XL GROUP PLC
Form 10-K
February 27, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2011

OR

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

For the transition period from _____ to _____

Commission file number 1-10804

XL GROUP
Public Limited Company

(Exact name of registrant as specified in its charter)

Ireland	98-0665416
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
No. 1 Hatch Street Upper, 4th Floor, Dublin 2, Ireland	+353 (1) 405-2033
(Address of principal executive offices and zip code)	(Registrant s telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class	Name of each exchange on which registered
Ordinary Shares, Par Value $0.01 per Share	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No x

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 (§232.405 of this chapter) during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company 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

The aggregate market value of the voting common equity of the registrant held by non-affiliates of the registrant on June 30, 2011 was approximately $6.7 billion computed upon the basis of the closing sales price of the Ordinary Shares on June 30, 2011. For purposes of this computation, ordinary shares held by directors and officers of the registrant have been excluded. Such exclusion is not intended, nor shall it be deemed, to be an admission that such persons are affiliates of the registrant.

As of February 23, 2012, there were outstanding 315,666,944 Ordinary Shares, $0.01 par value per share, of the registrant.

Documents Incorporated by Reference

Portions of the Registrant s Definitive Proxy Statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A not later than 120 days after the end of the fiscal year covered by this report relating to the annual meeting of ordinary shareholders to be held on April 27, 2012 are incorporated by reference into Part III of this Form 10-K.

XL GROUP PLC

TABLE OF CONTENTS

This Annual Report on Form 10-K contains Forward-Looking Statements as defined in the Private Securities Litigation Reform Act of 1995. A non-exclusive list of the important factors that could cause actual results to differ materially from those in such Forward-Looking Statements is set forth herein under Item 1A, Risk Factors, and Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, under the caption Cautionary Note Regarding Forward-Looking Statements.

PART I

ITEM 1. BUSINESS

History

XL Group plc, through its subsidiaries, is a global insurance and reinsurance company providing property, casualty and specialty products to industrial, commercial and professional firms, insurance companies and other enterprises on a worldwide basis. The company was incorporated with limited liability under the Cayman Islands Companies Act on March 16, 1998, as EXEL Merger Company. XL Capital Ltd was formed as a result of the merger of EXEL Limited and Mid Ocean Limited on August 7, 1998, and the company was named EXEL Limited on that date. At a special general meeting held on February 1, 1999, the shareholders of EXEL Limited approved a resolution changing the name of the company to XL Capital Ltd.

EXEL Limited and Mid Ocean Limited were incorporated in the Cayman Islands with principal operations in Bermuda in 1986 and 1992, respectively. EXEL Limited and its subsidiaries were formed in response to a shortage of high excess liability underwriting capacity in the insurance industry at that time and included a subsidiary organized in Ireland to serve the European Community. Mid Ocean Limited and its subsidiaries were formed to capitalize on the supply/demand imbalance in the global property catastrophe reinsurance market at that time and included dedicated Lloyd s syndicate capacity. On June 18, 1999, XL Capital Ltd merged with NAC Re Corp. (NAC), a Delaware corporation organized in 1985, in a stock merger.

On July 25, 2001, the company acquired certain Winterthur International insurance operations (Winterthur International) to extend its predominantly North American-based large corporate insurance business globally.

Effective January 1, 2002, the company increased its shareholding in Le Mans Ré from 49% to 67% in order to expand its international reinsurance operations. On September 3, 2003, the company exercised its option to buy the remaining 33% from Les Mutuelles du Mans Assurances (MMA) and changed the name of Le Mans Ré to XL Re Europe S.A. On October 18, 2006, the company received approval to form a new European company, XL Re Europe Ltd, based in Dublin, Ireland, which is licensed to write all classes of reinsurance business. XL Re Europe Ltd is the headquarters of the company s European reinsurance platform with branch offices in France and the United Kingdom (the U.K.).

On August 4, 2006, the company completed the sale of approximately 37% of its then financial guarantee reinsurance and insurance businesses through an initial public offering of 23.4 million common shares of Syncora Holdings Ltd. (Syncora) (formerly Security Capital Assurance Ltd. or SCA). On June 6, 2007, the company completed the sale of an additional portion of Syncora s common shares still owned by the company through a secondary offering and thereby reduced its ownership of Syncora s outstanding common shares further from approximately 63% to approximately 46%. On August 5, 2008, the company closed an agreement (the Master Agreement) with Syncora and its subsidiaries, as well as certain counterparties to credit default swap agreements, in connection with the termination of certain reinsurance and other agreements. As part of the Master Agreement, the company transferred all of the shares it owned in Syncora to a trust and, as a result, has no further ownership interest in the company.

On July 1, 2010, XL Group plc, a newly formed Irish public limited company (XL-Ireland) and XL Capital Ltd (now known as XLIT Ltd.), an exempted company organized under the laws of the Cayman Islands (XL-Cayman), completed a redomestication transaction in which all of the ordinary shares of XL-Cayman were exchanged for all of the ordinary shares of XL-Ireland (the Redomestication). As a result, XL-Cayman became a wholly-owned subsidiary of XL-Ireland. On July 23, 2010, the Irish High Court approved XL-Ireland s creation of distributable reserves, subject to the completion of certain formalities under Irish Company law. These formalities were completed in early August 2010. For further detailed information on this transaction and its impacts on shareholder rights, shareholders equity, debt and notes then outstanding and employee stock plan awards, see the company s Report on Form 8-K filed with the U.S. Securities and Exchange Commission on July 1, 2010. In addition, on July 1, 2010, XL Capital Ltd changed its name to XL Group Ltd., and in November 2011, changed its name to XLIT Ltd.

For periods prior to July 1, 2010, unless the context otherwise indicates, references herein to the Company are to, and the Consolidated Financial Statements herein include the accounts of XL-Cayman and its consolidated subsidiaries. For periods on and subsequent to July 1, 2010, unless the context otherwise indicates, references herein to the Company are to, and the Consolidated Financial Statements herein include, the accounts of XL-Ireland and its consolidated subsidiaries.

See further information under Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations.

SEGMENTS

Following the streamlining of the Company s operating segments in the first quarter of 2009, the Company is organized into three operating segments: Insurance, Reinsurance and Life operations. The general investment and financing operations of the Company are reflected in Corporate.

The Company evaluates the performance of both the Insurance and Reinsurance segments based on underwriting profit and the performance of the Life operations segment based on its contribution to net income. Other items of revenue and expenditure of the Company are not evaluated at the segment level for reporting purposes. In addition, the Company does not allocate investment assets of its property and casualty (P&C) operations to the other segments. Investment assets related to the Company s Life operations and certain structured products included in the Insurance and Reinsurance segments are held in separately identified portfolios. As such, net investment income from these assets is included in the contribution from each of these operations.

The following table sets forth an analysis of gross premiums written by segment for the years ended December 31, 2011, 2010 and 2009. Additional financial information about the Company s segments, including financial information about geographic areas, is included in Item 8, Note 4 to the Consolidated Financial Statements, Segment Information.

Year ended December 31 *(U.S. dollars in thousands)*	**2011 Gross Premiums Written**	**Percentage Change**	**2010 Gross Premiums Written**	**Percentage Change**	**2009 Gross Premiums Written**
Insurance	$ 4,824,665	9.2%	$ 4,418,380	3.9%	$ 4,251,888
Reinsurance	2,073,619	12.5%	1,842,951	(0.9)%	1,859,423
Life operations	394,555	(4.2)%	411,938	(28.5)%	576,162
	$ 7,292,839	9.3%	$ 6,673,269	(0.2)%	$ 6,687,473

Insurance Segment

General

In October 2009, the Company s insurance operations were reorganized into four business units: International Property and Casualty (IPC), North America Property and Casualty (NAPC), Global Professional (Professional) and Global Specialty Lines (Specialty). The Company operated under its product and geography based matrix business structure until October 2009.

The insurance operations market and distribute coverage through a wide variety of local, national and international producers and provide customized insurance policies for complex corporate risks that may require large limits. Large deductibles and self-insured retentions are incorporated into these policies to further manage risk along with stringent underwriting guidelines. While the insurance segment is known for insuring large complex risk, certain of its products are targeted to small and midsize companies and organizations - for example, professional liability and program business. The Company focuses on those lines of business that it believes will provide the best return on capital over time.

