company’s own judgments about assumptions where there is little, if any, market activity for that asset or liability that market participants might use.

The availability of observable inputs can vary from financial instrument to financial instrument and is affected by a wide variety of factors including, for example, the type of financial instrument, whether the financial instrument is new and not yet established in the marketplace, and other characteristics particular to the instrument. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires significantly more judgment.

Accordingly, the degree of judgment exercised by management in determining fair value is greatest for instruments categorized in Level 3. In periods of market dislocation, the observability of prices and inputs may be reduced for many instruments. This may lead the Company to change the selection of our valuation technique (for example, from market to cash flow approach) or to use multiple valuation techniques to estimate the fair value of a financial instrument. These circumstances could cause an instrument to be reclassified between levels within the fair value hierarchy.

(Expressed in thousands of U.S. dollars, except share and per share information)

At June 30, 2017, the Company’s investments were allocated between Levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Fair value based on NAV practical expedient [(a)]	Total
Managed investments					
U.S. government and government agency	$—	$646,436	$—	$ —	$646,436
Non-U.S. government and government agency	—	292,504	—	—	292,504
U.S. states, municipalities and political subdivisions	—	227,949	—	—	227,949
Agency residential mortgage-backed securities	—	783,006	—	—	783,006
Non-agency residential mortgage-backed securities	—	26,683	—	—	26,683
U.S. corporate	—	1,386,484	—	—	1,386,484
Non-U.S. corporate	—	379,480	—	—	379,480
Bank loans	—	328,729	224,172	—	552,901
Asset-backed securities	—	466,135	35,921	—	502,056
Commercial mortgage-backed securities	—	316,190	—	—	316,190
Total fixed maturities	—	4,853,596	260,093	—	5,113,689
Short-term investments	248,439	7,077	—	—	255,516
Other investments					
Hedge funds	—	—	—	18,303	18,303
Private equity investments	—	—	—	100,391	100,391
Fixed income investment funds	—	30,137	16,400	221,573	268,110
Overseas deposits	—	—	—	57,874	57,874
Mutual funds	—	3,940	—	—	3,940
Total other investments	—	34,077	16,400	398,141	448,618
Investments in investment affiliates [(b)]	—	—	—	—	103,377
Total managed investments	$248,439	$4,894,750	$276,493	$ 398,141	$5,921,200
Non-managed investments					
Catastrophe bonds	$—	$236,929	$68,025	$ —	$304,954
Short-term investments	2,615,837	—	—	—	2,615,837
Total non-managed investments	2,615,837	236,929	68,025	—	2,920,791
Total investments	$2,864,276	$5,131,679	$344,518	$ 398,141	$8,841,991

(a) In accordance with ASC Topic 820 “Fair Value Measurements,” investments measured at fair value using the net asset value (“NAV”) per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

(b) In accordance with ASC Topic 825 “Financial Instruments,” the Company’s investments in investment affiliates have not been classified in the fair value hierarchy.

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At December 31, 2016, the Company’s investments were allocated between Levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Fair value based on NAV practical expedient (a)	Total
Managed investments					
U.S. government and government agency	$—	$804,126	$—	$—	$804,126
Non-U.S. government and government agency	—	240,791	—	—	240,791
U.S. states, municipalities and political subdivisions	—	271,830	—	—	271,830
Agency residential mortgage-backed securities	—	679,595	—	—	679,595
Non-agency residential mortgage-backed securities	—	15,477	—	—	15,477
U.S. corporate	—	1,534,508	—	—	1,534,508
Non-U.S. corporate	—	410,227	—	—	410,227
Bank loans	—	323,903	246,496	—	570,399
Asset-backed securities	—	502,883	23,931	—	526,814
Commercial mortgage-backed securities	—	330,932	—	—	330,932
Total fixed maturities	—	5,114,272	270,427	—	5,384,699
Short-term investments	209,651	18,735	—	—	228,386
Other investments					
Fund of hedge funds	—	—	—	955	955
Hedge funds	—	—	—	17,381	17,381
Private equity investments	—	—	—	82,627	82,627
Fixed income investment funds	—	30,941	12,168	206,166	249,275
Overseas deposits	—	—	—	50,106	50,106
Mutual funds	—	5,368	—	—	5,368
Total other investments	—	36,309	12,168	357,235	405,712
Investments in investment affiliates (b)	—	—	—	—	100,431
Total managed investments	$209,651	$5,169,316	$282,595	$357,235	$6,119,228
Non-managed investments					
Catastrophe bonds	$—	$109,956	$48,375	$—	$158,331
Short-term investments	2,567,784	—	—	—	2,567,784
Total non-managed investments	2,567,784	109,956	48,375	—	2,726,115
Total investments	$2,777,435	$5,279,272	$330,970	$357,235	$8,845,343

(a) In accordance with ASC Topic 820 “Fair Value Measurements,” investments measured at fair value using the net asset value (“NAV”) per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

(b) In accordance with ASC Topic 825 “Financial Instruments,” the Company’s investments in investment affiliates have not been classified in the fair value hierarchy.

At June 30, 2017, managed Level 3 investments totaled $276,493 (December 31, 2016: $282,595), representing 4.7% (December 31, 2016: 4.6%) of total managed investments.

(b) Valuation techniques

There have been no material changes in the Company’s valuation techniques during the period, or periods, represented by these Consolidated Financial Statements. The following methods and assumptions were used in estimating the fair value of each class of financial instrument recorded in the Consolidated Balance Sheets.

Fixed maturity investments

In general, valuation of the Company's fixed maturity investment portfolio is provided by pricing services, such as index providers and pricing vendors, as well as broker quotations. The pricing vendors provide valuations for a high volume of liquid securities that are actively traded. For securities that do not trade on an exchange, the pricing services generally utilize market data and other observable inputs in matrix pricing models to determine month end prices. Prices are generally verified using third party data. Securities which are priced by an index provider are generally included in the index.

In general, broker-dealers value securities through their trading desks based on observable inputs. The methodologies include mapping securities based on trade data, bids or offers, observed spreads, and performance on newly issued securities. Broker-dealers also determine valuations by observing secondary trading of similar securities. Prices obtained from broker quotations are considered non-binding, however they are based on observable inputs and by observing secondary trading of similar securities obtained from active, non-distressed markets. The Company considers these Level 2 inputs as they are corroborated with other market observable inputs. The techniques generally used to determine the fair value of the Company's fixed maturity investments are detailed below by asset class.

U.S. government and government agency

U.S. government and government agency securities consist primarily of debt securities issued by the U.S. Treasury and mortgage pass-through agencies such as the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and the Government National Mortgage Association. Fixed maturity investments included in U.S. government and government agency securities are primarily priced by pricing services. When evaluating these securities, the pricing services gather information from market sources and integrate other observations from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trade volumes, when available. The fair value of each security is individually computed using analytical models which incorporate option adjusted spreads and other daily interest rate data. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Non-U.S. government and government agency

Non-U.S. government and government agency securities consist of debt securities issued by non-U.S. governments and their agencies along with supranational organizations (also known as sovereign debt securities). Securities held in these sectors are primarily priced by pricing services who employ proprietary discounted cash flow models to value the securities. Key quantitative inputs for these models are daily observed benchmark curves for treasury, swap and high issuance credits. The pricing services then apply a credit spread for each security which is developed by in-depth and real time market analysis. For securities in which trade volume is low, the pricing services utilize data from more frequently traded securities with similar attributes. These models may also be supplemented by daily market and credit research for international markets. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

U.S. states, municipalities and political subdivisions

The Company's U.S. states, municipalities and political subdivisions portfolio contains debt securities issued by U.S. domiciled state and municipal entities. These securities are generally priced by independent pricing services using the techniques described for U.S. government and government agency securities described above. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Agency residential mortgage-backed securities

The Company's agency residential mortgage-backed investments are primarily priced by pricing services using a mortgage pool specific model which utilizes daily inputs from the active to be announced ("TBA") market which is very liquid, as well as the U.S. treasury market. The model also utilizes additional information, such as the weighted average maturity, weighted average coupon and other available pool level data which is provided by the sponsoring agency. Valuations are also corroborated with daily active market quotes. As the significant inputs used to price these

securities are observable, the fair value of these investments are classified as Level 2.
Non-agency residential mortgage-backed securities
The Company’s non-agency mortgage-backed investments include non-agency prime residential mortgage-backed fixed maturity investments. The Company has no fixed maturity investments classified as sub-prime held in its fixed maturity investments portfolio. Securities held in these sectors are primarily priced by pricing services using an option adjusted spread model or other

relevant models, which principally utilize inputs including benchmark yields, available trade information or broker quotes, and issuer spreads. The pricing services also review collateral prepayment speeds, loss severity and delinquencies among other collateral performance indicators for the securities valuation, when applicable. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

U.S. corporate

Corporate debt securities consist primarily of investment-grade debt of a wide variety of U.S. corporate issuers and industries. The Company's corporate fixed maturity investments are primarily priced by pricing services. When evaluating these securities, the pricing services gather information from market sources regarding the issuer of the security and obtain credit data, as well as other observations, from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trade volumes, when available. The pricing services also consider the specific terms and conditions of the securities, including any specific features which may influence risk. In certain instances, securities are individually evaluated using a spread which is added to the U.S. treasury curve or a security specific swap curve as appropriate. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Non-U.S. corporate

Non-U.S. corporate debt securities consist primarily of investment-grade debt of a wide variety of non-U.S. corporate issuers and industries. The Company's non-U.S. corporate fixed maturity investments are primarily priced by pricing services. When evaluating these securities, the pricing services gather information from market sources regarding the issuer of the security and obtain credit data, as well as other observations, from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trade volumes, when available. The pricing services also consider the specific terms and conditions of the securities, including any specific features which may influence risk. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Bank loans

The Company's bank loan investments consist primarily of below-investment-grade debt of a wide variety of corporate issuers and industries. The Company's bank loans are primarily priced by pricing services. When evaluating these securities, the pricing services gather information from market sources regarding the issuer of the security and obtain credit data, as well as other observations, from markets and sector news. Evaluations are updated by obtaining broker dealer quotes and other market information including actual trade volumes, when available. The pricing services also consider the specific terms and conditions of the securities, including any specific features which may influence risk. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Also, included in the bank loan portfolio is a collection of loan participations held through an intermediary. A third party pricing service provides monthly valuation reports for each loan and participation using a combination of quotations from loan pricing services, leveraged loan indices or market price quotes obtained directly from the intermediary. Significant unobservable inputs used to price these securities include credit spreads and default rates; therefore, the fair value of these investments are classified as Level 3.

Asset-backed securities

Asset backed securities include mostly investment-grade debt securities backed by pools of loans with a variety of underlying collateral, including automobile loan receivables, student loans, credit card receivables, and collateralized loan obligations originated by a variety of financial institutions. Securities held in these sectors are primarily priced by pricing services. The pricing services apply dealer quotes and other available trade information such as bids and offers, prepayment speeds which may be adjusted for the underlying collateral or current price data, the U.S. treasury curve and swap curve as well as cash settlement. The pricing services determine the expected cash flows for each security held in this sector using historical prepayment and default projections for the underlying collateral and current market data. In addition, a spread is applied to the relevant benchmark and used to discount the cash flows noted above to determine the fair value of the securities held in this sector. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2. Where pricing is unavailable from pricing services, we obtain non-binding quotes from broker-dealers. This is generally the case when there is a low volume of trading activity and current transactions are not orderly. Broker-dealer quotes for which significant observable inputs are unable to be corroborated with market observable information are classified as Level 3.

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Commercial mortgage-backed securities

Commercial mortgage backed securities are investment-grade debt primarily priced by pricing services. The pricing services apply dealer quotes and other available trade information such as bids and offers, prepayment speeds which may be adjusted for the underlying collateral or current price data, the U.S. treasury curve and swap curve as well as cash settlement. The pricing services determine the expected cash flows for each security held in this sector using historical prepayment and default projections for the underlying collateral and current market data. In addition, a spread is applied to the relevant benchmark and used to discount the cash flows noted above to determine the fair value of the securities held in this sector. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2.

Catastrophe bonds

Catastrophe bonds are priced based on broker or underwriter bid indications. As the significant inputs used to price these securities are observable, the fair value of these investments are classified as Level 2. To the extent that these indications are based on significant unobservable inputs, the fair value of the relevant bonds will be classified as a Level 3.

Short-term investments

Short-term investments consist primarily of highly liquid securities, all with maturities of less than one year from the date of purchase. The fair value of the portfolio is generally determined using amortized cost which approximates fair value. As the highly liquid money market-type funds are actively traded, the fair value of these investments are classified as Level 1. To the extent that the remaining securities are not actively traded due to their approaching maturity, the fair value of these investments are classified as Level 2.

Other investments

Fund of hedge funds

During the three months ended June 30, 2017, the Company's investment in a fund of hedge funds was liquidated. Prior to liquidation, the fund's administrator provided a monthly reported NAV with a three month delay in its valuation. The fund manager provided an estimate of the fund NAV at year end based on the estimated performance provided from the underlying funds. To determine the reasonableness of the estimated NAV, the Company compared the fund administrator's NAV to the fund manager's estimated NAV that incorporates relevant valuation sources. Prior to liquidation, the fair value of these investments were measured using the NAV practical expedient and therefore were not categorized within the fair value hierarchy.

Hedge funds

The hedge fund investment was assumed by the Company in the acquisition of Flagstone Reinsurance Holdings, S.A. ("Flagstone") (the "Flagstone hedge fund"). The Flagstone hedge fund's administrator provides quarterly NAVs with a three month delay in valuation. The fair value of this investment is measured using the NAV practical expedient and therefore has not been categorized within the fair value hierarchy.

Private equity investments

The private equity funds provide quarterly or semi-annual partnership capital statements with a three or six month delay which are used as a basis for valuation. These private equity investments vary in investment strategies and are not actively traded in any open markets. The fair value of these investments are measured using the NAV practical expedient and therefore have not been categorized within the fair value hierarchy.

Fixed income investment funds

The Company's investment funds classified as Level 2 consist of a pooled investment fund. The pooled investment is invested in fixed income securities with high credit ratings and is only open to Lloyd's Trust Fund participants. The fair value of units in the investment fund is based on the NAV of the fund and is traded on a daily basis.

Included in investment funds is a residual equity tranche of a structured credit fund valued using a dynamic yield that calculates an income accrual based on an underlying valuation model with a typical cash flow waterfall structure.

Significant unobservable inputs used to price this fund include default rates and prepayment rates; therefore, the fair value of the investment fund is classified as Level 3.

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The fair value of the Company’s remaining investment funds is based on the NAV of the fund as reported by the independent fund administrator. The fund’s administrators provide a monthly reported NAV with a one or three month delay in their valuation. The fair value of these investments are measured using the NAV practical expedient and therefore have not been categorized within the fair value hierarchy.

Overseas deposits

The Company’s share of a portfolio of Lloyd’s overseas deposits are managed centrally by Lloyd’s and invested according to local regulatory requirements. The composition of the portfolio varies and the deposits are made across the market. The fair value of the deposits is based on the portfolio level reporting that is provided by Lloyd’s. The fair value of these investments are measured using the NAV practical expedient and therefore have not been categorized within the fair value hierarchy.

Mutual funds

Mutual funds consist of an investment fund which invests in various quoted investments. The fair value of units in the mutual fund is based on the NAV of the fund as reported by the fund manager. The mutual fund has daily liquidity which allows us to redeem our holdings at the applicable NAV in the near term. As such, the Company has classified this investment as Level 2.