The segment s most significant operating legal entities in 2011 based on revenues were as follows: XL Insurance (Bermuda) Ltd, XL Insurance Company Limited, XL Specialty Insurance Company, Indian Harbor Insurance Company, Greenwich Insurance Company and XL Insurance America, Inc., as well as certain Lloyd s syndicates.

The excess nature of many of the Company s insurance products, coupled with historically large policy limits, results in a book of business that can have losses characterized as low frequency and high severity. As a result, large losses, though infrequent, can have a significant impact on the Company s results of operations, financial condition and liquidity. The Company attempts to mitigate this risk by, among other things, using strict underwriting guidelines, effective risk management practices (e.g., monitoring of aggregate exposures) and various reinsurance arrangements, discussed below.

International Property and Casualty

IPC includes the following lines of business: property, primary and excess casualty, environmental liability and upper middle markets (UMM).

Property and casualty products are typically written as global insurance programs for large multinational companies and institutions and include property and liability coverages. Property and casualty products generally provide large capacity on a primary, quota share or excess of loss basis. Global insurance programs are targeted to large multinational companies in major industry groups including aerospace, automotive, consumer products, pharmaceutical, pulp and paper, high technology, telecommunications, transportation and basic metals. The primary casualty programs generally require customers to take large deductibles or self-insured retentions. For the excess business, the Company s liability attaches after large deductibles, including self insurance or insurance layers provided by other companies. Policies are written on an occurrence, claims-made and occurrence reported basis. The

Company s property business, which also includes construction projects, is short-tail by nature and written on both a primary and excess of loss basis. Property business includes exposures to man-made and natural disasters, and generally, loss experience is characterized as low frequency and high severity.

Environmental liability products include pollution and remediation legal liability, general and project-specific pollution and professional liability, and commercial general property redevelopment and contractor s pollution liability. Business is written for both single and multiple years on a primary or excess of loss, claims-made or, less frequently, occurrence basis. Targeted industries include environmental service firms, contractors, healthcare facilities, manufacturing facilities, real estate redevelopment, transportation and construction.

North America Property and Casualty

NAPC includes the following lines of business: property, primary and excess casualty, environmental liability, excess and surplus lines, construction, surety and program business.

In addition to the property, casualty, environmental and UMM products described under IPC, the NAPC business unit also includes 100% property products for the large account risk engineered markets and general liability, U.S. workers compensation and auto liability for the risk management accounts, which require customers to take large deductibles or self-insured retentions.

Excess and surplus lines products include general liability and property coverages where most Insurance Services Office, Inc. (ISO) products are written. Targets include a variety of classes with focus on one-off risks generated from a limited number of contracted wholesale brokers.

Construction products include property coverages (builders risk, contractors equipment, property and inland marine), general liability, U.S. workers compensation and commercial auto, as well as professional liability for contractors and owner, excess umbrella, subcontractor default insurance and primary casualty wrap ups.

Surety products include contract bonds, including bid, performance, payment, and contractor qualification bonds, as well as commercial surety bonds, including appeal, court and qualification bonds. Products in general provide large capacity and are written on a sole surety, co-surety or shared surety basis.

The Company s program business specializes in insurance coverages for distinct market segments in North America, including program administrators and managing general agents who operate in a specialized market niche and have unique industry backgrounds or specialized underwriting capabilities. Products encompass mostly property and casualty coverages.

Global Professional Lines

Professional includes directors and officers liability, errors and omissions liability and employment practices liability coverages. Policies are written on both a primary and excess of loss basis. Directors and officers coverage includes primary and excess directors and officers liability, employment practices liability and company securities and private company directors and officers liability. Products are targeted at a variety of different sized companies, with a heavy concentration on small to medium-sized firms when written on a primary basis. Employment practices liability is written primarily for very large corporations on an excess of loss basis and covers those firms for legal liability in regard to the treatment of employees. Errors and omissions coverage is written on a primary and excess basis.

Errors and omissions insurance written on a primary basis is targeted to small and medium-sized firms and coverage is provided for various professional exposures, including, but not limited to, architects and engineers, insurance brokers, consultants, lawyers, public entities and real estate agents.

Global Specialty Lines

Specialty includes the following lines of business: aviation and satellite, marine and offshore energy, fine art and specie, equine, product recall, political risk and North America inland marine.

Aviation and satellite products include comprehensive airline hull and liability, airport liability, aviation manufacturers product liability, aviation ground handler liability, large aircraft hull and liability, corporate non-owned aircraft liability, space third party liability and satellite risk including damage or malfunction during ascent to orbit and continual operation, and aviation war. Aviation liability and physical damage coverage is offered for large aviation risks on a proportional basis, while smaller general aviation risks are offered on a primary basis. Satellite risks are generally written on a proportional basis. The target markets for aviation and satellite products include airlines, aviation product manufacturers, aircraft service firms, general aviation operators and telecommunications firms.

Marine and offshore energy coverage includes marine hull and machinery, marine war, marine excess liability, cargo and offshore energy insurance. Fine art and specie coverages include fine art and other collections, jewelers block, cash in transit and related coverages for financial institutions. Equine products specialize in providing bloodstock and livestock insurance. Product recall coverages include product contamination for the food and beverage sector and end-product consumer goods and product guarantee aimed at component part manufacturers.

In 2011, the Company launched underwriting capabilities for political risk and North America inland marine business.

Also included as part of the Insurance segment is XL Global Asset Protection Services (XL GAPS), a fee for service loss prevention consulting service that offers individually tailored risk management solutions to risk managers, insurance brokers and insurance company clients operating on a global basis. Services are offered on an unbundled (services not tied to an insurance contract) and bundled basis.

Underwriting

The Company underwrites and prices most risks individually following a review of the exposure and in accordance with the Company s underwriting guidelines. Most of the Company s insurance operations have underwriting guidelines that are industry-specific. The Company seeks to serve its clients while controlling its exposure on individual insurance contracts through terms and conditions, policy limits and sublimits, attachment points, and facultative and treaty reinsurance arrangements on certain types of risks.

The Company s underwriters generally evaluate each industry category and subgroups within each category. Premiums are set and adjusted for an insured based, in large part, on the industry group in which the insured is placed and the insured s perceived risk relative to the other risks in that group. Rates may vary significantly according to the industry group of the insured as well as the insured s risk relative to the group. The Company s rating methodology for individual insureds seeks to set premiums in accordance with claims potential as measured by past experience and future expectations, the attachment point and amount of underlying insurance, the nature and scope of the insured s operations, exposures to loss, including natural hazard exposures, risk management quality and other specific risk factors relevant in the judgment of the Company s underwriters to the type of business being written.

Underwriting and loss experience is reviewed regularly for, among other things, loss trends, emerging exposures, changes in the regulatory or legal environment as well as the efficacy of policy terms and conditions.

As the Company s insurance products are primarily specialized coverages, underwriting guidelines and policy forms differ by product offering as well as by legal jurisdiction. Liability insurance is written on both a primary and excess of loss basis, on occurrence, occurrence reported and claims-made policy forms. Occurrence reported policies typically cover occurrences causing unexpected and unintended personal injury or property damage to third parties arising from events or conditions that commence at or subsequent to an inception date, or retroactive date, if applicable, and prior to the expiration of the policy provided that proper notice is given during the term of the policy or the discovery period. Claims-made policies typically cover only claims made during the policy period or extended reporting period and are generally associated with professional liability and environmental coverages. Traditional occurrence coverage is also available for restricted classes of risk and is generally written on a follow-form basis for excess of loss coverage, where the policy adopts the terms, conditions and exclusions of the underlying policy. Property insurance risks are written on a lead or follow-form basis that usually provides coverage for all risks of physical damage and business interruption. Maximum limits are generally subject to sublimits for coverage in critical earthquake and flood zones, where the Company seeks to limit its liability in these areas.

Engineering

Property engineering for the insurance operations includes conducting on-site inspections and consulting services related to loss prevention, reviews of building plans for fire protection design, Computer Assisted Drawings (diagrams) of facilities, recommendations on how to improve site protection, reviews of existing loss prevention reports/information for underwriters, summarizing multiple sources of information into an account summary, and providing underwriters an opinion on the risk to assist with risk selection, pricing and other underwriting decisions. The property engineering team consists of staff located in 22 countries.