(c) Level 3 investments

The following table presents a reconciliation of the beginning and ending balances for all investments measured at fair value on a recurring basis using Level 3 inputs during the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30, 2017				
	Bank Loans	Catastrophe Bonds	Fixed Income Investment Funds	Asset Backed Securities	Total
Level 3 investments, beginning of period	$236,694	$ 72,676	$ 12,560	$ 23,882	$345,812
Purchases	16,757	5,000	3,432	11,053	36,242
Sales	—	—	—	(53)	(53)
Settlements	(28,893)	(10,216)	408	—	(38,701)
Net realized gains	—	216	—	—	216
Change in net unrealized (losses) gains	(386)	349	—	49	12
Amortization	—	—	—	990	990
Level 3 investments, end of period	$224,172	$ 68,025	$ 16,400	$ 35,921	$344,518

	Three Months Ended June 30, 2016			
	Bank Loans	Catastrophe Bonds	Asset Backed Securities	Total
Level 3 investments, beginning of period	$255,011	$ 37,105	$ —	$292,116
Purchases	8,885	—	12,383	21,268
Settlements	(17,784)	—	—	(17,784)
Change in net unrealized (losses) gains	(2,964)	413	—	(2,551)
Level 3 investments, end of period	$243,148	$ 37,518	$ 12,383	$293,049

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	Six Months Ended June 30, 2017				
	Bank Loans	Catastrophe Bonds	Fixed Income Investment Funds	Asset Backed Securities	Total
Level 3 investments—beginning of period	$246,496	$ 48,375	$ 12,168	$23,931	$330,970
Purchases	39,933	66,091	3,432	11,053	120,509
Sales	—	—	—	(53)	(53)
Settlements	(62,003)	(48,996)	800	—	(110,199)
Net realized gains	—	3,350	—	—	3,350
Change in net unrealized (losses)	(254)	(795)	—	—	(1,049)
Amortization	—	—	—	990	990
Level 3 investments—end of period	$224,172	$ 68,025	$ 16,400	$35,921	$344,518

	Six Months Ended June 30, 2016			
	Bank Loans	Catastrophe Bonds	Asset Backed Securities	Total
Level 3 investments—beginning of period	$232,337	$ 13,500	$ —	$245,837
Purchases	50,988	23,272	12,383	86,643
Sales	(2,389)	—	—	(2,389)
Settlements	(34,033)	(125)	—	(34,158)
Change in net unrealized (losses) gains	(3,755)	871	—	(2,884)
Level 3 investments—end of period	$243,148	$ 37,518	$ 12,383	$293,049

There have not been any transfers into or out of Level 3 during the three and six months ended June 30, 2017 or 2016.

(d) Financial instruments not carried at fair value

ASC Topic 825 “Financial Instruments” is also applicable to disclosures of financial instruments not carried at fair value, except for certain financial instruments, including insurance contracts and investments in affiliates. The carrying values of cash and cash equivalents, restricted cash, accrued investment income, other assets, net payable for investments purchased and accounts payable and accrued expenses approximated their fair values at June 30, 2017, due to their respective short maturities. As these financial instruments are not actively traded, their respective fair values are classified within Level 2.

6. Variable interest entities

The Company consolidates all VOEs in which it has a controlling financial interest and all VIEs in which it is considered to be the primary beneficiary. The Company’s VIEs are primarily entities in the AlphaCat segment.

(a) Consolidated VIEs

AlphaCat sidecars

Beginning on May 25, 2011, the Company joined with other investors in capitalizing a series of sidecars for the purpose of investing in collateralized reinsurance and retrocessional contracts. Certain of these sidecars deployed their capital through transactions entered into by AlphaCat Reinsurance Ltd. (“AlphaCat Re”). Each of these entities return capital once the risk period expires and all losses have been paid out. The AlphaCat sidecars are VIEs and are consolidated by the Company as the primary beneficiary. The Company’s maximum exposure to any of the sidecars is the amount of capital invested at any given time.

AlphaCat ILS funds

The AlphaCat ILS funds received third party subscriptions beginning on December 17, 2012. The Company and third party investors invest in the AlphaCat ILS funds for the purpose of investing in instruments with returns linked to property catastrophe reinsurance, retrocession and ILS contracts. The AlphaCat ILS funds have varying risk profiles and are categorized by the expected loss of the fund. Expected loss represents the average annual loss over the set of simulation scenarios divided by the total limit. Lower risk ILS funds are defined as having a maximum permitted portfolio expected loss of less than 7%, whereas higher risk ILS funds have a maximum permitted portfolio expected loss of greater than 7%. The AlphaCat ILS funds primarily deploy their capital through transactions entered into by AlphaCat Re and AlphaCat Master Fund Ltd. ("AlphaCat Master Fund"). All of the AlphaCat ILS funds are VIEs and were consolidated by the Company as the primary beneficiary through May 31, 2017. However, on June 1, 2017, the Company redeemed its investment in one of the lower risk AlphaCat ILS funds. As a result, the Company was no longer deemed to be the primary beneficiary and therefore this fund was deconsolidated effective June 1, 2017. The deconsolidation resulted in a loss of $402 which is included in the Consolidated Statements of Comprehensive Income as other insurance related income for the three and six months ended June 30, 2017. The Company's maximum exposure to any of the funds is the amount of capital invested at any given time and any remaining capital commitments. Refer to Note 15, "Commitments and contingencies," for further details.

AlphaCat Re and AlphaCat Master Fund

The Company utilizes AlphaCat Re and AlphaCat Master Fund (collectively the "master funds"), both market facing entities, for the purpose of writing collateralized reinsurance and investing in capital markets products, respectively, on behalf of certain entities within the AlphaCat segment and direct third party investors. AlphaCat Re enters into transactions on behalf of the AlphaCat sidecars and ILS funds (collectively the "feeder funds") and direct third party investors, whereas AlphaCat Master Fund only enters into transactions on behalf of certain AlphaCat ILS funds. All of the risks and rewards of the underlying transactions are allocated to the feeder funds and direct third party investors using variable funding notes. The master funds are VIEs and are consolidated by the Company as the primary beneficiary.

Notes Payable to AlphaCat Investors

The master funds issue variable funding notes to the feeder funds, and direct to third party investors, in order to write collateralized reinsurance and invest in capital markets products on their behalf. The Company's investments in the feeder funds, together with investments made by third parties in the feeder funds and on a direct basis, are provided as consideration for the notes to the master funds. The duration of the underlying collateralized reinsurance contracts and capital market products is typically twelve months; however, the variable funding notes do not have a stated maturity date or principal amount since repayment is dependent on the settlement and income or loss of the underlying transactions. Therefore, the notes are subsequently redeemed as the underlying transactions are settled. The income or loss generated by the underlying transactions is then transferred to the feeder funds and direct third party investors via the variable funding notes.

Any notes issued by the master funds to the consolidated feeder funds are eliminated on consolidation and only variable funding notes issued by AlphaCat Re to direct third party investors and non-consolidated feeder funds remain on the Consolidated Balance Sheets as notes payable to AlphaCat investors with the related income or loss included in the Consolidated Statements of Income and Comprehensive Income as (income) attributable to AlphaCat investors. To the extent that the income has not been returned to the investors, it is included in accounts payable and accrued expenses in the Consolidated Balance Sheets.

During 2017 and 2016, one of the AlphaCat ILS funds (the "Fund") issued both common shares and structured notes to the Company and other third party investors in order to capitalize the fund. The Fund deploys its capital through AlphaCat Re; therefore, the structured notes do not have a stated maturity date or principal amount since repayment is dependent on the settlement and income or loss of the variable funding notes with AlphaCat Re. The structured notes rank senior to the common shares of the Fund and earn an interest rate of 7% (2016: 8%) per annum, payable on a cumulative basis in arrears.

As the Fund is consolidated by the Company, the structured notes issued to the Company are eliminated on consolidation and only the structured notes issued to third party investors remain on the Consolidated Balance Sheets as notes payable to AlphaCat investors with any related interest included in the Consolidated Statements of Income and Comprehensive Income as (income) attributable to AlphaCat investors. To the extent that the accrued interest on the structured notes has not been returned to the investors, it is included in accounts payable and accrued expenses in the Consolidated Balance Sheets.

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The following tables present a reconciliation of the beginning and ending notes payable to AlphaCat investors for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30, 2017		
	Variable Funding Notes	Structured Notes	Total
Notes payable to AlphaCat investors, beginning of period	$343,256	$103,320	$446,576
Notes payable to AlphaCat investors recognized on deconsolidation of AlphaCat ILS fund	423,269	—	423,269
Issuance of notes payable to AlphaCat investors	267,867	68,880	336,747
Redemption of notes payable to AlphaCat investors	(140,150)	—	(140,150)
Foreign exchange gains	(283)	—	(283)
Notes payable to AlphaCat investors, end of period	$893,959	$172,200	$1,066,159

	Three Months Ended June 30, 2016		
	Variable Funding Notes	Structured Notes	Total
Notes payable to AlphaCat investors, beginning of period	$261,793	$61,717	$323,510
Issuance of notes payable to AlphaCat investors	102,817	32,609	135,426
Redemption of notes payable to AlphaCat investors	(88,079)	—	(88,079)
Foreign exchange losses	125	—	125
Notes payable to AlphaCat investors, end of period	$276,656	$94,326	$370,982

	Six Months Ended June 30, 2017		
	Variable Funding Notes	Structured Notes	Total
Notes payable to AlphaCat investors, beginning of period	$278,202	$—	$278,202
Notes payable to AlphaCat investors recognized on deconsolidation of AlphaCat ILS fund	423,269	—	423,269
Issuance of notes payable to AlphaCat investors	541,877	172,200	714,077
Redemption of notes payable to AlphaCat investors	(349,106)	—	(349,106)
Foreign exchange gains	(283)	—	(283)
Notes payable to AlphaCat investors, end of period	$893,959	$172,200	$1,066,159

	Six Months Ended June 30, 2016		
	Variable Funding Notes	Structured Notes	Total
Notes payable to AlphaCat investors, beginning of period	$75,493	$—	$75,493
Issuance of notes payable to AlphaCat investors	298,105	94,326	392,431
Redemption of notes payable to AlphaCat investors	(97,684)	—	(97,684)
Foreign exchange losses	742	—	742
Notes payable to AlphaCat investors, end of period	$276,656	$94,326	$370,982

As at December 31, 2016, $1,000 of the structured notes redeemed during the year were payable to AlphaCat investors and included in accounts payable and accrued expenses.

The income attributable to AlphaCat investors for the three and six months ended June 30, 2017 was $11,830 and $19,333 (2016: $6,114 and $10,714), with $63,352 included in accounts payable and accrued expenses as at June 30, 2017 (December 31, 2016: $17,068).

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BetaCat ILS funds

The BetaCat ILS funds invest exclusively in catastrophe bonds (principal-at-risk variable rate notes and other event-linked securities, being referred to collectively as “Cat Bonds”) focused on property and casualty risk and issued under Rule 144A of the Securities Act of 1933, as amended, following a passive buy-and-hold investment strategy. Two of the funds are VIEs, one of which is consolidated by the Company as the primary beneficiary. The remaining fund is a VOE and is consolidated by the Company as it owns all of the voting equity interests. The Company’s maximum exposure to any of the funds is the amount of capital invested at any given time.
The following table presents the total assets and total liabilities of the Company’s consolidated VIEs, excluding intercompany eliminations, as at June 30, 2017 and December 31, 2016:

	June 30, 2017		December 31, 2016	
	Total Assets	Total Liabilities	Total Assets	Total Liabilities
AlphaCat sidecars	$29,330	$ 3,455	$40,041	$ 3,206
AlphaCat ILS funds - Lower Risk [(a)]	951,428 951,428	13,371	1,498,276	42,457
AlphaCat ILS funds - Higher Risk [(a)]	1,037,568	207,300	972,633	381,332
AlphaCat Re and AlphaCat Master Fund	2,828,096	2,827,926	2,510,415	2,510,245
BetaCat ILS funds	146,098	278	82,471	30,663

(a) Lower risk AlphaCat ILS funds have a maximum permitted portfolio expected loss of less than 7%, whereas higher risk AlphaCat ILS funds have a maximum permitted portfolio expected loss of greater than 7%. Expected loss represents the average annual loss over the set of simulation scenarios divided by the total limit.

Assets of consolidated VIEs can only be used to settle obligations and liabilities of the consolidated VIEs and do not have recourse to the general credit of the Company. Investments held by these entities are presented separately in Note 4, “Investments,” as non-managed investments.

(b) Non-Consolidated VIEs

The Company invests in private equity and other investment vehicles as part of the Company’s investment portfolio. The activities of these VIEs are generally limited to holding investments and the Company’s involvement in these entities is passive in nature. The Company’s maximum exposure to the VIEs is the amount of capital invested at any given time, and the Company does not have the power to direct the activities which most significantly impact the VIEs economic performance. The Company is therefore not the primary beneficiary of these VIEs.

7. Noncontrolling interests

Investors in certain of the AlphaCat and BetaCat ILS funds have rights that enable them, subject to certain limitations, to redeem their shares. The third party equity is therefore recorded in the Company’s Consolidated Balance Sheets as redeemable noncontrolling interests. When and if a redemption notice is received, the fair value of the redemption is reclassified to a liability.
The AlphaCat sidecars and one of the AlphaCat ILS funds have no shareholder redemption rights. Therefore, the third party equity is recorded in the Company’s Consolidated Balance Sheets as noncontrolling interests.

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The following tables present a reconciliation of the beginning and ending balances of redeemable noncontrolling interests and noncontrolling interests for the three and six months ended June 30, 2017 and 2016:

	Redeemable noncontrolling interests		Noncontrolling interests		Total	
	Three Months Ended June 30,		Three Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016	2017	2016
Balance, beginning of period	$1,657,630	$1,409,037	$330,597	$157,223	$1,988,227	$1,566,260
Issuance of shares	106,501	112,500	103,320	59,349	209,821	171,849
Adjustment to noncontrolling interests as a result of deconsolidation	(459,021)	—	—	—	(459,021)	—
Income attributable to noncontrolling interests	28,555	17,230	15,095	3,963	43,650	21,193
Redemption of shares / distributions	(82,005)	(6,484)	(33,354)	(8,381)	(115,359)	(14,865)
Balance, end of period	$1,251,660	$1,532,283	$415,658	$212,154	$1,667,318	$1,744,437

	Redeemable noncontrolling interests		Noncontrolling interests		Total	
	Six Months Ended June 30,		Six Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016	2017	2016
Balance, beginning of period	$1,528,001	$1,111,714	$165,977	$154,662	$1,693,978	$1,266,376
Issuance of shares	210,200	381,250	258,300	171,674	468,500	552,924
Adjustment to noncontrolling interests as a result of deconsolidation	(459,021)	—	—	—	(459,021)	—
Income attributable to noncontrolling interests	54,485	45,803	31,737	12,921	86,222	58,724
Redemption of shares / distributions	(82,005)	(6,484)	(40,356)	(127,103)	(122,361)	(133,587)
Balance, end of period	$1,251,660	$1,532,283	$415,658	$212,154	$1,667,318	$1,744,437

As at June 30, 2017, redemptions of $74,200 and distributions of $nil (December 31, 2016: $71,530 and $16,144) were payable to redeemable noncontrolling interests and noncontrolling interests, respectively. These amounts are classified within accounts payable and accrued expenses on the Company’s Consolidated Balance Sheets.

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8. Derivative instruments

The Company enters into derivative instruments for risk management purposes, specifically to hedge unmatched foreign currency exposures, interest rate exposures and to shorten the duration of the Company's fixed maturities portfolio.

(a) Derivatives not designated as hedging instruments

The following table summarizes information on the classification and amount of the fair value of derivatives not designated as hedging instruments for accounting purposes within the Company's Consolidated Balance Sheets as at June 30, 2017 and December 31, 2016:

Derivatives not designated as hedging instruments	June 30, 2017 Notional Exposure	June 30, 2017 Asset Derivative at Fair Value [(a)]	June 30, 2017 Liability Derivative at Fair Value [(a)]	December 31, 2016 Notional Exposure	December 31, 2016 Asset Derivative at Fair Value [(a)]	December 31, 2016 Liability Derivative at Fair Value [(a)]
Foreign currency forward contracts	$223,018	$ 1,972	$ 6,325	$181,375	$ 2,351	$ 3,421
Interest rate swap contracts	$150,000	$ 330	$ 648	$—	$ —	$ —

(a) Asset and liability derivatives are classified within other assets and accounts payable and accrued expenses, respectively, within the Company's consolidated balance sheets.

The following table summarizes information on the classification and net impact on earnings, recognized in the Company's Consolidated Statements of Income and Comprehensive Income relating to the foreign currency forward and interest rate swap contracts that were not designated as hedging instruments for accounting purposes during the three and six months ended June 30, 2017 and 2016:

Derivatives not designated as hedging instruments	Classification of (losses) gains recognized in earnings	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Foreign currency forward contracts	Foreign exchange (losses) gains	$(6,525)	$896	$(6,072)	$(1,117)
Foreign currency forward contracts	Other (loss) income	$(874)	$84	$(979)	$120
Interest rate swap contracts	Change in unrealized losses on investments	$(319)	$—	$(319)	$—

(b) Derivatives designated as hedging instruments

The following table summarizes information on the classification and amount of the fair value of derivatives designated as hedging instruments for accounting purposes on the Consolidated Balance Sheets as at June 30, 2017 and December 31, 2016:

Derivatives designated as hedging instruments	June 30, 2017 Notional Exposure	June 30, 2017 Asset Derivative at Fair Value [(a)]	June 30, 2017 Liability Derivative at Fair Value [(a)]	December 31, 2016 Notional Exposure	December 31, 2016 Asset Derivative at Fair Value [(a)]	December 31, 2016 Liability Derivative at Fair Value [(a)]
Interest rate swap contracts	$552,263	$ 20	$ 1,409	$552,263	$ 20	$ 1,479

(a) Asset and liability derivatives are classified within other assets and accounts payable and accrued expenses, respectively, within the Company's consolidated balance sheets.

Derivative instruments designated as a cash flow hedge

The Company designates its interest rate derivative instruments as cash flow hedges for accounting purposes and formally and contemporaneously documents all relationships between the hedging instruments and hedged items and links the derivative instruments to specific assets and liabilities. The Company assesses the effectiveness of the hedges, both at inception and on an on-going basis and determines whether the hedges are highly effective in offsetting changes in fair value of the linked hedged items. The Company currently applies the long haul method when assessing the hedge's effectiveness.

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The following table provides the total impact on other comprehensive income (loss) and earnings relating to the derivative instruments formally designated as cash flow hedges along with the impact of the related hedged items for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
Interest rate swap contracts	2017	2016	2017	2016
Amount of effective portion recognized in other comprehensive income	$2,217	$2,694	$4,376	$6,350
Amount of effective portion subsequently reclassified to earnings	$(2,073)	$(2,758)	$(4,330)	$(5,656)
Amount of ineffective portion excluded from effectiveness testing	$(144)	$64	$(46)	$(694)

The above balances relate to interest payments and have therefore been classified as finance expenses in the Consolidated Statements of Income and Comprehensive Income.

(c) Classification within the fair value hierarchy

As described in Note 5, “Fair value measurements,” under U.S. GAAP, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The assumptions used within the valuation of the Company’s derivative instruments are observable in the marketplace, can be derived from observable data or are supported by observable levels at which other similar transactions are executed in the marketplace. Accordingly, these derivatives were classified within Level 2 of the fair value hierarchy.

(d) Balance sheet offsetting

There was no balance sheet offsetting activity as at June 30, 2017 or December 31, 2016.

The Company currently provides cash collateral as security for interest rate swap contracts. The Company does not provide cash collateral or financial instruments as security for foreign currency forward contracts. Our derivative instruments are generally traded under International Swaps and Derivatives Association master netting agreements, which establish terms that apply to all transactions. On a periodic basis, the amounts receivable from or payable to the counterparties are settled in cash.

The Company has not elected to settle multiple transactions with an individual counterparty on a net basis.

9. Reserve for losses and loss expenses

Reserves for losses and loss expenses are based in part upon the estimation of case reserves from broker, insured and ceding company reported data. The Company also uses statistical and actuarial methods to estimate ultimate expected losses and loss expenses, from which incurred but not reported losses (“IBNR”) can be calculated. The period of time from the occurrence of a loss to the reporting of a loss to the Company and to the settlement of the Company’s liability may be several months or years. During this period, additional facts and trends may be revealed. As these factors become apparent, reserves will be adjusted, sometimes requiring an increase or decrease in the overall reserves of the Company, and at other times requiring a reallocation of incurred but not reported reserves to specific case reserves. These estimates are reviewed and adjusted regularly, and such adjustments, if any, are reflected in earnings in the period in which they become known. While management believes that it has made a reasonable estimate of ultimate losses, there can be no assurances that ultimate losses and loss expenses will not exceed this estimate.

The following table summarizes the total reserve for losses and loss expenses as at June 30, 2017 and December 31, 2016:

	June 30, 2017	December 31, 2016
Case reserves	$1,236,799	$ 1,237,772
IBNR	2,068,392	1,757,423
Total reserve for losses and loss expenses	$3,305,191	$ 2,995,195

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The following table represents an analysis of paid and unpaid losses and loss expenses incurred and a reconciliation of the beginning and ending unpaid losses and loss expenses for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Reserve for losses and loss expenses, beginning of period	$3,052,745	$2,980,300	$2,995,195	$2,996,567
Loss reserves recoverable	(451,856)	(370,689)	(430,421)	(350,586)
Net reserves for losses and loss expenses, beginning of period	2,600,889	2,609,611	2,564,774	2,645,981
Net reserves acquired [(a)]	23,753	—	23,753	—
Increase (decrease) in net reserves for losses and loss expenses in respect of losses occurring in:				
Current year	339,439	369,911	670,255	648,097
Prior years	(43,290)	(62,781)	(104,521)	(116,520)
Total net incurred losses and loss expenses	296,149	307,130	565,734	531,577
Less net losses and loss expenses paid in respect of losses occurring in:				
Current year	(42,758)	(45,882)	(50,456)	(61,655)
Prior years	(193,265)	(176,775)	(431,354)	(430,079)
Total net paid losses	(236,023)	(222,657)	(481,810)	(491,734)
Foreign exchange losses (gains)	20,216	(14,354)	32,533	(6,094)
Net reserve for losses and loss expenses, end of period	2,704,984	2,679,730	2,704,984	2,679,730
Loss reserves recoverable	600,207	442,987	600,207	442,987
Reserve for losses and loss expenses, end of period	$3,305,191	$3,122,717	$3,305,191	$3,122,717

(a) Equals net reserves acquired of $42,575 less net reserves commuted at closing of $18,822.

Incurred losses and loss expenses comprise:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Gross losses and loss expenses	$415,013	$397,863	$761,808	$667,716
Reinsurance recoverable	(118,864)	(90,733)	(196,074)	(136,139)
Net incurred losses and loss expenses	$296,149	$307,130	$565,734	$531,577

The net favorable development on prior years by segment and line of business for the three and six months ended June 30, 2017 and 2016 was as follows:

	Three Months Ended June 30, 2017				
	Property	Marine	Specialty	Liability	Total
Validus Re	$(671)	$(16,313)	$(6,115)	$ —	$(23,099)
Talbot	(4,894)	(17,056)	6,074	—	(15,876)
Western World	(479)	—	—	16	(463)
AlphaCat	(3,097)	—	(755)	—	(3,852)
Net (favorable) adverse development	$(9,141)	$(33,369)	$(796)	$ 16	$(43,290)

The net favorable loss reserve development on prior accident years of $43.3 million during the three months ended June 30, 2017 was primarily due to favorable development on attritional losses.

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	Three Months Ended June 30, 2016				
	Property	Marine	Specialty	Liability	Total
Validus Re	$(9,468)	$(10,018)	$(11,391)	$—	$(30,877)
Talbot	(10,094)	(8,928)	(9,306)	—	(28,328)
Western World	(1,582)	—	—	(1,576)	(3,158)
AlphaCat	(296)	—	(122)	—	(418)
Net favorable development	$(21,440)	$(18,946)	$(20,819)	$(1,576)	$(62,781)

The net favorable loss reserve development on prior accident years of $62.8 million during the three months ended June 30, 2016 was primarily due to favorable development on attritional losses.

	Six Months Ended June 30, 2017				
	Property	Marine	Specialty	Liability	Total
Validus Re	$(4,242)	$(31,742)	$(15,895)	$—	$(51,879)
Talbot	(11,228)	(33,052)	(410)	—	(44,690)
Western World	(3,302)	—	—	2,620	(682)
AlphaCat	(7,492)	—	222	—	(7,270)
Net (favorable) adverse development	$(26,264)	$(64,794)	$(16,083)	$ 2,620	$(104,521)

The net favorable loss reserve development on prior accident years of $104.5 million during the six months ended June 30, 2017 was primarily due to favorable development on attritional losses.

	Six Months Ended June 30, 2016				
	Property	Marine	Specialty	Liability	Total
Validus Re	$(32,300)	$(6,463)	$(17,798)	$—	$(56,561)
Talbot	(28,540)	(5,964)	(16,544)	—	(51,048)
Western World	(2,023)	—	—	(5,561)	(7,584)
AlphaCat	(477)	—	(850)	—	(1,327)
Net favorable development	$(63,340)	$(12,427)	$(35,192)	$(5,561)	$(116,520)

The net favorable development of $116.5 million for the six months ended June 30, 2016 was primarily due to favorable development on attritional losses.

10. Reinsurance

The Company’s reinsurance balances recoverable at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017	December 31, 2016
Loss reserves recoverable on unpaid:		
Case reserves	$176,416	$ 165,328
IBNR	423,791	265,093
Total loss reserves recoverable	600,207	430,421
Paid losses recoverable	35,675	35,247
Total reinsurance balances recoverable	$635,882	$ 465,668

The Company enters into reinsurance and retrocession agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks, enable it to underwrite policies with higher limits and increase its aggregate capacity. The cession of insurance and reinsurance does not legally discharge the Company from its primary liability for the full amount of the policies, and the Company is required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance or retrocession agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities.

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Credit risk

The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better as rated by Standard & Poor's or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. As at June 30, 2017, $630,821 or 99.2% (December 31, 2016: $461,369 or 99.1%) of the Company's reinsurance balances recoverable were either fully collateralized or recoverable from reinsurers rated A- or better.

Reinsurance balances recoverable by reinsurer as at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017			December 31, 2016		
	Reinsurance Recoverable	% of Total		Reinsurance Recoverable	% of Total	
Top 10 reinsurers	$521,027	81.9	%	$395,308	84.9	%
Other reinsurers' balances > $1 million	106,432	16.8	%	66,944	14.4	%
Other reinsurers' balances < $1 million	8,423	1.3	%	3,416	0.7	%
Total	$635,882	100.0	%	$465,668	100.0	%

The following tables show the reinsurance balances recoverable due from, and the ratings associated with, the Company's top ten reinsurers as at June 30, 2017 and December 31, 2016:

	June 30, 2017			
Top 10 Reinsurers	Rating	Reinsurance Recoverable	% of Total	
Munich Re	AA-	$ 96,997	15.2	%
Lloyd's Syndicates	A+	84,742	13.2	%
Fully collateralized reinsurers	NR	80,558	12.7	%
Swiss Re	AA-	77,928	12.3	%
Everest Re	A+	54,565	8.6	%
Hannover Re	AA-	48,037	7.6	%
Federal Crop Insurance Corporation	(a)	29,009	4.6	%
Transatlantic Re	A+	23,066	3.6	%
XL Catlin	A+	16,062	2.5	%
Helvetia Group	A	10,063	1.6	%
Total		$ 521,027	81.9	%

(a) The Company participates in a crop reinsurance program sponsored by the U.S. federal government. The Company remains obligated for amounts ceded in the event that its reinsurers or retrocessionaires do not meet their obligations, except for amounts ceded to the U.S. federal government in the agriculture line of business.

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	December 31, 2016			
Top 10 Reinsurers	Rating	Reinsurance Recoverable	% of Total	
Lloyd's Syndicates	A+	$ 84,419	18.2	%
Swiss Re	AA-	84,044	18.1	%
Fully collateralized reinsurers	NR	83,088	17.8	%
Hannover Re	AA-	50,603	10.9	%
Everest Re	A+	36,912	7.9	%
Munich Re	AA-	18,214	3.9	%
Transatlantic Re	A+	10,593	2.3	%
Hamilton Re	A-	10,343	2.2	%
Toa Re	A+	9,510	2.0	%
National Indemnity Company	AA+	7,582	1.6	%
Total		$ 395,308	84.9	%

At June 30, 2017 and December 31, 2016, the provision for uncollectible reinsurance relating to reinsurance balances recoverable was $6,741 and $5,153, respectively. To estimate this provision for uncollectible reinsurance, reinsurance balances recoverable are first allocated to applicable reinsurers. This determination is based on a process rather than an estimate, although an element of judgment is applied, especially in relation to ceded IBNR. The Company then uses default factors to determine the portion of a reinsurer's balance deemed to be uncollectible. Default factors require considerable judgment and are determined in part using the current rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions.

11. Share capital

The Company is authorized to issue up to an aggregate of 571,428,571 common and preferred shares with a par value of $0.175 per share.

(a) Preferred shares

On June 12, 2017, the Company issued 10,000 shares of its 5.800% Non-Cumulative Preferred Shares, Series B (the "Series B Preferred Shares") (equivalent to 10,000,000 Depositary Shares, each of which represents a 1/1,000th interest in a Series B Preferred Share), $0.175 par value and $25,000 liquidation preference per share (equivalent to $25 per Depositary Share). The Series B Preferred Shares were registered and sold under the Securities Act of 1933, as amended, and were issued at a price to the public of $25,000 per share (equivalent to $25 per Depositary Share). After underwriting discounts and expenses, the Company received net proceeds of $241,686 which was used for general corporate purposes.

The Depositary Shares, representing the Series B Preferred Shares, are traded on the New York Stock Exchange ("NYSE") under the symbol "VRPRB." The Series B Preferred Shares have no stated maturity date and are redeemable, in whole or in part, at the Company's option on and after June 21, 2022, at a redemption price of $25,000 per Series B Preferred Share (equivalent to $25 per Depository Share), plus declared and unpaid dividends. The Company may also redeem all, but not less than all, of the Series B Preferred Shares before the redemption date at a redemption price of $26,000 per share (equivalent to $26 per Depository Share), plus declared and unpaid dividends, if the Company is required to submit a proposal to the holders of the Series B Preferred Shares concerning an amalgamation, consolidation, merger or other similar corporate transaction or change in Bermuda law. The Series B Preferred Shares may also be redeemed before the redemption date at a redemption price of $25,000 per Series B Preferred Share (equivalent to $25.00 per Depository Share), plus declared and unpaid dividends, in whole, if there is a certain change in tax law, or in whole or in part, in the case of a capital disqualification event. However, no redemption may occur prior to June 21, 2027 unless the Company has sufficient funds in order to meet the Bermuda Monetary Authority's ("the BMA") Enhanced Capital Requirements ("ECR") and the BMA approves of the redemption, or the Company

replaces the capital represented by the Series B Preferred Shares with capital having equal or better capital treatment as the Series B Preferred Shares under the ECR.
Dividends on the Series B Preferred Shares, when, as and if declared by the Company's Board of Directors or a duly authorized committee thereof, will accrue and be payable on the liquidation preference amount from the original issue date, on a non-cumulative basis, quarterly in arrears on each dividend payment date at an annual rate of 5.800%. The Company will be restricted from paying dividends on and repurchasing its common shares, unless certain dividend payments are made on the Series B Preferred Shares.

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Upon any voluntary or involuntary liquidation, dissolution or winding up of the Company, holders of the Series B Preferred Shares and any parity shares are entitled to receive out of our assets available for distribution to shareholders, before any distribution is made to holders of common shares or other junior shares, a liquidating distribution in the amount of $25,000 per Series B Preferred Share (equivalent to $25 per Depositary Share) plus declared and unpaid dividends. Distributions will be made pro rata in accordance with the respective aggregate liquidation preferences of the Series B Preferred Shares and any parity shares and only to the extent of our assets, if any, that are available after satisfaction of all liabilities to creditors.

Holders of the Series B Preferred Shares have no voting rights, except with respect to certain fundamental changes in the terms of the Series B Preferred Shares and in the case of certain dividend non-payments or as otherwise required by Bermuda law or the Company's bye-laws.

On June 13, 2016, the Company issued 6,000 shares of its 5.875% Non-Cumulative Preferred Shares, Series A (the "Series A Preferred Shares") (equivalent to 6,000,000 Depositary Shares, each of which represents a 1/1,000th interest in a Series A Preferred Share), $0.175 par value and $25,000 liquidation preference per share (equivalent to $25 per Depositary Share). Holders of the Series A Preferred Shares have no voting rights, except with respect to certain fundamental changes in the terms of the Series A Preferred Shares and in the case of certain dividend non-payments or as otherwise required by Bermuda law or the Company's bye-laws.