Other engineering resources support casualty, environmental, specialty and construction lines and serve as internal consultants to their respective underwriting teams, assisting them with making underwriting decisions, as well as helping their customers improve their local site or account protection.

Reinsurance Ceded

In certain cases, the risks assumed by the Company in the Insurance segment are partially reinsured by third party reinsurers. Reinsurance ceded varies by location and line of business based on a number of factors, including market conditions. The benefits of ceding risks to third party reinsurers include reducing exposure on individual risks, protecting against catastrophic risks, maintaining acceptable capital ratios and enabling the writing of additional business. Reinsurance ceded does not legally discharge the Company from its liabilities to the original policyholder in respect of the risk being reinsured.

The Company uses reinsurance to support the underwriting and retention guidelines of each of its subsidiaries as well as to control the aggregate exposure of the Company to a particular risk or class of risks. Reinsurance is purchased at several levels ranging from reinsurance of risks assumed on individual contracts to reinsurance covering the aggregate exposure on a portfolio of policies issued by groups of companies. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, for further information.

Premiums

Premium rates and underwriting terms and conditions for all lines of business written vary by jurisdiction principally due to local market conditions, competitor product offerings and legal requirements.

The following table provides an analysis of gross premiums written, net premiums written and net premiums earned for the Insurance segment for the three years ended December 31:

	2011			2010			2009 (1)		
(U.S. dollars in thousands)	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned
Casualty professional lines	$ 1,377,560	$ 1,278,723	$ 1,287,230	$ 1,412,131	$ 1,306,441	$ 1,316,173	$ 1,423,756	$ 1,336,541	$ 1,276,005
Casualty other lines	1,158,493	714,184	695,094	1,030,877	650,717	632,737	947,121	570,887	655,126
Other property	896,794	534,799	481,148	699,442	414,251	416,917	649,592	361,841	426,441
Marine, energy, aviation, and satellite	657,898	544,499	528,454	668,878	570,957	540,319	644,898	516,408	546,806
Other specialty lines (2)	734,194	636,047	665,727	602,787	519,557	606,682	577,804	483,166	634,436
Other (3)	(404)	(718)	3,552	(2,545)	(7,582)	1,554	5,257	1,077	12,217
Structured indemnity	130	130	2,522	6,810	6,809	14,756	3,460	3,460	8,762
Total	$ 4,824,665	$ 3,707,664	$ 3,663,727	$ 4,418,380	$ 3,461,150	$ 3,529,138	$ 4,251,888	$ 3,273,380	$ 3,559,793

(1) Certain reclassifications have been made to conform to current year presentation.
(2) Other specialty lines within the Insurance segment includes: environmental, programs, equine, warranty, specie, middle markets and excess and surplus lines.
(3) Other includes credit and surety and other lines.

Competition

The Company competes globally in the property and casualty insurance markets. Its competitors include the following companies and their affiliates: The ACE Group of Companies (ACE); Allianz Aktiengesellschaft (Allianz); American International Group, Inc., primarily their Chartis subsidiary (AIG); Factory Mutual Global (FMG) for property only; Hartford Financial Services (Hartford); Lloyd s of London Syndicates (Lloyd s); The Chubb Corporation (Chubb); The Travelers Companies (Travelers); and Zurich Financial Services Group (Zurich).

The Company s major geographical markets for its property and casualty insurance operations are North America, Europe and Bermuda. The Company s main competitors in each of these markets include the following:

North America AIG, ACE, Chubb, FMG, Zurich, Travelers, CNA Financial Corporation, Hartford, Liberty Mutual Group, Arch Capital Group Ltd (Arch) and Lloyd s.

Europe Allianz, AIG, FMG, Zurich, AXA Insurance Ltd. (AXA), ACE, Lloyd s, Assicurazioni Generali (Generali) and HDI-Gerling Industrie Versicherung AG (HDI-Gerling).

Bermuda ACE, Allied World Assurance Company (AWAC), Axis Capital Group (Axis), Alterra Capital (Alterra), Endurance Specialty Insurance Ltd (Endurance) and Arch.

Marketing and Distribution

The majority of Insurance segment business originates via a large number of international, national and regional producers, acting as the brokers and representatives of current and prospective policyholders. This channel is supported by the Company s Global Distribution and Network Unit, which consists of sales and marketing representatives in key markets throughout the world, representing all of the Company s products in collaboration with the four business units. A portion of Insurance segment business is also marketed and underwritten by general agents and a portion by independent agents acting on behalf of the Company. Typically, all such producers, general agents and independent agents receive commission payments from the Company for their services, which payments are calculated as a percentage of the gross premium paid by the policyholder on an account-by-account basis. A certain portion of business originating from producers is submitted on a fee basis under which the producer is compensated by a fee paid to it by its policyholder client. From time to time, the Company also considers requests for commissions from a producer, with disclosure by the producer to the policyholder-client, where the producer receives a fee from the policyholder-client. The Company evaluates such requests on a case-by-case basis.

The Company considers requests for contingent commission arrangements where such additional commissions are based upon the volume of bound business originated from a specific producer during a prior calendar year where legal and appropriate. Such arrangements are distinct from program business where additional commissions are generally based on profitability of business submitted to and bound by the Company.

With regard to excess and surplus lines business, the Company receives submissions from licensed wholesale surplus lines brokers.

The Company has no implied or explicit commitments to accept business from any particular broker, and neither producers nor any other third party have the authority to bind the Company, except in the case where underwriting authority may be delegated contractually to selected general agents. Such general agents are subject to a financial and operational due diligence review prior to any such delegation of authority and ongoing reviews and audits are carried out as deemed necessary by the Company with the goal of assuring the continuing integrity of underwriting and related business operations. See Item 8, Note 17(a) to the Consolidated Financial Statements for information on the Company s major producers, Commitments and Contingencies Concentrations of Credit Risk.

Apart from compensation arrangements established with producers in connection with insurance transactions, the Company also has engaged, and may in the future engage, certain producers or their affiliates in consulting roles pursuant to which such producers provide access to certain systems and information that may assist the Company with its marketing and distribution strategy. In instances where the Company engages producers in such consulting roles, the Company may compensate the relevant producers on a fixed fee basis, a variable fee basis based upon Company usage of the systems and information proffered, or through a combination of fixed and variable fees.

Claims Administration

Claims management for the insurance operations includes the review of initial loss reports, administration of claims databases, generation of appropriate responses to claims reports, identification and handling of coverage issues, determination of whether further investigation is required and, where appropriate, retention of claims counsel, establishment of case reserves, payment of claims and notification to reinsurers. With respect to the establishment of case reserves, when the Company is notified of insured losses, claims personnel record a case reserve as appropriate for the estimated amount of the exposure at that time. The estimate reflects the judgment of claims personnel based on general reserving practices, the experience and knowledge of such personnel regarding the nature of the specific claim and, where appropriate, advice of counsel. Reserves are also established to provide for the estimated expense of settling claims, including legal and other fees and the general expenses of administering the claims adjustment process.

Claims in respect of business written by the Company s Lloyd s syndicates are primarily notified by various central market bureaus. Where a syndicate is a leading syndicate on a Lloyd s policy, its underwriters and claims adjusters will work directly with the broker or insured on behalf of itself and the following market for any particular claim. This may involve appointing attorneys or loss adjusters. The claims bureaus and the leading syndicate advise movement in loss reserves to all syndicates participating on the risk. The Company s claims department may adjust the case reserves it records from those advised by the bureaus as deemed necessary.

Certain of the Company s product lines have arrangements with third party administrators to provide claims handling services to the Company in respect of such product lines. These agreements set forth the duties of the third party administrators, limits of authority, protective indemnification language and various procedures that are required to meet statutory compliance. These arrangements are also subject to audit review by the Company s relevant claim department.

In February 2010, the insurance operations started deploying a new claims IT platform called XL GlobalClaim (GCS). The system was successfully deployed throughout the Company in 2011. GCS converts the claim operation to a paperless environment and connects the legacy systems to allow for consistent data aggregation for all global claims operations.