The following table is a summary of the preferred share activity during the six months ended June 30, 2017 and 2016:

	Six Months Ended June 30,	
	2017	2016
Preferred shares issued and outstanding, beginning of period	6,000	—
Preferred shares issued	10,000	6,000
Preferred shares issued and outstanding, end of period	16,000	6,000

The Company had 6,000 Series A Preferred Shares and 10,000 Series B Preferred Shares issued and outstanding as at June 30, 2017 and 6,000 Series A Preferred Shares issued and outstanding as at December 31, 2016.

(b) Common Shares

The holders of common shares are entitled to receive dividends and are allocated one vote per share, provided that, if the controlled shares of any shareholder or group of related shareholders constitute more than 9.09 percent of the outstanding common shares of the Company, their voting power will be reduced to 9.09 percent.

The Company may from time to time repurchase its securities, including common shares, Junior Subordinated Deferrable Debentures and Senior Notes. On February 3, 2015, the Board of Directors of the Company approved an increase in the Company's common share repurchase authorization to $750,000. This amount is in addition to the $2,274,401 of common shares repurchased by the Company through February 3, 2015 under its previously authorized share repurchase programs.

The Company has repurchased 80,776,802 common shares for an aggregate purchase price of $2,718,402 from the inception of its share repurchase program to June 30, 2017. The Company had $305,999 remaining under its authorized share repurchase program as of June 30, 2017.

The Company expects the purchases under its share repurchase program to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program will depend on a variety of factors, including market conditions, the Company's capital position relative to internal and rating agency targets, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time.

The following table is a summary of the common share activity during the six months ended June 30, 2017 and 2016:

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	Six Months Ended June 30,	
	2017	2016
Common shares issued, beginning of period	161,279,976	160,570,772
Restricted share awards vested, net of shares withheld	597,021	601,890
Restricted share units vested, net of shares withheld	14,948	18,486
Options exercised	—	13,635
Performance share awards vested, net of shares withheld	42,410	48,088
Common shares issued, end of period	161,934,355	161,252,871
Treasury shares, end of period	(82,415,774)	(80,480,633)
Common shares outstanding, end of period	79,518,581	80,772,238

(c) Dividends

On May 10, 2017, the Company announced a quarterly cash dividend of $0.38 (2016: $0.35) per common share and a quarterly cash dividend of $0.3671875 per depositary share on its outstanding Series A Preferred Shares. The common share dividend was paid on June 30, 2017 to holders of record on June 15, 2017. The preferred share dividend was paid on June 15, 2017 to holders of record on June 1, 2017.

On February 9, 2017, the Company announced a quarterly cash dividend of $0.38 (2016: $0.35) per common share and a quarterly cash dividend of $0.3671875 per depositary share on its outstanding Series A Preferred Shares. The common share dividend was paid on March 31, 2017 to holders of record on March 15, 2017. The preferred share dividend was paid on March 15, 2017 to holders of record on March 1, 2017.

12. Stock plans

(a) Long Term Incentive Plan

The Company’s Amended and Restated 2005 Long Term Incentive Plan (“LTIP”) provides for grants to employees of options, stock appreciation rights (“SARs”), restricted shares, restricted share units, performance shares, dividend equivalents or other share-based awards. The total number of shares reserved for issuance under the LTIP are 2,753,292 shares of which 714,817 shares remain available for issuance at June 30, 2017. The LTIP is administered by the Compensation Committee of the Board of Directors. No SARs have been granted to date. Grant prices are established at the fair market value of the Company’s common shares at the date of grant.

i. Options

Options may be exercised for voting common shares upon vesting. Outstanding options have a life of 10 years and vest either pro rata or at the end of the required service period from the date of grant. Fair value of the option awards at the date of grant is determined using the Black-Scholes option-pricing model.

Expected volatility is based on stock price volatility of comparable publicly-traded companies. The Company used the simplified method consistent with U.S. GAAP authoritative guidance on stock compensation expenses to estimate expected lives for options granted during the period as historical exercise data was not available and the options met the requirement as set out in the guidance.

The Company has not granted any stock option awards since September 4, 2009. These stock option awards were fully amortized during the year ended December 31, 2012.

Activity with respect to options for the six months ended June 30, 2017 and 2016 was as follows:

	Six Months Ended June 30,					
	2017			2016		
	Options	Weighted Average Grant Date Fair Value	Weighted Average Grant Date Exercise Price	Options	Weighted Average Grant Date Fair Value	Weighted Average Grant Date Exercise Price
Options outstanding, beginning of period	26,136	$ 6.78	$ 23.48	65,401	$ 7.74	$ 20.17

Options exercised	—	—	—	(14,044)	7.69	17.02
Options outstanding, end of period	26,136	$ 6.78	$ 23.48	51,357	$ 7.75	$ 21.03

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ii. Restricted share awards

Restricted shares granted under the LTIP vest either pro rata or at the end of the required service period and contain certain restrictions during the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. The Company recognized share compensation expenses during the three and six months ended June 30, 2017 of $9,745 (2016: $9,517) and $18,789 (2016: $18,646), respectively. The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.

Activity with respect to unvested restricted share awards for the six months ended June 30, 2017 and 2016 was as follows:

	Six Months Ended June 30,			
	2017		2016	
	Restricted Share Awards	Weighted Average Grant Date Fair Value	Restricted Share Awards	Weighted Average Grant Date Fair Value
Restricted share awards outstanding, beginning of period	2,469,982	$ 40.89	2,739,446	$ 38.25
Restricted share awards granted	481,619	53.42	534,905	48.69
Restricted share awards vested	(803,764)	41.31	(783,523)	37.32
Restricted share awards forfeited	(39,617)	41.98	(8,317)	37.94
Restricted share awards outstanding, end of period	2,108,220	$ 43.58	2,482,511	$ 40.79

At June 30, 2017, there were $63,931 (December 31, 2016: $58,804) of total unrecognized share compensation expenses in respect of restricted share awards that are expected to be recognized over a weighted-average period of 2.6 years (December 31, 2016: 2.3 years).

iii. Restricted share units

Restricted share units under the LTIP vest either ratably or at the end of the required service period and contain certain restrictions during the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. The Company recognized share compensation expenses during the three and six months ended June 30, 2017 of $327 (2016: $377) and $642 (2016: $688), respectively. The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.

Activity with respect to unvested restricted share units for the six months ended June 30, 2017 and 2016 was as follows:

	Six Months Ended June 30,			
	2017		2016	
	Restricted Share Units	Weighted Average Grant Date Fair Value	Restricted Share Units	Weighted Average Grant Date Fair Value
Restricted share units outstanding, beginning of period	112,808	$ 40.95	114,337	$ 38.47
Restricted share units granted	12,236	53.40	20,129	48.69
Restricted share units vested	(18,241)	41.66	(23,982)	38.18
Restricted share units issued in lieu of cash dividends	1,468	40.98	1,629	38.47
Restricted share units outstanding, end of period	108,271	$ 42.24	112,113	$ 40.37

At June 30, 2017, there were $2,558 (December 31, 2016: $2,542) of total unrecognized share compensation expenses in respect of restricted share units that are expected to be recognized over a weighted-average period of 2.6 years (December 31, 2016: 2.6 years).

iv. Performance share awards

The performance share awards contain a performance based component. The performance component relates to the compounded growth in the Dividend Adjusted Diluted Book Value per Share ("DBVPS") over a three-year period relative to the Company's peer group. For performance share awards granted during the period, the grant date DBVPS is based on the DBVPS at the end of the most recent financial reporting year. The Dividend Adjusted Performance Period End DBVPS will be the DBVPS three years after the grant date DBVPS. The fair value estimate earns over the requisite attribution period and the estimate will be reassessed at the end

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of each performance period which will reflect any adjustments in the Consolidated Statements of Income and Comprehensive Income in the period in which they are determined.

The Company recognized share compensation expenses during the three and six months ended June 30, 2017 of $1,074 (2016: $833) and $1,206 (2016: $2,630), respectively.

Activity with respect to unvested performance share awards for the six months ended June 30, 2017 and 2016 was as follows:

	Six Months Ended June 30,			
	2017		2016	
	Performance Share Awards	Weighted Average Grant Date Fair Value	Performance Share Awards	Weighted Average Grant Date Fair Value
Performance share awards outstanding, beginning of period	285,820	$ 44.53	172,594	$ 40.70
Performance share awards granted	107,209	53.40	121,844	48.69
Performance share awards vested	(52,639)	37.33	(57,581)	36.11
Performance share awards conversion adjustment	(26,322)	36.82	45,517	36.82
Performance share awards outstanding, end of period	314,068	$ 49.37	282,374	$ 44.46

At June 30, 2017, there were $10,250 (December 31, 2016: $6,902) of total unrecognized share compensation expenses in respect of performance share awards that are expected to be recognized over a weighted-average period of 2.3 years (December 31, 2016: 2.1 years).

(b) Total share compensation expenses

The breakdown of share compensation expenses by award type for the periods indicated was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Restricted share awards	$9,745	$9,517	$18,789	$18,646
Restricted share units	327	377	642	688
Performance share awards	1,074	833	1,206	2,630
Total	$11,146	$10,727	$20,637	$21,964

13. Debt and financing arrangements

The Company’s financing structure is comprised of debentures and senior notes payable along with credit and other facilities.

The Company’s outstanding debentures and senior notes payable as at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017	December 31, 2016
Deferrable debentures		
2006 Junior Subordinated	$150,000	$ 150,000
2007 Junior Subordinated	139,800	139,800
Flagstone 2006 Junior Subordinated	134,850	133,676
Flagstone 2007 Junior Subordinated	113,750	113,750
Total debentures payable	538,400	537,226
2010 Senior notes payable	250,000	250,000
Less: Unamortized debt issuance costs	(4,537)	(4,638)

Total senior notes payable	245,463	245,362
Total debentures and senior notes payable	$783,863	$ 782,588

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The Company's outstanding credit and other facilities as at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017		December 31, 2016	
	Commitment	Drawn and outstanding	Commitment	Drawn and outstanding
Credit and other facilities				
$85,000 syndicated unsecured letter of credit facility	$85,000	$ —	$85,000	$ —
$300,000 syndicated secured letter of credit facility	300,000	87,718	300,000	90,252
$24,000 secured bi-lateral letter of credit facility	24,000	5,648	24,000	4,553
$20,000 AlphaCat Re secured letter of credit facility [(a)]	—	—	20,000	20,000
$25,000 IPC bi-lateral facility	25,000	5,535	25,000	5,842
$236,000 Flagstone bi-lateral facility	236,000	102,190	236,000	144,392
Total credit and other facilities	$670,000	$ 201,091	$690,000	$ 265,039

(a) The Company terminated its AlphaCat Re secured letter of credit facility on January 6, 2017.

(a) Senior notes and junior subordinated deferrable debentures

The following table summarizes the key terms of the Company's senior notes and junior subordinated deferrable debentures:

Description	Issuance date	Issued	Maturity date	Interest Rate as at Issuance Date	Interest Rate as at June 30, 2017	Interest payments due
2006 Junior Subordinated Deferrable Debentures	June 15, 2006	$150,000	June 15, 2036	9.069% [(a)]	5.831% [(e)]	Quarterly
Flagstone 2006 Junior Subordinated Deferrable Debentures	August 23, 2006	$134,850	September 15, 2036	3.540% [(b)]	6.463% [(e)]	Quarterly
2007 Junior Subordinated Deferrable Debentures	June 21, 2007	$200,000	June 15, 2037	8.480% [(c)]	5.180% [(e)]	Quarterly
Flagstone 2007 Junior Subordinated Deferrable Debentures	June 8, 2007	$100,000	July 30, 2037	3.000% [(b)]	5.900% [(e)]	Quarterly
Flagstone 2007 Junior Subordinated Deferrable Debentures	September 20, 2007	$25,000	September 15, 2037	3.100% [(b)]	5.983% [(e)]	Quarterly
2010 Senior Notes due 2040	January 26, 2010	$250,000	January 26, 2040	8.875% [(d)]	8.875% [(d)]	Semi-annually in arrears

(a) Fixed interest rate for 5 years, floating interest rate of three-month LIBOR plus 3.550% thereafter, reset quarterly.
(b) Floating interest rate of three-month LIBOR plus amount stated, reset quarterly.
(c) Fixed interest rate for 5 years, floating interest rate of three-month LIBOR plus 2.950% thereafter, reset quarterly.
(d) Fixed interest rate.
(e) Fixed interest rate as a result of interest rate swap contracts entered into by the Company.

Future payments of principal of $250,000 and $538,400 on the 2010 Senior Notes and the debentures, respectively, are expected to be made after 2022.

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(b) Credit facilities

The Company has pledged cash and investments as collateral under the Company's credit facilities in the total amount of $404,516 (December 31, 2016: $442,184) as detailed in the table below:

	Cash and investments pledged as collateral	
	June 30, 2017	December 31, 2016
$300,000 syndicated secured letter of credit facility	$147,048	$ 157,597
$24,000 secured bi-lateral letter of credit facility	33,353	48,097
AlphaCat Re secured letter of credit facility [(a)]	—	20,032
$236,000 Flagstone bi-lateral facility	224,115	216,458
Total cash and investments pledged as collateral	$404,516	$ 442,184

(a) The Company terminated its AlphaCat Re secured letter of credit facility on January 6, 2017.

As of June 30, 2017 and December 31, 2016, the Company was in compliance with all covenants and restrictions under its credit facilities.

(c) Finance expenses

Finance expenses consist of interest on the junior subordinated deferrable debentures and senior notes, the amortization of debt offering costs, credit facility fees, bank charges, Talbot Funds at Lloyds ("FAL") facility, AlphaCat financing fees and other charges as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
2006 Junior Subordinated Deferrable Debentures	$2,211	$2,211	$4,398	$4,422
2007 Junior Subordinated Deferrable Debentures	1,831	1,830	3,641	3,661
Flagstone 2006 Junior Subordinated Deferrable Debentures	2,248	2,244	4,469	4,489
Flagstone 2007 Junior Subordinated Deferrable Debentures	1,751	1,766	3,474	3,533
2010 Senior Notes due 2040	5,598	5,597	11,195	11,194
Credit facilities	403	235	621	896
Bank and other charges	131	206	282	213
AlphaCat fees [(a)]	36	77	72	961
Total finance expenses	$14,209	$14,166	$28,152	$29,369

(a) Includes finance expenses incurred by AlphaCat Managers Ltd. in relation to fund raising for the AlphaCat sidecars, the AlphaCat ILS funds and AlphaCat direct.

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14. Accumulated other comprehensive loss

The changes in accumulated other comprehensive loss, by component for the three and six months ended June 30, 2017 and 2016 was as follows:

	Three Months Ended June 30, 2017			
	Foreign currency translation adjustment	Minimum pension liability	Cash flow hedge	Total
Balance, net of tax, beginning of period	$(21,677)	$(82)	$(694)	$(22,453)
Other comprehensive income (loss), net of tax	1,489	1,184	(144)	2,529
Balance, net of tax, end of period	$(20,188)	$1,102	$(838)	$(19,924)

	Three Months Ended June 30, 2016			
	Foreign currency translation adjustment	Minimum pension liability	Cash flow hedge	Total
Balance, net of tax, beginning of period	$(13,862)	$251	$(1,827)	$(15,438)
Other comprehensive (loss) income, net of tax	(3,287)	479	64	(2,744)
Balance, net of tax, end of period	$(17,149)	$730	$(1,763)	$(18,182)

	Six Months Ended June 30, 2017			
	Foreign currency translation adjustment	Minimum pension liability	Cash flow hedge	Total
Balance, net of tax, beginning of period	$(22,274)	$(150)	$(792)	$(23,216)
Other comprehensive income (loss), net of tax	2,086	1,252	(46)	3,292
Balance, net of tax, end of period	$(20,188)	$1,102	$(838)	$(19,924)

	Six Months Ended June 30, 2016			
	Foreign currency translation adjustment	Minimum pension liability	Cash flow hedge	Total
Balance, net of tax, beginning of period	$(11,834)	$334	$(1,069)	$(12,569)
Other comprehensive (loss) income, net of tax	(5,315)	396	(694)	(5,613)
Balance, net of tax, end of period	$(17,149)	$730	$(1,763)	$(18,182)

(Expressed in thousands of U.S. dollars, except share and per share information)

15. Commitments and contingencies

(a) Funds at Lloyd's

Talbot operates in Lloyd's through a corporate member, Talbot 2002 Underwriting Capital Ltd ("T02"), which is the sole participant in Syndicate 1183. Lloyd's sets T02's required capital annually based on Syndicate 1183's business plan, rating environment and reserving environment together with input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. Such capital, called Funds at Lloyd's ("FAL"), comprises cash and investments. The Company provided FAL in the amount of $583,600 for the 2017 underwriting year (2016 underwriting year: $617,000).

The amounts which are provided as FAL are not available for distribution to the Company for the payment of dividends. Talbot's corporate member may also be required to maintain funds under the control of Lloyd's in excess of its capital requirement and such funds also may not be available for distribution to the Company for the payment of dividends.

(b) Lloyd's Central Fund

Whenever a member of Lloyd's is unable to pay its debts to policyholders, such debts may be payable by the Lloyd's Central Fund. If Lloyd's determines that the Central Fund needs to be increased, it has the power to assess premium levies on current Lloyd's members up to 3% of a member's underwriting capacity in any one year. The Company does not believe that any assessment is likely in the foreseeable future and has not provided any allowance for such an assessment. However, based on the Company's 2017 underwriting capacity at Lloyd's of £600,000, at the June 30, 2017 exchange rate of £1 equals $1.30 and assuming the maximum 3% assessment, the Company would be assessed approximately $23,400.

(c) Marketing Services Agreement ("MSA")

On May 1, 2017, the Company entered into a MSA with Archer Daniels Midland ("ADM"). Under this agreement, ADM agrees to provide marketing services via its own distribution channels for an annual fee of $2,000 for a period of seven years, with an option for the Company to extend for an additional three years. For the three and six months ended June 30, 2017, the Company had incurred fees of $333 in relation to the MSA.

(d) Unfunded investment commitments

As at June 30, 2017 and December 31, 2016, the Company had total unfunded investment commitments related to the following:

	Unfunded investment commitments	
	June 30, 2017	December 31, 2016
Fixed maturity investments [(a)]	$25,238	$ 28,499
Other investments [(b)]	119,495	156,134
Investments in investment affiliates [(c)]	84,046	64,071
AlphaCat ILS Fund	—	10,000
Total unfunded investment commitments	$228,779	$ 258,704

(a) The Company has an outstanding commitment to participate in certain secured loan facilities through participation agreements with an established loan originator.

(b) The Company's total capital commitments related to other investments as at June 30, 2017 was $313,000 (December 31, 2016: $308,000).

(c) Refer to Note 4(c), "Investments in Investment Affiliates."

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16. Related party transactions

The transactions listed below are classified as related party transactions as principals and/or directors of each counterparty are members of the Company's board of directors.

(a) Aquiline Capital Partners LLC ("Aquiline Capital")

Group Ark Insurance

Subsequent to July 2016, Aquiline Capital ceased to be shareholders of Group Ark Insurance Holdings Ltd. ("Group Ark"). Christopher E. Watson, a director of the Company and senior principal of Aquiline Capital, continues to serve as a director of Group Ark. Pursuant to reinsurance agreements with a subsidiary of Group Ark, the Company recognized gross premiums written during the three and six months ended June 30, 2016 of $65 and $1,971, respectively. The Company also recognized reinsurance premiums ceded during the three and six months ended June 30, 2016 of $(17) and $nil, respectively. Earned premium adjustments were recorded during the three and six months ended June 30, 2016 of $473 and $999, respectively. As at December 31, 2016 the Company had recorded premiums receivable and loss reserves recoverable of $292 and $798, respectively.

Wellington

Pursuant to reinsurance agreements with a subsidiary of Wellington Insurance Company ("Wellington"), during the three and six months ended June 30, 2017 the Company recognized gross premiums written of $1,144 and $4,118 (2016: $nil and $nil), respectively, and earned premium adjustments of $1,676 and $2,537 (2016: $nil and $nil), respectively. As at June 30, 2017 and December 31, 2016 the Company had recorded premiums receivable of $3,531 and $666, respectively. Aquiline Capital are shareholders of Wellington and Christopher E. Watson, a director of the Company and senior principal of Aquiline Capital, serves as a director of Wellington.

Aquiline II, Aquiline III and Aquiline Tech

The Company had, as of June 30, 2017 and December 31, 2016, investments in Aquiline II, III and Tech with a total value of $103,377 and $100,431 and outstanding unfunded commitments of $84,046 and $64,071, respectively. For the three and six months ended June 30, 2017, the Company incurred $130 and $486 (2016: $440 and $440), respectively, in partnership fees associated with these investments. Additional information related to Aquiline II, III and Tech is disclosed in Note 4(c), "Investments in Investment Affiliates."

(b) Other

Certain shareholders of the Company and their affiliates, as well as employers of entities associated with directors or officers have purchased insurance and/or reinsurance from the Company in the ordinary course of business. The Company believes these transactions were settled for arm's length consideration.

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17. Earnings per common share
The following table sets forth the computation of basic earnings per common share and earnings per diluted common share for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Basic earnings per common share				
Net income available to Validus common shareholders	$101,095	$ 94,963	$195,656	$ 261,773
Weighted average number of common shares outstanding	79,270,561	81,950,833	79,202,116	82,386,047
Basic earnings per share available to Validus common shareholders	$1.28	$ 1.16	$2.47	$ 3.18
Earnings per diluted common share				
Net income available to Validus common shareholders	$101,095	$ 94,963	$195,656	$ 261,773
Weighted average number of common shares outstanding	79,270,561	81,950,833	79,202,116	82,386,047
Share equivalents:				
Stock options	14,739	33,796	15,059	34,837
Unvested restricted shares	1,587,151	1,388,374	1,644,823	1,364,775
Weighted average number of diluted common shares outstanding	80,872,451	83,373,003	80,861,998	83,785,659
Earnings per diluted share available to Validus common shareholders	$1.25	$ 1.14	$2.42	$ 3.12

Share equivalents that would result in the issuance of common shares of 412,603 (2016: 507,262) and 207,054 (2016: 253,631) were outstanding for the three and six months ended June 30, 2017, respectively, but were not included in the computation of earnings per diluted common share because the effect would be antidilutive.

18. Segment information

The Company conducts its operations worldwide through four operating segments, which have been determined under ASC Topic 280 “Segment Reporting” to be Validus Re, Talbot, Western World and AlphaCat. For segmental reporting purposes, the results of CRS have been included in the results of the Western World segment as of May 1, 2017, the date of acquisition. The Company’s operating segments are strategic business units that offer different products and services. They are managed and have capital allocated separately because each segment undertakes different strategies.

A description of each of the Company’s operating segments and its Corporate and Investments function is as follows:

Validus Re Segment

The Validus Re segment is focused primarily on treaty reinsurance. The primary lines in which the segment conducts business are property, marine and specialty which includes agriculture, aerospace and aviation, financial lines of business, nuclear, terrorism, life, accident & health, workers’ compensation, crisis management, contingency, technical lines, composite, trade credit and casualty.

Talbot Segment

The Talbot segment is focused on a wide range of marine and energy, political lines, commercial property, financial lines, contingency, accident & health and aviation classes of business on an insurance or facultative reinsurance basis and principally property, aerospace and marine classes of business on a treaty reinsurance basis.

Western World Segment

The Western World segment is focused on providing commercial insurance products on a surplus lines and specialty admitted basis. Western World specializes in underwriting classes of business that are not easily placed in the standard insurance market due to their complexity, high hazard, or unusual nature; including general liability, property and professional liability, homeowners, commercial package and agriculture classes of business.

AlphaCat Segment

The AlphaCat segment leverages the Company’s underwriting and analytical expertise and earns management and performance fees from the Company and other third party investors primarily through the AlphaCat ILS funds and sidecars.

Corporate and Investments

The Company has a corporate and investments function (“Corporate and Investments”), which includes the activities of the parent company, and which carries out certain functions for the group, including investment management. Corporate and Investments includes investment income on a managed basis and other non-segment expenses, predominantly general and administrative, stock compensation, finance and transaction expenses. Transaction expenses are primarily comprised of legal, financial advisory and audit related services incurred in connection with the acquisition of CRS. Corporate and Investments also includes the activities of certain key executives such as the Chief Executive Officer and Chief Financial Officer. For reporting purposes, Corporate and Investments is reflected separately; however, it is not considered an operating segment under these circumstances. Other reconciling items include, but are not limited to, the elimination of certain inter segment revenues and expenses and other items that are not allocated to the operating segments.

A reconciliation of segmental income to net income available to Validus is included in the tables below.

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The following tables summarize the results of our operating segments and "Corporate and Investments":

	Three Months Ended June 30,		Six Months Ended June 30,	
Validus Re Segment Information	2017	2016	2017	2016
Underwriting revenues				
Gross premiums written	$296,997	$285,810	$917,519	$977,478
Reinsurance premiums ceded	(11,387)	(3,196)	(120,200)	(95,691)
Net premiums written	285,610	282,614	797,319	881,787
Change in unearned premiums	(45,003)	(35,492)	(338,300)	(390,834)
Net premiums earned	240,607	247,122	459,019	490,953
Other insurance related income (loss)	58	150	136	(165)
Total underwriting revenues	240,665	247,272	459,155	490,788
Underwriting deductions				
Losses and loss expenses	104,685	132,139	190,839	215,007
Policy acquisition costs	47,158	42,564	88,414	84,823
General and administrative expenses	19,274	17,872	36,106	35,051
Share compensation expenses	2,663	2,775	5,140	5,676
Total underwriting deductions	173,780	195,350	320,499	340,557
Underwriting income	$66,885	$51,922	$138,656	$150,231
Selected ratios				
Ratio of net to gross premiums written	96.2 %	98.9 %	86.9 %	90.2 %
Losses and loss expense ratio	43.5 %	53.5 %	41.6 %	43.8 %
Policy acquisition cost ratio	19.6 %	17.2 %	19.3 %	17.3 %
General and administrative expense ratio (a)	9.1 %	8.4 %	8.9 %	8.3 %
Expense ratio	28.7 %	25.6 %	28.2 %	25.6 %
Combined ratio	72.2 %	79.1 %	69.8 %	69.4 %

(a) The general and administrative expense ratio includes share compensation expenses.

(Expressed in thousands of U.S. dollars, except share and per share information)

	Three Months Ended June 30,		Six Months Ended June 30,	
Talbot Segment Information	2017	2016	2017	2016
Underwriting revenues				
Gross premiums written	$262,477	$296,067	$509,652	$562,384
Reinsurance premiums ceded	(24,977)	(27,161)	(117,801)	(114,619)
Net premiums written	237,500	268,906	391,851	447,765
Change in unearned premiums	(45,626)	(67,357)	(4,912)	(39,424)
Net premiums earned	191,874	201,549	386,939	408,341
Other insurance related income	65	279	820	290
Total underwriting revenues	191,939	201,828	387,759	408,631
Underwriting deductions				
Losses and loss expenses	93,389	109,310	199,801	209,411
Policy acquisition costs	44,305	43,613	87,581	87,956
General and administrative expenses	35,582	39,061	74,025	77,596
Share compensation expenses	3,155	3,270	5,982	6,792
Total underwriting deductions	176,431	195,254	367,389	381,755
Underwriting income	$15,508	$6,574	$20,370	$26,876
Selected ratios				
Ratio of net to gross premiums written	90.5 %	90.8 %	76.9 %	79.6 %
Losses and loss expense ratio	48.7 %	54.2 %	51.6 %	51.3 %
Policy acquisition cost ratio	23.1 %	21.6 %	22.6 %	21.5 %
General and administrative expense ratio [(a)]	20.2 %	21.1 %	20.7 %	20.7 %
Expense ratio	43.3 %	42.7 %	43.3 %	42.2 %
Combined ratio	92.0 %	96.9 %	94.9 %	93.5 %

(a) The general and administrative expense ratio includes share compensation expenses.

(Expressed in thousands of U.S. dollars, except share and per share information)

Western World Segment Information	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Underwriting revenues				
Gross premiums written	$131,068	$86,971	$303,111	$150,930
Reinsurance premiums ceded	(23,180)	(5,006)	(28,798)	(9,145)
Net premiums written	107,888	81,965	274,313	141,785
Change in unearned premiums	22,806	(16,309)	(46,347)	(14,630)
Net premiums earned	130,694	65,656	227,966	127,155
Other insurance related income	663	189	904	477
Total underwriting revenues	131,357	65,845	228,870	127,632
Underwriting deductions				
Losses and loss expenses	97,008	44,229	171,933	83,875
Policy acquisition costs	19,230	15,410	39,466	29,610
General and administrative expenses	18,316	11,458	29,070	23,533
Share compensation expenses	609	542	1,301	1,123
Total underwriting deductions	135,163	71,639	241,770	138,141
Underwriting loss	$(3,806)	$(5,794)	$(12,900)	$(10,509)
Selected ratios				
Ratio of net to gross premiums written	82.3 %	94.2 %	90.5 %	93.9 %
Losses and loss expense ratio	74.2 %	67.4 %	75.4 %	66.0 %
Policy acquisition cost ratio	14.7 %	23.5 %	17.3 %	23.3 %
General and administrative expense ratio [a]	14.5 %	18.2 %	13.4 %	19.3 %
Expense ratio	29.2 %	41.7 %	30.7 %	42.6 %
Combined ratio	103.4 %	109.1 %	106.1 %	108.6 %

(a) The general and administrative expense ratio includes share compensation expenses.

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AlphaCat Segment Information	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Fee revenues				
Third party	$5,549	$3,091	$10,193	$7,818
Related party	644	328	1,275	1,219
Total fee revenues	6,193	3,419	11,468	9,037
Expenses				
General and administrative expenses	3,549	2,751	7,393	4,233
Share compensation expenses	83	133	165	274
Finance expenses	44	75	75	883
Tax expense	135	—	134	—
Foreign exchange losses	1	4	—	12
Total expenses	3,812	2,963	7,767	5,402
Income before investments from AlphaCat Funds and Sidecars	2,381	456	3,701	3,635
Investment income (loss) from AlphaCat Funds and Sidecars [(a)]				
AlphaCat Sidecars	(21)	541	(133)	665
AlphaCat ILS Funds - Lower Risk [(b)]	1,301	2,075	3,490	4,582
AlphaCat ILS Funds - Higher Risk [(b)]	2,600	692	4,967	3,128
BetaCat ILS Funds	263	1,113	631	1,676
PaCRe	—	—	—	(23)
Validus' share of investment income from AlphaCat Funds and Sidecars	4,143	4,421	8,955	10,028
Validus' share of AlphaCat segment income	$6,524	$4,877	$12,656	$13,663
Supplemental information				
Gross premiums written				
AlphaCat Sidecars	$—	$(14)	$66	$(66)
AlphaCat ILS Funds - Lower Risk [(b)]	53,632	50,234	106,540	110,192
AlphaCat ILS Funds - Higher Risk [(b)]	43,672	42,010	137,208	138,330
AlphaCat Direct [(c)]	8,378	6,675	26,794	17,797
Total gross premiums written	$105,682	$98,905	$270,608	$266,253

(a) The investment income from the AlphaCat funds and sidecars is based on equity accounting.

(b) Lower risk AlphaCat ILS funds have a maximum permitted portfolio expected loss of less than 7%, whereas higher risk AlphaCat ILS funds have a maximum permitted portfolio expected loss of greater than 7%. Expected loss represents the average annual loss over the set of simulation scenarios divided by the total limit.

(c) AlphaCat Direct includes direct investments from third party investors in AlphaCat Re.

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Corporate and Investments	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Investment income				
Managed net investment income [a]	$38,063	$36,849	$74,255	$64,772
Corporate expenses				
General and administrative expenses	18,847	17,872	36,024	34,055
Share compensation expenses	4,636	4,007	8,049	8,099
Finance expenses [b]	14,149	13,979	28,013	28,320
Dividends on preferred shares	2,203	—	4,406	—
Tax (benefit) expense	(1,122)	1,706	(4,670)	(412)
Total Corporate expenses	38,713	37,564	71,822	70,062
Other items				
Net realized gains (losses) on managed investments [b]	2,269	2,520	(623)	1,434
Change in net unrealized gains on managed investments [b]	15,942	30,052	30,291	77,130
Income (loss) from investment affiliate	9,466	(589)	14,654	(4,702)
Foreign exchange (losses) gains [b]	(7,323)	6,621	(6,220)	12,695
Other income	174	79	268	756
Transaction expenses	(4,427)	—	(4,427)	—
Total other items	16,101	38,683	33,943	87,313
Total Corporate and Investments	$15,451	$37,968	$36,376	$82,023

(a) Managed net investment income excludes the components which are included in the Company’s share of AlphaCat, net realized and change in unrealized gains on managed investments and income (loss) from investment affiliates.