Reinsurance Segment

General

The Company s Reinsurance segment is structured geographically into Bermuda operations, North American operations, European/Asia Pacific operations and Latin American operations.

The segment provides casualty, property risk, property catastrophe, marine, aviation, treaty and other specialty reinsurance on a global basis with business being written on both a proportional and non-proportional basis and also on a facultative basis. Given challenging market conditions and the changing economic environment that was experienced since 2008, the Company s lines of business within its reinsurance operations continued to focus on those that provide the best return on capital. For the Company s Reinsurance segment, this resulted, in certain instances, in a greater emphasis being placed on short-tail lines of business.

Business written on a non-proportional basis generally provides for an indemnification by the Company to the ceding company for a portion of losses, both individually and in the aggregate, on policies with limits in excess of a specified individual or aggregate loss deductible. For business written on a proportional basis, including quota share or surplus basis, the Company receives an agreed percentage of the premium and is liable for the same percentage of each and all incurred loss. For proportional business, the ceding company normally receives a ceding commission for the premiums ceded and may also, under certain circumstances, receive a profit commission based on performance of the contract. Occasionally this commission could be on a sliding scale depending on the loss ratio performance of the contract. The Company s casualty reinsurance includes general liability, professional liability, automobile and workers compensation. Professional liability includes directors and officers , employment practices, medical malpractice and environmental liability. Casualty lines are written as treaties or programs and on both a proportional and a non-proportional basis. The treaty business includes clash programs, which cover a number of underlying policies involved in one occurrence or a judgment above an underlying policy s limit, before suffering a loss.

The Company s property business, primarily short-tail in nature, is written on both a portfolio/treaty and individual/facultative basis and includes property catastrophe, property risk excess of loss and property proportional. A significant portion of the property business underwritten consists of large aggregate exposures to man-made and natural disasters and, generally, loss experience is characterized as low frequency and high severity. This may result in volatility in the Company s results of operations, financial condition and liquidity. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations.

The Company seeks to manage its reinsurance exposures to catastrophic events by limiting the amount of exposure written in each geographic or peril zone worldwide, underwriting in excess of varying attachment points and requiring that contracts exposed to catastrophe loss include aggregate limits. The Company also seeks to protect its total aggregate exposures by peril and zone through the purchase of reinsurance programs.

The Company s property catastrophe reinsurance account is generally all risk in nature. As a result, the Company is exposed to losses from sources as diverse as hurricanes and other windstorms, earthquakes, freezing, riots, floods, industrial explosions, fires, and many other potential natural or man-made disasters. In accordance with market practice, the Company s policies generally exclude certain risks such as war, nuclear contamination or radiation. Following the terrorist attacks at the World Trade Center in New York City, Washington, D.C. and Pennsylvania on September 11, 2001 (collectively, the September 11 event), terrorism cover, including, nuclear, biological, radiological and chemical, or NBRC , has been restricted or excluded in many territories and classes. Some U.S. states require some cover for Fire Following terrorism and some countries make terrorism coverage mandatory. The Company s predominant exposure under such coverage is to property damage.

Property catastrophe reinsurance provides coverage on an excess of loss basis when aggregate losses and loss adjustment expenses from a single occurrence of a covered event exceed the attachment point specified in the policy. Some of the Company s property catastrophe contracts limit coverage to one occurrence in any single policy year, but most contracts generally enable at least one reinstatement to be purchased by the reinsured.

The Company also writes property risk excess of loss reinsurance. Property risk excess of loss reinsurance covers a loss to the reinsured on a single risk of the type reinsured rather than to aggregate losses for all covered risks on a specific peril, as is the case with catastrophe reinsurance. The Company s property proportional account includes reinsurance of direct property insurance. The Company seeks to limit the catastrophe exposure from its proportional and per risk excess business through extensive use of occurrence and cession limits.

Other specialty reinsurance products include energy, marine, aviation, space, engineering, fidelity, trade credit and political risk. The Company underwrites a small portfolio of contracts covering political risk and trade credit. Exposure is assumed from a limited number of trade credit contracts.

The segment s most significant operating legal entities in 2011 based on revenues were as follows: XL Reinsurance America Inc., XL Re Europe Limited, XL Re Ltd and XL Re Latin America Ltd.

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Underwriting

Underwriting risks for the reinsurance property and casualty business are evaluated using a number of factors including, but not limited to, the type and layer of risk to be assumed, the actuarial evaluation of premium adequacy, the cedant s underwriting and claims experience, the cedant s financial condition and claims paying rating, the exposure and/or experience with the cedant, and the line of business to be reinsured.

Other factors assessed by the Company include the reputation of the proposed cedant, the geographic area in which the cedant does business and its market share, a detailed evaluation of catastrophe and risk exposures, and historical loss data for the cedant where available and for the industry as a whole in the relevant regions in order to compare the cedant s historical loss experience to industry averages. On-site underwriting and claim reviews are performed where it is deemed necessary to determine the quality of a current or prospective cedant s underwriting operations, with particular emphasis on casualty proportional and working excess of loss placements.

For property catastrophe reinsurance business, the Company s underwriting guidelines generally limit the amount of exposure it will directly underwrite for any one reinsured and the amount of the aggregate exposure to catastrophic losses in any one geographic zone. The Company believes that it has defined geographic and peril zones such that a single occurrence, for example, an earthquake or hurricane, should not affect more than one peril zone. While the exposure to multiple zones is considered remote for events such as a hurricane, the Company does manage its aggregate exposures for such a scenario where the Company considers it appropriate to do so. The definition of the Company s peril zones is subject to periodic review. The Company also generally seeks an attachment point for its property catastrophe reinsurance at a level that is high enough to produce a low frequency of loss. The Company seeks to limit its aggregate exposure in the proportional business through extensive use of occurrence and cession limits.

Reinsurance Retroceded

The Company uses third party reinsurance to support the underwriting and retention guidelines of each reinsurance subsidiary as well as to seek to limit the aggregate exposure of the Company to a particular risk or class of risks. Reinsurance is purchased at several levels ranging from reinsurance of risks assumed on individual contracts to reinsurance covering aggregate exposures. The benefits of ceding risks to other reinsurers include reducing exposure on individual risks, protecting against catastrophic risks, maintaining acceptable capital ratios and enabling the writing of additional business. Reinsurance ceded does not legally discharge the Company from its liabilities in respect of the risk being reinsured. Reinsurance ceded varies by location and line of business based on factors including, among others, market conditions and the credit worthiness of the counterparty.

The Company s traditional catastrophe retrocession program was renewed in June 2011 to cover certain of the Company s exposures. These protections, in various layers and in excess of varying attachment points according to the territory exposed, assist in managing the Company s net retention to an acceptable level. The Company has co-reinsurance retentions within this program. The Company renewed additional structures with a restricted territorial scope for 12 months in July 2011. The Company continues to buy additional protection for the Company s marine and offshore energy exposures. These covers provide protection in various layers and excess of varying attachment points according to the scope of cover provided. The Company has co-reinsurance participations within this program.

The Company continues to buy specific reinsurance on its property and aviation portfolios to manage its net exposures in these classes. The motor third party liability specific reinsurance was not renewed on April 1, 2011.

See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Note 9 to the Consolidated Financial Statements, Reinsurance, for further information.

Premiums

The following table provides an analysis of gross premiums written, net premiums written and net premiums earned for the Reinsurance segment for the last three years ended December 31:

	2011			2010			2009 (2)		
(U.S. dollars in thousands)	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned
Casualty professional lines	$ 217,389	$ 217,389	$ 213,949	$ 218,301	$ 222,133	$ 222,720	$ 170,928	$ 166,903	$ 196,624
Casualty other lines	292,508	290,963	256,853	229,535	222,351	219,154	218,778	217,889	257,610
Property catastrophe	461,742	404,447	387,523	370,266	326,758	323,588	357,267	312,321	312,780
Other property	847,816	583,100	587,611	802,494	562,416	534,422	862,310	553,556	560,379
Marine, energy, aviation, and satellite	156,161	141,924	130,855	117,438	103,926	88,855	89,100	82,393	83,532
Other (1)	102,185	92,083	90,776	103,959	99,897	112,305	156,092	132,322	172,588
Structured indemnity	(4,182)	(4,182)	(4,182)	958	957	955	4,948	4,948	8,433
Total	$ 2,073,619	$ 1,725,724	$ 1,663,385	$ 1,842,951	$ 1,538,438	$ 1,501,999	$ 1,859,423	$ 1,470,332	$ 1,591,946

(1) Other includes credit and surety, whole account contracts and other lines.
(2) Certain reclassifications have been made to conform to current year presentation.