(b) These items exclude the components which are included in Validus’ share of AlphaCat and amounts which are consolidated from VIEs.

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The following tables reconcile the results of our operating segments along with our corporate and investments function to the Consolidated results of the Company for the periods indicated:

	Three Months Ended June 30, 2017						
	Validus Re Segment	Talbot Segment	Western World Segment	AlphaCat Segment and Consolidated VIEs	Corporate and Investments	Eliminations	Total
Underwriting revenues							
Gross premiums written	$296,997	$262,477	$131,068	$ 105,682	$ —	$ (3,322)	$792,902
Reinsurance premiums ceded	(11,387)	(24,977)	(23,180)	—	—	3,322	(56,222)
Net premiums written	285,610	237,500	107,888	105,682	—	—	736,680
Change in unearned premiums	(45,003)	(45,626)	22,806	(37,830)	—	—	(105,653)
Net premiums earned	240,607	191,874	130,694	67,852	—	—	631,027
Other insurance related income	58	65	663	5,874	—	(5,495)	1,165
Total underwriting revenues	240,665	191,939	131,357	73,726	—	(5,495)	632,192
Underwriting deductions							
Losses and loss expenses	104,685	93,389	97,008	1,067	—	—	296,149
Policy acquisition costs	47,158	44,305	19,230	7,165	—	(590)	117,268
General and administrative expenses	19,274	35,582	18,316	9,768	18,847	(5,438)	96,349
Share compensation expenses	2,663	3,155	609	83	4,636	—	11,146
Total underwriting deductions	173,780	176,431	135,163	18,083	23,483	(6,028)	520,912
Underwriting income (loss)	$66,885	$15,508	$(3,806)	$ 55,643	$ (23,483)	$ 533	$111,280
Other items [(a)]	—	—	—	183	7,501	—	7,684
Dividends on preferred shares	—	—	—	—	(2,203)	—	(2,203)
Net investment income	—	—	—	6,178	38,063	—	44,241
Transaction expenses	—	—	—	—	(4,427)	—	(4,427)
(Income) attributable to AlphaCat investors	—	—	—	(11,830)	—	—	(11,830)
Net (income) attributable to noncontrolling interest	—	—	—	(43,650)	—	—	(43,650)
Segmental income (loss)	$66,885	$15,508	$(3,806)	$ 6,524	$ 15,451	$ 533	
Net income available to Validus common shareholders							$101,095

(a) Other items includes finance expenses, tax benefit (expense), foreign exchange gains (losses), net realized and change in net unrealized gains (losses) on investments, income from investment and operating affiliates and other income (loss).

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	Three Months Ended June 30, 2016						
	Validus Re Segment	Talbot Segment	Western World Segment	AlphaCat Segment and Consolidated VIEs	Corporate and Investments	Eliminations	Total
Underwriting revenues							
Gross premiums written	$285,810	$296,067	$86,971	$ 98,905	$ —	$ (3,711)	$764,042
Reinsurance premiums ceded	(3,196)	(27,161)	(5,006)	(4,577)	—	3,711	(36,229)
Net premiums written	282,614	268,906	81,965	94,328	—	—	727,813
Change in unearned premiums	(35,492)	(67,357)	(16,309)	(34,932)	—	—	(154,090)
Net premiums earned	247,122	201,549	65,656	59,396	—	—	573,723
Other insurance related income	150	279	189	3,401	—	(3,274)	745
Total underwriting revenues	247,272	201,828	65,845	62,797	—	(3,274)	574,468
Underwriting deductions							
Losses and loss expenses	132,139	109,310	44,229	21,452	—	—	307,130
Policy acquisition costs	42,564	43,613	15,410	6,530	—	(151)	107,966
General and administrative expenses	17,872	39,061	11,458	6,561	17,872	(3,136)	89,688
Share compensation expenses	2,775	3,270	542	133	4,007	—	10,727
Total underwriting deductions	195,350	195,254	71,639	34,676	21,879	(3,287)	515,511
Underwriting income (loss)	$51,922	$6,574	$(5,794)	$ 28,121	$ (21,879)	$ 13	$58,957
Other items [(a)]	—	—	—	1,058	22,998	—	24,056
Dividends on preferred shares	—	—	—	—	—	—	—
Net investment income	—	—	—	3,005	36,849	(597)	39,257
(Income) attributable to AlphaCat investors	—	—	—	(6,114)	—	—	(6,114)
Net (income) attributable to noncontrolling interest	—	—	—	(21,193)	—	—	(21,193)
Segmental income (loss)	$51,922	$6,574	$(5,794)	$ 4,877	$ 37,968	$ (584)	
Net income available to Validus common shareholders							$94,963

(a) Other items includes finance expenses, tax expenses, foreign exchange gains (losses), net realized and change in net unrealized gains (losses) on investments, income from investment and operating affiliates and other income (loss).

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	Six Months Ended June 30, 2017						
	Validus Re Segment	Talbot Segment	Western World Segment	AlphaCat Segment and Consolidated VIEs	Corporate and Investments	Eliminations	Total
Underwriting revenues							
Gross premiums written	$917,519	$509,652	$303,111	$ 270,608	$ —	$ (17,131)	$1,983,759
Reinsurance premiums ceded	(120,200)	(117,801)	(28,798)	(6,660)	—	17,131	(256,328)
Net premiums written	797,319	391,851	274,313	263,948	—	—	1,727,431
Change in unearned premiums	(338,300)	(4,912)	(46,347)	(131,469)	—	—	(521,028)
Net premiums earned	459,019	386,939	227,966	132,479	—	—	1,206,403
Other insurance related income	136	820	904	11,035	—	(10,494)	2,401
Total underwriting revenues	459,155	387,759	228,870	143,514	—	(10,494)	1,208,804
Underwriting deductions							
Losses and loss expenses	190,839	199,801	171,933	3,161	—	—	565,734
Policy acquisition costs	88,414	87,581	39,466	14,066	—	(631)	228,896
General and administrative expenses	36,106	74,025	29,070	19,409	36,024	(10,361)	184,273
Share compensation expenses	5,140	5,982	1,301	165	8,049	—	20,637
Total underwriting deductions	320,499	367,389	241,770	36,801	44,073	(10,992)	999,540
Underwriting income (loss)	$138,656	$20,370	$(12,900)	$ 106,713	$ (44,073)	$ 498	$209,264
Other items [(a)]	—	—	—	1,298	15,027	—	16,325
Dividends on preferred shares	—	—	—	—	(4,406)	—	(4,406)
Net investment income	—	—	—	10,200	74,255	—	84,455
Transaction expenses	—	—	—	—	(4,427)	—	(4,427)
(Income) attributable to AlphaCat investors	—	—	—	(19,333)	—	—	(19,333)
Net (income) attributable to noncontrolling interest	—	—	—	(86,222)	—	—	(86,222)
Segmental income (loss)	$138,656	$20,370	$(12,900)	$ 12,656	$ 36,376	$ 498	
Net income available to Validus common shareholders							$195,656

(a) Other items includes finance expenses, tax expenses, foreign exchange gains (losses), net realized and change in net unrealized gains (losses) on investments, income from investment and operating affiliates and other income (loss).

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Validus Holdings, Ltd.
Notes to the Consolidated Financial Statements (unaudited)
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	Six Months Ended June 30, 2016						
	Validus Re Segment	Talbot Segment	Western World Segment	AlphaCat Segment and Consolidated VIEs	Corporate and Investments	Eliminations	Total
Underwriting revenues							
Gross premiums written	$977,478	$562,384	$150,930	$266,253	$—	$(20,212)	$1,936,833
Reinsurance premiums ceded	(95,691)	(114,619)	(9,145)	(4,821)	—	20,212	(204,064)
Net premiums written	881,787	447,765	141,785	261,432	—	—	1,732,769
Change in unearned premiums	(390,834)	(39,424)	(14,630)	(142,890)	—	—	(587,778)
Net premiums earned	490,953	408,341	127,155	118,542	—	—	1,144,991
Other insurance related (loss) income	(165)	290	477	9,066	—	(8,187)	1,481
Total underwriting revenues	490,788	408,631	127,632	127,608	—	(8,187)	1,146,472
Underwriting deductions							
Losses and loss expenses	215,007	209,411	83,875	23,284	—	—	531,577
Policy acquisition costs	84,823	87,956	29,610	12,687	—	83	215,159
General and administrative expenses	35,051	77,596	23,533	14,017	34,055	(8,356)	175,896
Share compensation expenses	5,676	6,792	1,123	274	8,099	—	21,964
Total underwriting deductions	340,557	381,755	138,141	50,262	42,154	(8,273)	944,596
Underwriting income (loss)	$150,231	$26,876	$(10,509)	$77,346	$(42,154)	$86	$201,876
Other items [(a)]	—	—	—	1,212	59,405	—	60,617
Dividends on preferred shares	—	—	—	—	—	—	—
Net investment income	—	—	—	4,543	64,772	(597)	68,718
(Income) attributable to AlphaCat investors	—	—	—	(10,714)	—	—	(10,714)
Net (income) attributable to noncontrolling interest	—	—	—	(58,724)	—	—	(58,724)
Segmental income (loss)	$150,231	$26,876	$(10,509)	$13,663	$82,023	$(511)	
Net income available to Validus common shareholders							$261,773

(a) Other items includes finance expenses, tax expenses, foreign exchange gains (losses), net realized and change in net unrealized gains (losses) on investments, income from investment and operating affiliates and other income (loss).

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Validus Holdings, Ltd.
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The Company's exposures are generally diversified across geographic zones. The following tables set forth the gross premiums written by operating segment allocated to the territory of coverage exposure for the periods indicated:

	Gross Premiums Written						
	Three Months Ended June 30, 2017						
	Validus Re	Talbot	Western World	AlphaCat	Eliminations	Total	%
United States	$100,312	$34,470	$131,068	$70,048	$ (3,443)	$332,455	41.9 %
Worldwide excluding United States [(a)]	4,537	32,627	—	870	114	38,148	4.7 %
Australia and New Zealand	3,264	1,848	—	2,003	40	7,155	0.9 %
Europe	748	5,857	—	(15)	275	6,865	0.9 %
Latin America and Caribbean	11,874	24,800	—	46	(1,411)	35,309	4.5 %
Japan	39,305	3,381	—	2,662	(6)	45,342	5.7 %
Canada	3,155	1,111	—	130	(4)	4,392	0.6 %
Rest of the world [(b)]	4,877	23,168	—	—	105	28,150	3.6 %
Sub-total, non United States	67,760	92,792	—	5,696	(887)	165,361	20.9 %
Worldwide including United States [(a)]	53,524	30,735	—	29,937	1,006	115,202	14.5 %
Other locations non-specific [(c)]	75,401	104,480	—	1	2	179,884	22.7 %
Total	$296,997	$262,477	$131,068	$105,682	$ (3,322)	$792,902	100.0%

	Gross Premiums Written						
	Three Months Ended June 30, 2016						
	Validus Re	Talbot	Western World	AlphaCat	Eliminations	Total	%
United States	$129,087	$39,135	$86,971	$37,338	$ (417)	$292,114	38.2 %
Worldwide excluding United States [(a)]	16,975	30,028	—	6,496	(136)	53,363	7.0 %
Australia and New Zealand	1,926	2,063	—	867	21	4,877	0.6 %
Europe	3,267	6,855	—	(145)	216	10,193	1.3 %
Latin America and Caribbean	5,992	27,597	—	—	(2,511)	31,078	4.1 %
Japan	39,053	3,965	—	1,721	(7)	44,732	5.9 %
Canada	1,821	2,470	—	223	(36)	4,478	0.6 %
Rest of the world [(b)]	3,259	29,806	—	—	(457)	32,608	4.3 %
Sub-total, non United States	72,293	102,784	—	9,162	(2,910)	181,329	23.8 %
Worldwide including United States [(a)]	35,561	34,198	—	52,394	(380)	121,773	15.9 %
Other locations non-specific [(c)]	48,869	119,950	—	11	(4)	168,826	22.1 %
Total	$285,810	$296,067	$86,971	$98,905	$ (3,711)	$764,042	100.0%

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Validus Holdings, Ltd.
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	Gross Premiums Written Six Months Ended June 30, 2017						
	Validus Re	Talbot	Western World	AlphaCat	Eliminations	Total	%
United States	$314,180	$63,555	$303,111	$98,251	$ (4,323)	$774,774	39.1 %
Worldwide excluding United States [a]	38,605	66,958	—	7,905	(539)	112,929	5.7 %
Australia and New Zealand	4,195	5,030	—	2,003	(110)	11,118	0.6 %
Europe	30,364	17,572	—	451	(430)	47,957	2.3 %
Latin America and Caribbean	21,216	48,977	—	46	(4,283)	65,956	3.3 %
Japan	40,466	5,206	—	3,855	(36)	49,491	2.5 %
Canada	4,870	2,248	—	130	(49)	7,199	0.4 %
Rest of the world [b]	18,782	46,440	—	—	(1,577)	63,645	3.2 %
Sub-total, non United States	158,498	192,431	—	14,390	(7,024)	358,295	18.0 %
Worldwide including United States [a]	155,945	58,092	—	153,246	(5,784)	361,499	18.2 %
Other locations non-specific [c]	288,896	195,574	—	4,721	—	489,191	24.7 %
Total	$917,519	$509,652	$303,111	$270,608	$ (17,131)	$1,983,759	100.0 %

	Gross Premiums Written Six Months Ended June 30, 2016						
	Validus Re	Talbot	Western World	AlphaCat	Eliminations	Total	%
United States	$424,481	$65,245	$150,930	$62,729	$ (1,555)	$701,830	36.2 %
Worldwide excluding United States [a]	47,239	65,532	—	22,507	(611)	134,667	7.0 %
Australia and New Zealand	6,849	4,375	—	4,949	(113)	16,060	0.8 %
Europe	25,734	20,716	—	3,306	(708)	49,048	2.5 %
Latin America and Caribbean	19,574	51,404	—	—	(5,537)	65,441	3.4 %
Japan	39,925	4,582	—	3,221	(31)	47,697	2.5 %
Canada	3,497	3,562	—	223	(87)	7,195	0.4 %
Rest of the world [b]	19,947	57,290	—	—	(2,342)	74,895	3.9 %
Sub-total, non United States	162,765	207,461	—	34,206	(9,429)	395,003	20.5 %
Worldwide including United States [a]	147,338	62,652	—	167,767	(9,214)	368,543	19.0 %
Other locations non-specific [c]	242,894	227,026	—	1,551	(14)	471,457	24.3 %
Total	$977,478	$562,384	$150,930	$266,253	$ (20,212)	$1,936,833	100.0 %

(a) Represents risks in two or more geographic zones.
(b) Represents risks in one geographic zone.
(c) The Other locations non-specific category refers to business for which an analysis of exposure by geographic zone is not applicable since these exposures can span multiple geographic areas and, in some instances, are not fixed locations.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion and analysis of the Company's unaudited consolidated results of operations for the three and six months ended June 30, 2017 and 2016 and the Company's consolidated financial condition, liquidity and capital resources as at June 30, 2017 and December 31, 2016. This discussion and analysis should be read in conjunction with the Company's unaudited Consolidated Financial Statements and notes thereto included in this filing and the Company's audited Consolidated Financial Statements and related notes for the fiscal year ended December 31, 2016, the discussions of critical accounting policies and the qualitative and quantitative disclosure about market risk, as well as management's discussion and analysis of financial condition and results of operations contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

For a number of reasons, the Company's historical financial results may not accurately indicate future performance. See "Cautionary Note Regarding Forward-Looking Statements." The Risk Factors set forth in Part I, Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016 present a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained herein.

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Executive Overview

The Company conducts its operations worldwide through four operating segments which have been determined under U.S. GAAP segment reporting to be Validus Re, Talbot, Western World, and AlphaCat. On May 1, 2017, the Company acquired all of the outstanding capital stock of CRS and its related agriculture book of business. For segmental reporting purposes, the results of CRS have been included in the results of the Western World segment as of May 1, 2017, the date of acquisition.

In addition, the Company has a corporate and investment function ("Corporate and Investments"), which includes the activities of the parent company, and which carries out certain functions for the group, including investment management. Corporate and Investments includes investment income on a managed basis and other non-segment expenses, predominantly general and administrative, stock compensation, finance and transaction expenses. Corporate and Investments also includes the activities of certain key executives such as the Chief Executive Officer and Chief Financial Officer. For reporting purposes, Corporate and Investments is reflected separately; however, it is not considered an operating segment. The Company's corporate expenses, capital servicing and debt costs and investment results are presented separately within the corporate and investments discussion.

The Company's strategy is to concentrate primarily on short-tail risks, which has been an area where management believes prices and terms provide an attractive risk-adjusted return and the management team has proven expertise. The Company's profitability in any given period is a function of net earned premium and investment revenues, less net losses and loss expenses, acquisition expenses and operating expenses. Financial results in the insurance and reinsurance industry are influenced by the frequency and/or severity of claims and losses, including as a result of catastrophic events; changes in interest rates, financial markets and general economic conditions; the supply of insurance and reinsurance capacity and changes in legal, regulatory and judicial environments.

Business Outlook and Trends

We underwrite global property insurance and reinsurance and have large aggregate exposures to natural and man-made disasters. The occurrence of claims from catastrophic events results in substantial volatility, and can have material adverse effects on the Company's financial condition and results and its ability to write new business. This volatility affects results for the period in which the loss occurs because U.S. GAAP does not permit reinsurers to reserve for such catastrophic events until they occur. Catastrophic events of significant magnitude historically have been relatively infrequent, although management believes the property catastrophe reinsurance market has experienced a higher level of worldwide catastrophic losses in terms of both frequency and severity in the period from 1992 to the present. We also expect that increases in the values and concentrations of insured property will increase the severity of such occurrences in the future. The Company seeks to reflect these types of trends when pricing contracts.

Property and other reinsurance premiums have historically risen in the aftermath of significant catastrophic losses. As loss reserves are established, industry surplus is depleted and the industry's capacity to write new business diminishes. The global property and casualty insurance and reinsurance industry has historically been highly cyclical. Since 2007, increased capital provided by new entrants or by the commitment of capital by existing insurers and reinsurers increased the supply of insurance and reinsurance which resulted in a softening of rates on most lines. From 2010 to 2012, there was an increased level of catastrophe activity, principally the Chilean earthquake, Deepwater Horizon, the Tohoku earthquake, the New Zealand earthquakes and Superstorm Sandy, but the Company continues to see increased competition and decreased premium rates in most classes of business. In the absence of significant catastrophes in recent years, the market supply of capital is greater than the demand and therefore we expect to see continued pressure on rates in the near term.

During the Validus Re and AlphaCat mid year 2017 renewal period, the U.S. property market saw a continuation of the rate trend observed at the January 1 renewals where rate declines were in the low single-digits, with terms and conditions generally unchanged. However, the rate environment in the international property market proved to be more challenging with average rate reductions ranging between 4% and 5%.

Business written by the Talbot and Western World segments is distributed more evenly throughout the year. Through June 30, 2017, the Talbot segment experienced a whole account rate decrease of approximately 4.3% driven primarily by decreases in the downstream and upstream energy classes. The Western World segment experienced a modest whole account rate increase of approximately 0.1% through June 30, 2017.

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Non-GAAP Financial Measures

In presenting the Company's results, management has included and discussed certain non-GAAP financial measures. The Company believes that these non-GAAP measures, which may be defined and calculated differently by other companies, better explain and enhance the understanding of the Company's results of operations. However, these measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP.

Book value financial indicators

In addition to presenting book value per common share determined in accordance with U.S. GAAP, the Company believes that the key financial indicator for evaluating our performance and measuring the overall growth in value generated for shareholders is book value per diluted common share plus accumulated dividends, a non-GAAP financial measure.

The following table presents reconciliations of book value per common share to book value per diluted common share plus accumulated dividends and other non-GAAP book value financial indicators:

	June 30, 2017		
	Equity Amount	Common Shares	Per Share Amount (a)
Book value per common share (b)	$3,811,431	79,518,581	$ 47.93
Non-GAAP Adjustments:			
Assumed exercise of outstanding stock options (c)(d)	614	26,136	
Unvested restricted shares	—	2,530,559	
Book value per diluted common share (e)	3,812,045	82,075,276	$ 46.45
Goodwill	(227,701)	—	
Intangible assets	(175,518)	—	
Tangible book value per diluted common share (e)	$3,408,826	82,075,276	$ 41.53
Book value per diluted common share (e)			$ 46.45
Accumulated dividends			12.32
Book value per diluted common share plus accumulated dividends (e)			$ 58.77

	December 31, 2016		
	Equity Amount	Common Shares	Per Share Amount (a)
Book value per common share (b)	$3,688,291	79,132,252	$ 46.61
Non-GAAP Adjustments:			
Assumed exercise of outstanding stock options (c)(d)	614	26,136	
Unvested restricted shares	—	2,868,610	
Book value per diluted common share (e)	3,688,905	82,026,998	$ 44.97
Goodwill	(196,758)	—	
Intangible assets	(115,592)	—	
Tangible book value per diluted common share (e)	$3,376,555	82,026,998	$ 41.16
Book value per diluted common share (e)			$ 44.97
Accumulated dividends			11.56
Book value per diluted common share plus accumulated dividends (e)			$ 56.53

(a) Per share amounts are calculated by dividing the equity amount by the common shares.

(b) The equity amount used in the calculation of book value per common share represents total shareholders' equity available to Validus excluding the liquidation value of the preferred shares.

(c) Using the “as-if-converted” method, assuming all proceeds received upon exercise of stock options will be retained by the Company and the resulting common shares from exercise remain outstanding.
(d) At June 30, 2017, the weighted average exercise price for those stock options that had an exercise price lower than book value per share was $23.48 (December 31, 2016: $23.48).
(e) Non-GAAP financial measure.

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Book value per common share, a GAAP financial measure, increased by $1.32, or 2.8%, from $46.61 at December 31, 2016 to $47.93 at June 30, 2017.

Book value per diluted common share plus accumulated dividends, a non-GAAP financial measure, is considered by management to be the key financial indicator of performance, as the Company believes growth in book value on a diluted basis, plus the dividends that have accumulated, ultimately translates into the return that a shareholder will receive. Book value per diluted common share plus accumulated dividends increased by $2.24, or 4.0%, from $56.53 at December 31, 2016 to $58.77 at June 30, 2017. Cash dividends per common share are an integral part of the value created for shareholders. During the six months ended June 30, 2017, the Company paid cash dividends of $0.76 (2016: $0.70) per common share.

Book value per diluted common share, a non-GAAP financial measure, is considered by management to be a measure of returns to common shareholders, as the Company believes growth in book value on a diluted basis ultimately translates into growth in stock price. Book value per diluted common share after dividends paid increased by $1.48, or 3.3%, from $44.97 at December 31, 2016 to $46.45 at June 30, 2017. Growth in book value per diluted common share inclusive of dividends paid was 5.0% and 6.6% for the six months ended June 30, 2017 and 2016, respectively.

Tangible book value per diluted common share, a non-GAAP financial measure, is considered by management to be a measure of returns to common shareholders excluding goodwill and other intangible assets, as the Company believes growth in tangible book value on a diluted basis ultimately translates into growth in the tangible value of the Company. Tangible book value per diluted common share increased by $0.37, or 0.9%, from $41.16 at December 31, 2016 to $41.53 at June 30, 2017.

Other financial indicators

In addition to presenting net income available to Validus common shareholders determined in accordance with U.S. GAAP, the Company believes that showing net operating income available to Validus common shareholders, a non-GAAP financial measure, provides investors with a valuable measure of profitability and enables investors, analysts, rating agencies and other users of its financial information to more easily analyze the Company's results in a manner similar to how management analyzes the Company's underlying business performance.

Net operating income available to Validus common shareholders is calculated by the addition or subtraction of certain Consolidated Statement of Income and Comprehensive Income line items from net income available to Validus common shareholders, the most directly comparable GAAP financial measure, as illustrated in the table below:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2017	2016	2017	2016
Net income available to Validus common shareholders	$101,095	$94,963	$195,656	$261,773
Non-GAAP Adjustments:				
Net realized gains on investments	(2,274)	(2,724)	(1,110)	(2,140)
Change in net unrealized gains on investments	(16,321)	(31,428)	(29,669)	(78,872)
(Income) loss from investment affiliates	(9,466)	589	(14,654)	4,702
Foreign exchange losses (gains)	7,329	(6,286)	5,760	(12,531)
Other income	(174)	(79)	(268)	(756)
Transaction expenses	4,427	—	4,427	—
Net income (loss) attributable to noncontrolling interests	2,102	(135)	2,830	102
Tax expense [(a)]	1,748	2,980	2,328	7,107
Net operating income available to Validus common shareholders [(b)]	$88,466	$57,880	$165,300	$179,385
Average shareholders' equity available to Validus common shareholders [(c)]	$3,786,654	$3,720,341	$3,753,866	$3,693,219
Annualized return on average equity	10.7%	10.2%	10.4%	14.2%
Annualized net operating return on average equity [(b)]	9.3%	6.2%	8.8%	9.7%

(a) Represents the tax expense or benefit associated with the specific country to which the pre-tax adjustment relates to. The tax impact is estimated by applying the statutory rates of applicable jurisdictions, after consideration of other relevant factors including the ability to utilize tax losses carried forward.

(b) Non-GAAP financial measure.

(c) Average shareholders’ equity for the three months ended is the average of the beginning and ending quarter end shareholders’ equity balances, excluding the liquidation value of the preferred shares.

Net operating income available to Validus common shareholders, a non-GAAP financial measure, measures the performance of the Company’s operations without the influence of gains or losses on investments and foreign currencies and other items as noted

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in the table above. The Company excludes these items from its calculation of net operating income available to Validus common shareholders because the amount of these gains and losses is heavily influenced by, and fluctuates in part, according to availability of investment market opportunities and other factors. The Company believes these amounts are largely independent of its core underwriting activities and including them distorts the analysis of trends in its operations. The Company believes the reporting of net operating income available to Validus common shareholders enhances the understanding of results by highlighting the underlying profitability of the Company's core (re)insurance operations. This profitability is influenced significantly by earned premium growth, adequacy of the Company's pricing, as well as loss frequency and severity. Over time it is also influenced by the Company's underwriting discipline, which seeks to manage exposure to loss through favorable risk selection and diversification, its management of claims, its use of reinsurance and its ability to manage its expense ratio, which it accomplishes through its management of acquisition costs and other underwriting expenses.

Return on average equity, a GAAP financial measure, and net operating return on average equity, a non-GAAP financial measure, represents the returns generated on common shareholders' equity during the year. The Company's objective is to generate superior returns on capital that appropriately reward shareholders for the risks assumed.

For further discussion of the components driving the Company's financial indicators refer to the "Results of Operations" sections.

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Second Quarter 2017 Results of Operations - Consolidated

The following table presents the results of operations for the three months ended June 30, 2017 and 2016:

	Three Months Ended June 30,	
	2017	2016
Revenues		
Gross premiums written	$792,902	$764,042
Reinsurance premiums ceded	(56,222)	(36,229)
Net premiums written	736,680	727,813
Change in unearned premiums	(105,653)	(154,090)
Net premiums earned	631,027	573,723
Net investment income	44,241	39,257
Net realized gains on investments	2,274	2,724
Change in net unrealized gains on investments	16,321	31,428
Income (loss) from investment affiliates	9,466	(589)
Other insurance related income and other income	1,339	824
Foreign exchange (losses) gains	(7,329)	6,286
Total revenues	697,339	653,653
Expenses		
Losses and loss expenses	296,149	307,130
Policy acquisition costs	117,268	107,966
General and administrative expenses	96,349	89,688
Share compensation expenses	11,146	10,727
Finance expenses	14,209	14,166
Transaction expenses	4,427	—
Total expenses	539,548	529,677
Income before taxes and (income) attributable to AlphaCat investors	157,791	123,976
Tax benefit (expense)	987	(1,706)
(Income) attributable to AlphaCat investors	(11,830)	(6,114)
Net income	$146,948	$116,156
Net (income) attributable to noncontrolling interests	(43,650)	(21,193)
Net income available to Validus	103,298	94,963
Dividends on preferred shares	(2,203)	—
Net income available to Validus common shareholders	$101,095	$94,963
Supplemental information:		
Losses and loss expenses:		
Current period excluding items below	$331,871	$284,704
Current period—notable loss events	—	36,915
Current period—non-notable loss events	7,568	48,292
Change in prior accident years	(43,290)	(62,781)
Total losses and loss expenses	$296,149	$307,130
Selected ratios:		
Ratio of net to gross premiums written	92.9 %	95.3 %
Losses and loss expense ratio:		
Current period excluding items below	52.6 %	49.6 %
Current period—notable loss events	— %	6.4 %
Current period—non-notable loss events	1.2 %	8.4 %
Change in prior accident years	(6.9)%	(10.9)%

Losses and loss expense ratio	46.9	%	53.5	%
Policy acquisition cost ratio	18.6	%	18.8	%
General and administrative expense ratio [(a)]	17.0	%	17.6	%
Expense ratio	35.6	%	36.4	%
Combined ratio	82.5	%	89.9	%

(a) The general and administrative expense ratio includes share compensation expenses.

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Highlights for the second quarter 2017 as compared to 2016 were as follows:

- Gross premiums written for the three months ended June 30, 2017 were $792.9 million compared to $764.0 million for the three months ended June 30, 2016, an increase of $28.9 million, or 3.8%. The increase was primarily driven by an increase in the Western World, Validus Re and AlphaCat segments and was partially offset by a decrease in the Talbot segment.
- Reinsurance premiums ceded for the three months ended June 30, 2017 were $56.2 million compared to $36.2 million for the three months ended June 30, 2016, an increase of $20.0 million, or 55.2%. The increase was primarily driven by an increase in the Western World and Validus Re segments.
- Losses and loss expenses for the three months ended June 30, 2017 were $296.1 million compared to $307.1 million for the three months ended June 30, 2016, a decrease of $11.0 million or 3.6%. The decrease was primarily driven by a decrease in notable and non-notable losses and was partially offset by lower favorable development on prior accident years.

Notable and Non-notable Loss Events

The Company defines a notable loss event as an event whereby consolidated net losses and loss expenses aggregate to a threshold greater than or equal to $30.0 million. The Company defines a non-notable loss event as an event whereby consolidated net losses and loss expenses aggregate to a threshold greater than or equal to $15.0 million but less than $30.0 million. The term “events” refers to aggregate notable and non-notable losses incurred.

Notable Loss Events

There were no notable loss events occurring during the three months ended June 30, 2017.

Losses and loss expenses from a single notable loss event occurring during the three months ended June 30, 2016 were as follows:

(Dollars in thousands)	Three Months Ended June 30, 2016 Notable Loss Event Canadian Wildfires
Net losses and loss expenses	$ 36,915
Less: Net losses and loss expenses attributable to AlphaCat third party investors and noncontrolling interests	(6,422)
Validus’ share of net losses and loss expenses	30,493
Less: Reinstatement premiums, net	(3,632)
Net loss attributable to Validus	$ 26,861

Losses and loss expenses from the Canadian Wildfires notable loss event were $36.9 million, or 6.4 percentage points of the loss ratio. Net of losses of $6.4 million attributable to AlphaCat third party investors and noncontrolling interests and reinstatement premiums of $3.6 million, the net loss attributable to the Company was $26.9 million.

Non-notable Loss Events

There were no non-notable loss events occurring during the three months ended June 30, 2017. During the three months ended June 30, 2017, the Company increased its loss estimate on a first quarter 2017 energy non-notable loss event by $7.6 million, or 1.2 percentage points of the loss ratio.

Losses and loss expenses from three non-notable loss events occurring during the three months ended June 30, 2016 were as follows:

	Three Months Ended June 30, 2016	
	Non-notable Loss Events	Total
(Dollars in thousands)		

	Texas Hailstorms	Kumamoto Earthquake	Jubilee Oil	
Net losses and loss expenses	$17,760	$ 15,318	$15,214	$48,292
Less: Net losses and loss expenses attributable to AlphaCat third party investors and noncontrolling interests	(5,535)	—	—	(5,535)
Validus' share of net losses and loss expenses	12,225	15,318	15,214	42,757
Less: Reinstatement premiums, net	(1,967)	—	(7,667)	(9,634)
Net loss attributable to Validus	$10,258	$ 15,318	$7,547	$33,123

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Losses and loss expenses from the three non-notable loss events were $48.3 million, or 8.4 percentage points of the loss ratio. Net of losses attributable to AlphaCat third party investors and noncontrolling interests of $5.5 million and reinstatement premiums of $9.6 million, the net loss attributable to the Company from these non-notable loss events was $33.1 million.