Additional discussion and financial information about the Reinsurance segment are set forth in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 8, Note 4 to the Consolidated Financial Statements, Segment Information.

Competition

The Company competes globally in the property and casualty markets.

The Company s major geographical markets for its property and casualty reinsurance operations are North America, Europe, Bermuda and Emerging Markets (covering Asia/Pacific and Latin America). The main competitors in each of these markets include the following:

North America Berkshire Hathaway, Munich Re Corporation, Swiss Re America Corporation, Transatlantic Re, Everest Re Group Ltd, Hannover Re and PartnerRe Ltd.

Bermuda ACE Tempest Reinsurance Ltd, AXIS Specialty Limited, Arch Reinsurance Limited, Renaissance Reinsurance Limited, Montpelier Reinsurance Ltd, Platinum Underwriters Bermuda Ltd and PartnerRe Ltd.

Latin America Munich Re, Swiss Re, Mapfre Re and IRB

Europe and the rest of world Munich Re, Swiss Re, Lloyd s, SCOR Reinsurance Company, Hannover Re and PartnerRe Ltd.

Marketing and Distribution

See Insurance Segment Marketing and Distribution and Item 8, Note 17(a) to the Consolidated Financial Statements, Commitments and Contingencies Concentrations of Credit Risk, for information in the Company s marketing and distribution procedures and information on the

Company s major brokers.

Claims Administration

Claims management for the reinsurance operations includes the receipt of loss notifications, review and approval of claims through a claims approval process, establishment of loss reserves and approval of loss payments. Case reserves for reported claims are generally established based on reports received from ceding companies with additional case reserves being established when deemed appropriate. Additionally, claims audits are conducted for specific claims and claims procedures at the offices of selected ceding companies, particularly in the United States and the U.K.

Life Operations Segment

During 2009, the Company completed a strategic review of its life reinsurance business. In relation to this initiative, during 2009 the Company sold the renewal rights to certain of its businesses, sold its U.S. life reinsurance business and announced that it would run-off its existing book of U.K. and Irish traditional life and annuity business, and not accept new business. In addition, in 2010, the Company consummated various transactions to novate and recapture U.K. and Irish term assurance and critical illness treaties and U.S. mortality retrocession pools.

The Life operations segment provided life reinsurance on business written by life insurance companies, principally to help them manage mortality, morbidity, survivorship, investment and lapse risks.

Prior to the decision to run-off the U.K. and Irish business, products offered included a broad range of underlying lines of life insurance business, including term assurances, group life, critical illness cover, immediate annuities and disability income. In addition, prior to selling the renewal rights, the products offered included short-term life, accident and health business. Notwithstanding these sales, the segment still covers a range of geographic markets, with an emphasis on the U.K., U.S., Ireland and Continental Europe.

The portfolio has three particularly significant components:

(1) The portfolio includes a small number of large contracts relating to closed blocks of U.K. and Irish fixed annuities in payment. In relation to certain of these contracts, the Company received cash and investment assets at the inception of the reinsurance contract, relating to the future policy benefit reserves assumed. These contracts are long-term in nature, and the expected claims payout period can span up to 30 or 40 years with average duration of around 10 years. The Company is exposed to investment and survivorship risk over the life of these arrangements.

(2) The second component of the portfolio relates to life risks (in the U.S., the U.K. and Ireland) and critical illness risks (in the U.K. and Ireland) where the Company is exposed to the mortality, morbidity and lapse experience from the underlying business, over the medium to long-term.

(3) The third component relates to the annually renewable business covering life, accident and health risks written in Continental Europe. These contracts are short-term in nature and include both proportional and non-proportional reinsurance structures. While the renewal rights for this business have been sold, the existing business remains with the Company.

Underwriting & Claims Administration

While the Life operations segment was closed to new business in March 2009, the pricing information below reflects how new business was acquired prior to that date and hence is relevant to the in-force portfolio of business.

Life reinsurance transactions fall into two distinct forms. The first relates to the reinsurance of an existing and closed block of risks (in-force deal), where the nature of the underlying exposure is known at the date of execution. The second relates to the reinsurance of liabilities that are yet to be written by the ceding company (new business treaty) where, provided the subsequent risks are within the agreed treaty parameters, these risks may be added to the portfolio.

The underwriting of an in-force deal is highly actuarial in nature, requiring detailed analytical appraisal of the key parameters which drive the ultimate profitability of the deal. This includes analysis of historic experience (claims, lapses, etc.) as well as the projection of these assumptions into the future.

When new business was written, in addition to the actuarial analysis required to set the terms, there was also a requirement to establish medical underwriting criteria that will apply to the new risks that may be added to the treaty. Once a treaty is accepted, there is then an ongoing need to monitor the risk selection by the medical underwriters at the ceding company and to ensure that the criteria are being met.

The team includes many members with specialized actuarial knowledge. Claims administration also relies on experienced team members and specific medical expertise, supported where required by third party medical underwriters and claims managers.

The Company maintained comprehensive terms of trade guidelines for all core product lines. These guidelines describe the approach to be taken in assessing and underwriting opportunities, including the approach to be taken to the setting of core parameters and to the determination of appropriate pricing levels. The terms of trade were overseen by a separate team from the new business underwriters.

In addition, the Company maintained a medical underwriting manual that set out the approach to be taken to underwriting specific medical impairments when setting terms for a new business treaty.

Reinsurance Retroceded

The Company purchases limited retrocession capacity on a per-life basis in the United States in order to cap the maximum claim arising from the death of a single individual. Cover is purchased from professional retrocessionaires that meet the Company s criteria for counterparty exposures. Limited retrocession of fixed annuity business has been arranged to manage aggregate longevity capacity on specific deals. Limited retrocession of life, accident and health business on specific treaties written in Continental Europe has also been arranged to manage mortality and morbidity risks.

Premiums

The following table is an analysis of the Life operations gross premiums written, net premiums written and net premiums earned for the year ended December 31, 2011:

(U.S. dollars in thousands)	Gross Premiums Written	Net Premiums Written	Net Premiums Earned
Other Life	$ 232,754	$ 230,130	$ 230,786
Annuity	161,801	132,232	132,232
Total	$ 394,555	$ 362,362	$ 363,018

Additional discussion and financial information about the Life operations is set forth in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Note 4 to the Consolidated Financial Statements, Segment Information.

Competition

In regards to the Life operations segment, the core activity is in the U.S., the U.K., Ireland and Continental Europe. While the Company no longer competes for new business, it retains an in-force portfolio and hence views companies with similar portfolios as competitors.

For the fixed annuity business, competition has historically come from less traditional reinsurance entities, such as Canada Life and Prudential (U.K.) together with Swiss Re, Partner Re, Scor Global Life and Pacific Life Re, among others, who have entered or re-entered this market.

Marketing and Distribution

The Company no longer markets or distributes new products in this segment.

Other Financial Lines Business

Following the streamlining of the Company s operating segments in the first quarter of 2009, the Other Financial Lines business was included in Corporate. This business previously included contracts associated with the funding agreement (FA) business and the guaranteed investment contract (GIC) business. GICs and FAs provide users guaranteed rates of interest on amounts previously invested with the Company. FAs were very similar to GICs in that they have known cash flows. FAs were sold to institutional investors, typically through medium term note programs. During August 2010, the remaining balance of FAs of $450 million was settled and as a result, the Other Financial Lines entities and business are no longer active.

UNPAID LOSSES AND LOSS EXPENSES

Loss reserves are established due to the significant periods of time that may lapse between the occurrence, reporting and payment of a loss. To recognize liabilities for unpaid losses and loss expenses, the Company estimates future amounts needed to pay claims and related expenses with respect to insured events. The Company s reserving practices and the establishment of any particular reserve reflect management s judgment concerning sound financial practice and do not represent any admission of liability with respect to any claim. Unpaid losses and loss expense reserves are established for reported claims (case reserves) and incurred but not reported (IBNR) claims.