Change in prior accident years

Loss reserve development for the three months ended June 30, 2017 and 2016 was as follows:

(Dollars in thousands)	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016
Favorable development on event losses	$(5,069)	$(6,433)
Favorable development on attritional losses	(38,221)	(56,348)
Change in prior accident years	$(43,290)	$(62,781)

The favorable development for the three months ended June 30, 2017 and 2016 was primarily driven by favorable development on attritional losses.

Loss Ratios

The loss ratio for the three months ended June 30, 2017 and June 30, 2016 was 46.9% and 53.5%, respectively, a decrease of 6.6 percentage points.

Loss ratios by line of business for the three months ended June 30, 2017 and 2016 were as follows:

	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016
Property	35.2%	53.1%
Marine	14.1%	35.1%
Specialty	63.7%	61.0%
Liability	70.2%	66.1%
All lines	46.9%	53.5%

- Policy acquisition cost ratio for the three months ended June 30, 2017 was 18.6% compared to 18.8% for the three months ended June 30, 2016, a decrease of 0.2 percentage points.
- General and administrative ("G&A") expenses for the three months ended June 30, 2017 were $96.3 million compared to $89.7 million for the three months ended June 30, 2016, an increase of $6.7 million or 7.4%. The increase was primarily driven by an increase in G&A expenses in the Western World segment, which included $6.8 million of CRS expenses, of which $1.2 million related to the amortization of intangible assets acquired.
- Combined ratio for the three months ended June 30, 2017 and 2016 was 82.5% and 89.9%, respectively, a decrease of 7.4 percentage points.

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Second Quarter 2017 Results of Operations - Validus Re Segment

The following table presents underwriting income by line of business for the three months ended June 30, 2017 and 2016:

	Three Months Ended June 30,							
	2017				2016			
(Dollars in thousands)	Property	Marine	Specialty	Total	Property	Marine	Specialty	Total
Underwriting revenues								
Gross premiums written	$174,759	$14,557	$107,681	$296,997	$216,034	$7,806	$61,970	$285,810
Reinsurance premiums ceded	(4,227)	(38)	(7,122)	(11,387)	(8,892)	868	4,828	(3,196)
Net premiums written	170,532	14,519	100,559	285,610	207,142	8,674	66,798	282,614
Change in unearned premiums	(75,148)	15,275	14,870	(45,003)	(101,914)	22,423	43,999	(35,492)
Net premiums earned	95,384	29,794	115,429	240,607	105,228	31,097	110,797	247,122
Other insurance related income				58				150
Total underwriting revenues				240,665				247,272
Underwriting deductions								
Losses and loss expenses	32,750	(1,732)	73,667	104,685	51,856	6,921	73,362	132,139
Policy acquisition costs	17,359	5,246	24,553	47,158	18,269	5,281	19,014	42,564
Total underwriting deductions before G&A	50,109	3,514	98,220	151,843	70,125	12,202	92,376	174,703
Underwriting income before G&A	$45,275	$26,280	$17,209	$88,822	$35,103	$18,895	$18,421	$72,569
General and administrative expenses				19,274				17,872
Share compensation expenses				2,663				2,775
Total underwriting deductions				173,780				195,350
Underwriting income				$66,885				$51,922

Supplemental information:

Losses and loss expenses:								
Current period excluding items below	$28,360	$14,581	$77,275	$120,216	$21,361	$16,269	$75,046	$112,676
Current period—notable loss events	—	—	—	—	17,884	—	—	17,884
Current period—non-notable loss events	5,061	—	2,507	7,568	22,079	670	9,707	32,456
Change in prior accident years	(671)	(16,313)	(6,115)	(23,099)	(9,468)	(10,018)	(11,391)	(30,877)
Total losses and loss expenses	$32,750	$(1,732)	$73,667	$104,685	$51,856	$6,921	$73,362	$132,139
Selected ratios:								
Ratio of net to gross premiums written	97.6%	99.7%	93.4%	96.2%	95.9%	111.1%	107.8%	98.9%
Losses and loss expense ratio:								
Current period excluding items below	29.7%	49.0%	66.9%	50.0%	20.3%	52.3%	67.7%	45.7%
Current period—notable loss events	—%	—%	—%	—%	17.0%	—%	—%	7.2%
Current period—non-notable loss events	5.3%	—%	2.2%	3.1%	21.0%	2.2%	8.8%	13.1%
Change in prior accident years	(0.7)%	(54.8)%	(5.3)%	(9.6)%	(9.0)%	(32.2)%	(10.3)%	(12.5)%
Losses and loss expense ratio	34.3%	(5.8)%	63.8%	43.5%	49.3%	22.3%	66.2%	53.5%
Policy acquisition cost ratio	18.2%	17.6%	21.3%	19.6%	17.4%	17.0%	17.2%	17.2%
General and administrative expense ratio [(a)]				9.1%				8.4%
Expense ratio				28.7%				25.6%
Combined ratio				72.2%				79.1%

(a) The general and administrative expense ratio includes share compensation expenses.

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Highlights for the second quarter 2017 as compared to 2016 were as follows:

- Gross premiums written for the three months ended June 30, 2017 were $297.0 million compared to $285.8 million for the three months ended June 30, 2016, an increase of $11.2 million, or 3.9%. The increase in gross premiums written was driven by:
  An increase in the specialty lines of $45.7 million, primarily driven by new business in the casualty, composite and financial lines; and
  An increase in the marine lines of $6.8 million, primarily due to adjustments to existing business; partially offset by
  A decrease in the property lines of $41.3 million, primarily driven by reductions in participation and the non-renewal of various catastrophe programs due to market conditions.
- Reinsurance premiums ceded for the three months ended June 30, 2017 were $11.4 million compared to $3.2 million for the three months ended June 30, 2016, an increase of $8.2 million. The increase was primarily driven by an increase in the specialty lines of $12.0 million as a result of new non-proportional coverage purchased and adjustments to existing business and was partially offset by a decrease in the property lines of $4.7 million relating to the timing of certain reinsurance purchases.
- Net premiums earned for the three months ended June 30, 2017 were $240.6 million compared to $247.1 million for the three months ended June 30, 2016, a decrease of $6.5 million, or 2.6%.
- Losses and loss expenses for the three months ended June 30, 2017 were $104.7 million compared to $132.1 million for the three months ended June 30, 2016, a decrease of $27.5 million or 20.8%. The decrease was primarily driven by a decrease in notable and non-notable losses and was partially offset by lower favorable development on prior accident years.

Notable Loss Events

There were no notable loss events occurring during the three months ended June 30, 2017.

Losses and loss expenses from a single notable loss event occurring during the three months ended June 30, 2016 were as follows:

(Dollars in thousands)	Three Months Ended June 30, 2016 Notable Loss Event Canadian Wildfires
Validus Re’s share of net losses and loss expenses	$ 17,884
Less: Reinstatement premiums, net	(3,102)
Net loss attributable to Validus Re	$ 14,782

Losses and loss expenses from the Canadian Wildfires notable loss event were $17.9 million, or 7.2 percentage points of the loss ratio. Net of reinstatement premiums of $3.1 million, the net loss attributable to Validus Re was $14.8 million.

Non-notable Loss Events

There were no non-notable loss events occurring during the three months ended June 30, 2017. During the three months ended June 30, 2017, the Company increased its loss estimate on a first quarter 2017 energy non-notable loss event by $7.6 million, or 3.1 percentage points of the loss ratio.

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Losses and loss expenses from three non-notable loss events occurring during the three months ended June 30, 2016 were as follows:

(Dollars in thousands)	Three Months Ended June 30, 2016 Non-notable Loss Events Texas Hailstorms	Kumamoto Earthquake	Jubilee Oil	Total
Validus Re’s share of net losses and loss expenses	$6,884	$ 15,195	$10,377	$32,456
Less: Reinstatement premiums, net	(1,836)	—	(6,706)	(8,542)
Net loss attributable to Validus Re	$5,048	$ 15,195	$3,671	$23,914

Losses and loss expenses from the Texas Hailstorms, Kumamoto Earthquake and Jubilee Oil non-notable loss events were $32.5 million, or 13.1 percentage points of the loss ratio. Net of reinstatement premiums of $8.5 million, the net loss attributable to Validus Re was $23.9 million. The losses and loss expenses from the 2016 non-notable loss events by line of business were as follows:

- Texas Hailstorms and Kumamoto Earthquake - property lines of $22.1 million; and
- Jubilee Oil - marine and specialty lines of $0.7 million and $9.7 million, respectively.

Change in prior accident years

Loss reserve development by line of business for the three months ended June 30, 2017 and 2016 was as follows:

(Dollars in thousands)	Three Months Ended June 30, 2017 Property	Marine	Specialty	Total
(Favorable) adverse development on event losses	$(353)	$(6,115)	$6,235	$(233)
(Favorable) development on attritional losses	(318)	(10,198)	(12,350)	(22,866)
Change in prior accident years	$(671)	$(16,313)	$(6,115)	$(23,099)

The adverse development on event losses in the specialty lines was driven by additional reserves established on the second quarter 2016 non-notable loss event, Jubilee Oil, as a result of an increased industry loss estimate and was fully offset with favorable development in the marine lines relating to losses retroceded on the same event. The net favorable development across all lines was primarily driven by favorable development on attritional losses.

(Dollars in thousands)	Three Months Ended June 30, 2016 Property	Marine	Specialty	Total
(Favorable) adverse development on event losses	$(287)	$(11)	$2	$(296)
(Favorable) development on attritional losses	(9,181)	(10,007)	(11,393)	(30,581)
Change in prior accident years	$(9,468)	$(10,018)	$(11,391)	$(30,877)

The net favorable development across all lines was primarily driven by favorable development on attritional losses.

Loss Ratio

The loss ratio for the three months ended June 30, 2017 and June 30, 2016 was 43.5% and 53.5%, respectively, a decrease of 10.0 percentage points.

- Policy acquisition cost ratio for the three months ended June 30, 2017 was 19.6% compared to 17.2% for the three months ended June 30, 2016, an increase of 2.4 percentage points of the policy acquisition cost ratio. The increase was primarily driven by an increase in the specialty lines as a result of a change in business mix, notably an increase in casualty business which carries higher acquisition costs.
- General and administration expenses for the three months ended June 30, 2017 were $19.3 million compared to $17.9 million for the three months ended June 30, 2016, an increase of $1.4 million, or 7.8%, driven by a higher allocation of costs to the Validus Re segment.

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Second Quarter 2017 Results of Operations - Talbot Segment

The following table presents underwriting income by line of business for the three months ended June 30, 2017 and 2016:

	Three Months Ended June 30,							
	2017				2016			
(Dollars in thousands)	Property	Marine	Specialty	Total	Property	Marine	Specialty	Total
Underwriting revenues								
Gross premiums written	$88,525	$74,308	$99,644	$262,477	$111,646	$85,992	$98,429	$296,067
Reinsurance premiums ceded	(14,376)	(5,119)	(5,482)	(24,977)	(19,733)	(4,729)	(2,699)	(27,161)
Net premiums written	74,149	69,189	94,162	237,500	91,913	81,263	95,730	268,906
Change in unearned premiums	(16,408)	(15,570)	(13,648)	(45,626)	(37,054)	(7,341)	(22,962)	(67,357)
Net premiums earned	57,741	53,619	80,514	191,874	54,859	73,922	72,768	201,549
Other insurance related income				65				279
Total underwriting revenues				191,939				201,828
Underwriting deductions								
Losses and loss expenses	39,222	13,529	40,638	93,389	40,856	29,922	38,532	109,310
Policy acquisition costs	10,269	14,514	19,522	44,305	9,057	17,582	16,974	43,613
Total underwriting deductions before G&A	49,491	28,043	60,160	137,694	49,913	47,504	55,506	152,923
Underwriting income before G&A	$8,250	$25,576	$20,354	$54,245	$4,946	$26,418	$17,262	$48,905
General and administrative expenses				35,582				39,061
Share compensation expenses				3,155				3,270
Total underwriting deductions				176,431				195,254
Underwriting income				$15,508				$6,574

Supplemental information:

Losses and loss expenses:								
Current period excluding items below	$44,116	$30,585	$34,564	$109,265	$34,973	$34,013	$47,838	$116,824
Current period—notable loss events	—	—	—	—	11,703	—	—	11,703
Current period—non-notable loss events	—	—	—	—	4,274	4,837	—	9,111
Change in prior accident years	(4,894)	(17,056)	6,074	(15,876)	(10,094)	(8,928)	(9,306)	(28,328)
Total losses and loss expenses	$39,222	$13,529	$40,638	$93,389	$40,856	$29,922	$38,532	$109,310
Selected ratios:								
Ratio of net to gross premiums written	83.8 %	93.1 %	94.5 %	90.5 %	82.3 %	94.5 %	97.3 %	90.8 %
Losses and loss expense ratio:								
Current period excluding items below	76.4 %	57.0 %	43.0 %	57.0 %	63.8 %	46.1 %	65.8 %	58.0 %
Current period—notable loss events	— %	— %	— %	— %	21.3 %	— %	— %	5.8 %
Current period—non-notable loss events	— %	— %	— %	— %	7.8 %	6.5 %	— %	4.5 %
Change in prior accident years	(8.5)%	(31.8)%	7.5 %	(8.3)%	(18.4)%	(12.1)%	(12.8)%	(14.1)%
Losses and loss expense ratio	67.9 %	25.2 %	50.5 %	48.7 %	74.5 %	40.5 %	53.0 %	54.2 %
Policy acquisition cost ratio	17.8 %	27.1 %	24.2 %	23.1 %	16.5 %	23.8 %	23.3 %	21.6 %
General and administrative expense ratio [(a)]				20.2 %				21.1 %
Expense ratio				43.3 %				42.7 %
Combined ratio				92.0 %				96.9 %

(a) The general and administrative expense ratio includes share compensation expenses.

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Highlights for the second quarter 2017 as compared to 2016 were as follows:

- Gross premiums written for the three months ended June 30, 2017 were $262.5 million compared to $296.1 million for the three months ended June 30, 2016, a decrease of $33.6 million, or 11.3%. The decrease in gross premiums written was driven by:
  Decreases in the property and marine lines of $23.1 million and $11.7 million, respectively, driven by reductions in participation and non-renewals on various programs due to the current rate environment and adjustments to existing business; partially offset by
  An increase in the specialty lines of $1.2 million.
- Reinsurance premiums ceded for the three months ended June 30, 2017 were $25.0 million compared to $27.2 million for the three months ended June 30, 2016, a decrease of $2.2 million, or 8.0%.
- Net premiums earned for the three months ended June 30, 2017 were $191.9 million compared to $201.5 million for the three months ended June 30, 2016, a decrease of $9.7 million, or 4.8%.
- Losses and loss expenses for the three months ended June 30, 2017 were $93.4 million compared to $109.3 million for the three months ended June 30, 2016, a decrease of $15.9 million or 14.6%. The decrease was primarily driven by a decrease in notable and non-notable losses and was partially offset by lower favorable development on prior accident years.

Notable Loss Events

There were no notable loss events occurring during the three months ended June 30, 2017.

Losses and loss expenses from a single notable loss event occurring during the three months ended June 30, 2016 were as follows:

(Dollars in thousands)	Three Months Ended June 30, 2016 Notable Loss Event Canadian Wildfires
Talbot’s share of net losses and loss expenses	$ 11,703
Less: Reinstatement premiums, net	(530)
Net loss attributable to Talbot	$ 11,173

Losses and loss expenses from the Canadian Wildfires notable loss event were $11.7 million, or 5.8 percentage points of the loss ratio. Net of reinstatement premiums of $0.5 million, the net loss attributable to Talbot was $11.2 million.

Non-notable Loss Events

There were no non-notable loss events occurring during the three months ended June 30, 2017.

Losses and loss expenses from three non-notable loss events occurring during the three months ended June 30, 2016 were as follows:

Three Months Ended June 30, 2016