The nature of the Company s high excess of loss liability and catastrophe business can result in loss payments that are both irregular and significant. Similarly, adjustments to reserves for individual years can be irregular and significant. Such adjustments are part of the normal course of business for the Company. Certain aspects of the Company s business have loss experience characterized as low frequency and high severity. This may result in volatility in the Company s results of operations, financial condition and liquidity.

The tables below present the development of the Company s unpaid losses and loss expense reserves on both a net and gross basis. The cumulative redundancy (deficiency) calculated on a net basis differs from that calculated on a gross basis. As different reinsurance programs cover different underwriting years, net and gross loss experience will not develop proportionately. The top lines of the tables show the estimated liability, net of reinsurance recoveries, as at the year end balance sheet date for each of the indicated years. This represents the estimated amounts of losses and loss expenses, including IBNR, arising in the current and all prior years that are unpaid at the year end balance sheet date of the indicated year. The tables show the re-estimated amount of the previously recorded reserve liability based on experience as of the year end balance sheet date of each succeeding year. The estimate changes as more information becomes known about the frequency and severity of claims for individual years. The cumulative redundancy (deficiency) represents the aggregate change with respect to that liability originally estimated. The lower portion of the first table also reflects the cumulative paid losses relating to these reserves. Conditions and trends that have affected development of liabilities in the past may not necessarily occur in the future. Accordingly, it may not be appropriate to extrapolate redundancies or deficiencies into the future, based on the tables below. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Cautionary Note Regarding Forward-Looking Statements.

Analysis of P&C Losses and Loss Expense Reserve Development
Net of Reinsurance Recoveries

(U.S. dollars in millions)	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
ESTIMATED LIABILITY FOR UNPAID LOSSES AND LOSS EXPENSES, NET OF REINSURANCE RECOVERABLES	$ 7,004	$ 8,313	$ 10,532	$ 12,671	$ 17,200	$ 17,900	$ 18,191	$ 17,686	$ 17,266	$ 16,882	$ 16,984
LIABILITY RE-ESTIMATED AS OF:											
One year later	$ 7,404	$ 9,250	$ 10,800	$ 13,785	$ 17,090	$ 17,475	$ 17,580	$ 17,401	$ 16,893	$ 16,597	
Two years later	8,423	9,717	11,842	13,675	16,828	16,631	17,286	17,027	16,503		
Three years later	8,653	10,723	11,849	13,607	16,155	16,441	16,956	16,639			
Four years later	9,727	10,738	11,860	13,258	16,067	16,064	16,550				
Five years later	9,674	10,710	11,680	13,236	15,796	15,667					
Six years later	9,718	10,642	11,794	13,068	15,448						
Seven years later	9,680	10,824	11,669	12,819							
Eight years later	9,921	10,775	11,464								
Nine years later	9,863	10,617									
Ten years later	9,776										
CUMULATIVE REDUNDANCY (DEFICIENCY)	(2,772)	(2,304)	(932)	(148)	1,752	2,233	1,641	1,047	763	285	
CUMULATIVE PAID LOSSES, NET OF REINSURANCE RECOVERIES, AS OF:											
One year later	$ 2,011	$ 2,521	$ 1,985	$ 2,008	$ 3,437	$ 3,188	$ 3,207	$ 3,436	3,028	$ 3,256	
Two years later	3,984	3,800	2,867	3,884	5,759	5,620	5,673	5,848	5,530		
Three years later	4,703	4,163	4,380	5,181	7,590	7,528	7,471	7,860			
Four years later	4,641	5,365	5,286	6,392	8,936	8,787	8,941				
Five years later	5,526	6,018	6,225	7,386	9,882	9,763					
Six years later	5,969	6,764	7,002	8,098	10,636						
Seven years later	6,514	7,381	7,591	8,690							
Eight years later	6,965	7,797	8,106								
Nine years later	7,291	8,249									
Ten years later	7,634										

Analysis of P&C Losses and Loss Expense Reserve Development
Gross of Reinsurance Recoverables

(U.S. dollars in millions)	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
ESTIMATED GROSS LIABILITY FOR UNPAID LOSSES AND LOSS EXPENSES	$ 11,807	$ 13,333	$ 16,553	$ 19,616	$ 23,598	$ 22,895	$ 22,857	$ 21,650	$ 20,824	$ 20,532	$ 20,614
LIABILITY RE-ESTIMATED AS OF:											
One year later	$ 12,352	$ 15,204	$ 18,189	$ 19,987	$ 23,209	$ 22,458	$ 21,803	$ 21,348	$ 20,509	$ 20,258	
Two years later	14,003	16,994	18,520	19,533	22,937	21,337	21,445	21,094	19,982		
Three years later	15,377	17,210	18,324	19,525	22,139	21,057	21,305	20,605			
Four years later	15,441	17,048	18,362	19,153	21,992	20,787	20,853				
Five years later	15,267	17,106	18,236	19,099	21,835	20,350					
Six years later	15,401	17,051	18,328	19,050	21,426						
Seven years later	15,381	17,189	18,321	18,766							
Eight years later	15,602	17,253	18,083								
Nine years later	15,639	17,072									
Ten years later	15,508										
CUMULATIVE REDUNDANCY (DEFICIENCY)	(3,701)	(3,739)	(1,530)	850	2,172	2,545	2,004	1,045	842	274	

The following table presents an analysis of the Company s paid, unpaid and incurred losses and loss expenses and a reconciliation of beginning and ending unpaid losses and loss expenses for the years indicated:

Reconciliation of Unpaid Losses and Loss Expenses

(U.S. dollars in thousands)	2011	2010	2009
Unpaid losses and loss expenses at beginning of year	$ 20,531,607	$ 20,823,524	$ 21,650,315
Unpaid losses and loss expenses recoverable	3,649,290	3,557,391	3,964,836
Net unpaid losses and loss expenses at beginning of year	16,882,317	17,266,133	17,685,479
Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in:			
Current year	4,363,258	3,584,662	3,453,577
Prior years	(284,867)	(372,862)	(284,740)
Total net incurred losses and loss expenses	4,078,391	3,211,800	3,168,837
Exchange rate effects	(130,533)	(125,107)	287,752
Less net losses and loss expenses paid in respect of losses occurring in:			
Current year	589,870	442,262	439,638
Prior years	3,256,332	3,028,247	3,436,297
Total net paid losses	3,846,202	3,470,509	3,875,935
Net unpaid losses and loss expenses at end of year	16,983,973	16,882,317	17,266,133
Unpaid losses and loss expenses recoverable	3,629,928	3,649,290	3,557,391
Unpaid losses and loss expenses at end of year	$ 20,613,901	$ 20,531,607	$ 20,823,524

The Company s net unpaid losses and loss expenses relating to the Company s operating segments at December 31, 2011 and 2010 were as follows:

(U.S. dollars in millions)	**2011**	**2010**
Insurance	$ 11,374	$ 11,240
Reinsurance	5,610	5,642
Net unpaid loss and loss expense reserves	$ 16,984	$ 16,882

Current year net losses incurred

Current year net losses incurred increased by $778.6 million in 2011 as compared to 2010. This was mainly as a result of the current year loss ratio increasing by 10.7 loss percentage points due to higher losses from natural catastrophes as compared to 2010, but also from the following: (i) the Insurance segment in 2011 experienced higher large loss activity in the energy, property and marine businesses, as compared to 2010; and (ii) the Reinsurance segment in 2011 experienced higher levels of large loss events in U.S. property including a deterioration in the performance of a large U.S. agricultural program, higher attritional losses as well as business mix changes, as compared to 2010.

Current year net losses incurred increased by $131.1 million in 2010 as compared to 2009. This was mainly as a result of the current year loss ratio increasing by 4.2 loss percentage points due to higher losses from natural catastrophes as compared to 2009, but also from the following: (i) the Insurance segment - in 2010, there were higher large loss events in property and excess casualty, adverse experience in exited lines of business and the impact of flat to slightly negative rate changes partially offset by changes in business mix and improved loss experience in aerospace, as compared to 2009; and (ii) the Reinsurance segment in 2010, there were large loss events in the marine lines which were offset by changes in business mix, improved loss experience in property, discontinued financial lines and the professional and trade credit business related to the credit crisis, as compared to 2009.

See the Income Statement Analysis at Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, for further information regarding the current year loss ratios for each of the years indicated within each of the Company s operating segments.

Prior year net losses incurred

The following tables present the development of the Company s gross and net losses and loss expense reserves. The tables also show the estimated reserves at the beginning of each fiscal year and the favorable or adverse development (prior year development) of those reserves during such fiscal year.

Gross

(U.S. dollars in millions)	2011	2010	2009
Unpaid losses and loss expense reserves at January 1	$ 20,532	$ 20,824	$ 21,650
Gross (favorable) adverse development of those reserves during the year	(274)	(315)	(302)
Unpaid losses and loss expense reserves re-estimated at December 31	$ 20,258	$ 20,509	$ 21,348

Net

(U.S. dollars in millions)	2011	2010	2009
Unpaid losses and loss expense reserves at January 1	$ 16,882	$ 17,266	$ 17,686
Net (favorable) adverse development of those reserves during the year	(285)	(373)	(285)
Unpaid losses and loss expense reserves re-estimated at December 31	$ 16,597	$ 16,893	$ 17,401

As different reinsurance programs cover different underwriting years, contracts and lines of business, net and gross loss experience do not develop proportionately. In 2011 and 2009, gross prior year favorable development was in line with net prior year favorable development in total. However, during 2011, the Insurance segment experienced favorable net prior year development of $76.5 million compared to adverse gross prior year development of $23.1 million. The difference between net and gross development was driven primarily by adverse development related to large excess casualty claims associated with the Deepwater Horizon event in the 2010 accident year totaling $135.6 million on a gross basis while the net impact was $33.4 million due to the impact of outwards reinsurance protections. In addition, $150.0 million gross and $65.0 million net excess casualty IBNR reserves were reallocated to the 2010 accident year in respect of Deepwater Horizon exposures. These IBNR movements were entirely offset by reserve reductions in older accident years. This activity largely explains the difference between the gross and net prior year development for the Insurance segment in 2011 as well as the overall strengthening of the 2010 accident year reflected in the loss reserve development tables shown on the previous pages. During 2010, net prior year favorable development exceeded gross prior year favorable development due primarily to the Insurance segment from a single large claim in excess casualty that was heavily ceded.

The following table presents the net (favorable) adverse prior year loss development of the Company s loss and loss expense reserves by operating segment for each of the years indicated:

(U.S. dollars in millions)	2011	2010	2009
Insurance segment	$ (76.5)	$ (127.4)	$ (62.9)
Reinsurance segment	(208.4)	(245.5)	(221.8)
Total	$ (284.9)	$ (372.9)	$ (284.7)

The Company had net favorable prior year reserve development in property and casualty operations of $284.9 million, $372.9 million and $284.7 million for the years ended December 31, 2011, 2010 and 2009, respectively. See the Income Statement Analysis at Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 8, Note 10 to the Consolidated Financial Statements, Losses and Loss Expenses, for further information regarding the developments in prior year loss reserve estimates for each of the years indicated within each of the Company s operating segments.

Net loss reserves (disposed) acquired

The Company did not dispose of or acquire net loss reserves in 2011, 2010 or 2009.

Exchange rate effects

Exchange rate effects on net loss reserves in each of the three years ended December 31, 2011, 2010 and 2009 related to the global operations of the Company primarily where reporting units have a functional currency that is not the U.S. dollar. In 2011, the U.S. dollar was stronger against U.K. sterling, the Euro, the Brazilian real and the Swiss franc, which more than offset losses that were driven by a stronger Australian dollar In 2010, the U.S. dollar was stronger against the Euro, while weaker against the Swiss franc, Canadian dollar and Brazilian real. In 2009, the U.S. dollar weakened against all of the Company s major currency exposures, particularly the Canadian dollar and U.K. sterling. These movements in the U.S. dollar gave rise to translation and revaluation exchange movements related to carried loss reserve balances of $(130.5) million, $(125.1) million and $287.8 million in the years ended December 31, 2011, 2010 and 2009, respectively.

Net paid losses

Total net paid losses were $3.8 billion, $3.5 billion and $3.9 billion in 2011, 2010 and 2009, respectively. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, for further information.

Other loss related information

The Company s net incurred losses and loss expenses include actual and estimates of potential non-recoveries from reinsurers. As at December 31, 2011 and 2010, the reserve for potential non-recoveries from reinsurers was $99.2 million and $121.9 million, respectively. For further information, see Item 8, Note 9 to the Consolidated Financial Statements, Reinsurance.

Except for certain workers compensation (including long term disability) liabilities and certain U.K. motor liability claims, the Company does not discount its unpaid losses and loss expenses.

The Company utilizes tabular reserving for workers compensation (including long-term disability) unpaid losses that are considered fixed and determinable, and discounts such losses using an interest rate of 5% in 2011 and 2010. The interest rate approximates the average yield to maturity on specific fixed income investments that support these liabilities. The tabular reserving methodology results in applying uniform and consistent criteria for establishing expected future indemnity and medical payments (including an explicit factor for inflation) and the use of mortality tables to determine expected payment periods. Tabular unpaid losses and loss expenses, net of reinsurance, at December 31, 2011 and 2010 on an undiscounted basis were $612.9 million and $660.3 million, respectively. The related discounted unpaid losses and loss expenses were $290.3 million and $311.9 million at December 31, 2011 and 2010, respectively.

<u>INVESTMENTS</u>

Investment structure and strategy

The Company s investment operations are managed centrally by the Company s Investment Group. The Risk and Finance Committee (the RFC) of the Board of Directors of XL-Ireland approves overall investment policy and guidelines, and reviews the implementation of the investment strategies on a regular basis.

Strategic Asset Allocation

The investment strategy for the investment portfolio is based on the strategic asset allocation (SAA) process, which establishes a benchmark (SAA Benchmark) for each of the P&C and Life portfolios that is constructed to maximize company value subject to risk tolerance of management and various constraints, e.g., liability profile, local regulatory requirements, business needs, collateral management, risk tolerance and insurance regulation. This process involves an integrated and stochastic model of the Company that includes financial conditions, reserve volatility and loss payout patterns, premium expense and loss ratio projections and correlations among asset, liabilities and economic variables.

As part of the implementation of its SAA targets, the Company employs a comprehensive framework of investment decision authorities (Authorities Framework). The objective of the Authorities Framework is to ensure that the risk profile of the Company s investment portfolio is consistent with management s risk tolerance as reflected in the SAA Benchmarks. The Authorities Framework controls active or tactical deviations from the SAA Benchmarks. As the magnitude of these deviations increases or the resulting impact on the risk profile of the investment portfolio reaches certain predetermined thresholds, then additional levels of authority and approval are required, up to and including the RFC.

The RFC reviews and approves the SAA Benchmarks for P&C and Life operations and the Authorities Framework as part of the investment policy. Management approves further detailed Investment Authorities which integrate the Authorities Framework into the Company s risk governance processes. The Company has an ongoing process that focuses on optimizing the composition of the P&C and Life portfolios relative to the SAA Benchmarks. See Investment Portfolio Structure for more details.

Investment Portfolio Structure

The Company s investment portfolio consists of fixed income securities, equities, alternative investments, private investments, derivatives and other investments and cash. These securities and investments are denominated in U.S. dollar, U.K. sterling, Euro, Swiss franc, Canadian dollar and other foreign currencies.

The Company s direct use of investment derivatives includes futures, forwards, swaps and option contracts that derive their value from underlying assets, indices, reference rates or a combination of these factors. The Company s investment policy allows derivatives to be used in the investment portfolio to reduce risk and enhance portfolio efficiency. Derivatives may not be used to materially increase investment risk.

At December 31, 2011 and 2010, total investments, cash and cash equivalents, accrued investment income, and net receivable (payable) for investments sold (purchased), were $35.9 billion and $35.8 billion, respectively.

Functionally, the Company s investment portfolio is divided into two principal components:

1) P&C investment portfolio

The largest component is the P&C investment portfolio and its principal objective is to support the Company s insurance and reinsurance operations, the liabilities of which have some uncertainty as to the timing and/or amount. In addition, a smaller portion of the P&C investment portfolio supports corporate operations as well as run-off financial lines business, in which the liabilities have a greater level of certainty and much longer durations than typical P&C business.

The investment strategy for the P&C investment portfolio is based on the SAA process. The primary performance objective is for the total return of the P&C portfolio to meet or exceed the return of the benchmark. The second performance objective is capital preservation through managing the risk profile of the investment portfolio within management s risk tolerance. The third performance objective is achieving the budget for Net Investment Income.

2) Life investment portfolio

The second component of the investment portfolio is the Life investment portfolio, which was approximately $6.5 billion and $6.4 billion at December 31, 2011 and 2010, respectively. At December 31, 2011 and 2010, the securities in the Life investment portfolio represented approximately 18% of the total investment portfolio (including cash and cash equivalents, accrued investment income and net receivable (payable) for investments sold (purchased)).

The principal objective of the Life investment portfolio is to support the Company s Life operations, which are now in run-off. The largest portion of the Life investment portfolio supports the policy benefit reserves associated with asset annuity transactions, with limited uncertainty as to the timing or amount of the liability cash flows. A smaller portion of the Life investment portfolio supports life annuity liabilities that were assumed without portfolio asset transfer.

As discussed above, the investment strategy for the Life investment portfolio is based on the SAA process. The Life SAA process incorporates an additional overlay of the regulatory capital model and a more extensive focus on Asset-Liability Management (ALM), which is possible owing to the lower volatility of life liabilities relative to P&C liabilities.

The primary performance objective for the asset annuity transactions is to achieve a steady credit-adjusted book yield of the Life investment portfolio in order to maximize Life embedded value and minimize statutory capital needs (owing to unique technical requirements of the statutory capital model). For the investments supporting the other portions of the Life investment portfolio, which do not have this unique capital model, the performance objective is for the constrained total return to at least match the total return of the benchmark.

Implementation of investment strategy

Although the Company s management within the Investment Group is responsible for implementation of the investment strategy, the day-to-day management of the Company s investment portfolio is outsourced to investment management service providers in accordance with detailed investment guidelines provided and monitored by the Company. This approach gives the Company access to top investment talent with specialized skills across a broad range of investment products and provides flexibility to actively manage the structure of the portfolio as dictated by the business needs of the Company. Investment management service providers are selected directly by the Company on the basis of various criteria including investment style, track record, performance, risk management capabilities, internal controls, operational risk and diversification implications. The vast majority of the Company s investment portfolio is managed by large, well-established asset management institutions, while a small portion of the portfolio is managed by asset management specialist firms or boutiques. Each investment management service provider may manage one or more portfolios, each of which is generally governed by a detailed set of investment guidelines, including overall objectives, risk limits (where appropriate) and diversification requirements that fall within the Company s overall investment policies and guidelines, including but not limited to exposures to eligible securities, prohibited investments/transactions, credit quality and general concentration limits.

Investment performance

See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Investment Performance, for discussion of the Company s investment performance.

Investment portfolio credit ratings, duration and maturity profile

It is the Company s policy to operate the combined P&C and Life (aggregate) fixed income portfolio with a minimum weighted average credit rating of Aa3/AA . The aggregate credit rating is determined based on the weighted average rating of securities, where the average credit rating, where available, from Standard & Poor s (S&P), Moody s Investors Service (Moody s) and Fitch Ratings (Fitch) is allocated to each security. The weighted average credit rating of the aggregate fixed income portfolio was Aa2/AA at December 31, 2011 and 2010. U.S. agencies paper, whether with implicit or explicit government support, reflect the credit quality rating of the U.S. government for the purpose of these calculations.

The Company did not have an aggregate direct investment in a single corporate issuer in excess of 5% of shareholders equity at December 31, 2011 or 2010. Corporate issuers represent only direct exposure to fixed maturities and short-term investments of the parent issuer and its subsidiaries. These exposures exclude asset and mortgage back securities that were issued, sponsored or serviced by the parent and government-guaranteed issues, but does include covered bonds.

The overall duration and currency denomination of the aggregate fixed income portfolio is managed relative to the respective SAA Benchmarks for P&C and Life operations, both of which incorporate matching currency and duration within a range relative to liabilities. Duration measures bond price volatility and is an indicator of the sensitivity of the price of a bond (or a portfolio of bonds) to changes in interest rates, assuming a parallel change in all global yield curves reflecting the percentage change in price for a 100 basis point change in yield. Management believes that the duration of the aggregate fixed income portfolio is the best single measure of interest rate risk for the aggregate fixed income portfolio.

The maturity profile of the aggregate fixed income portfolio is a function of the maturity profile of estimated loss payments from the Company s liabilities, the expected operating cash flows of the Company and, to a lesser extent, the maturity profile of common fixed income benchmarks. For further information on the maturity profile of the fixed income portfolio see Item 8, Note 5 to the Consolidated Financial Statements, Investments.

ENTERPRISE RISK MANAGEMENT

Risk Management Framework

The Company faces strategic and operational risks related to, among others: underwriting activities, financial reporting, changing macroeconomic conditions, investment risks, reserving estimates, changes in laws or regulations, information systems, business interruption and fraud. The Company s global P&C business, its Life operations (which is in run-off) and its investment portfolios each have their own set of risks (see Item 1A, Risk Factors, for a discussion of such risks). From time to time, these risks may exhibit greater levels of correlation than might be expected over the longer term due to the presence of, to a greater or lesser degree, some common risk drivers (internal or external to the Company) embedded in the Company s businesses that may manifest themselves simultaneously. An enterprise view of risk is required to identify and manage the consequences of these common risks and risk drivers on the Company s profitability, capital strength and liquidity.

The Company s enterprise risk management (ERM) initiatives are led by the Chief Enterprise Risk Officer (CERO), who is a member of the Company s senior management team, and who reports to the Company s Chief Executive Officer. The CERO also acts as a liaison between the Company s Enterprise Risk Committee (see below) and the Board (or other of its committees) with respect to risk matters. All of the Company s employees are expected to assist in the appropriate and timely identification and management of risks and to enhance the quality and effectiveness of ERM.

The Company s ERM framework is designed to allow management to identify and understand material risk concentrations, including concentrations that have unattractive risk/reward dynamics so that prompt, appropriate, corrective or mitigating actions can be taken. To do this, the Company has risk management committees and processes to serve as points of managerial dialogue and convergence across its businesses and functional areas, creates risk aggregation methodologies and develops specific risk appetites to coordinate the identification, vetting and discussion of risk topics and metrics. As part of its ERM activities, the Company applies a suite of stress tests, tools, risk indicators, metrics and reporting processes that examine the consequences of low probability/high severity events (including those related to emerging risks) in order to drive mitigating actions where required.

Risk Governance

Risk Governance relates to the processes by which oversight and decision-making authorities with respect to risks are granted to individuals within the enterprise. The Company s governance framework establishes accountabilities for tasks and outcomes as well as escalation criteria. Governance processes are designed to ensure that transactions and activities, individually and in the aggregate, are carried out in accordance with the Company s risk policies, philosophies, appetites, limits and risk concentrations, and in a manner consistent with expectations of excellence of integrity, accountability and client service.

In July 2010, after completing a comprehensive review of the Company s ERM processes and controls, the Board determined that there was no longer a need for a special committee focused on ERM. As a result, the RFC now oversees ERM matters. With respect to the responsibilities relating to ERM, the RFC:

- Oversees ERM activities, including the risk management framework employed by management. In light of the overall risk management framework, the RFC (i) reviews the methodology for establishing the Company s overall risk capacity; (ii) reviews the policies for the establishment of risk limit frameworks, and adherence to such limits; and (iii) reviews and approves enterprise risk limits.

- Oversees the Company s compliance with any significant enterprise risk limits, authorities and policies. The RFC evaluates what actions to take with respect to such enterprise limits, authorities and policies, and approves any exceptions thereto from time to time as necessary.

- Reviews the Company s overall risk profile and monitor key risks across the Company s organization as a whole, which may involve coordination with other committees of the Board from time to time as appropriate.

- Reviews the Company s process controls over model use and development with respect to model effectiveness, accuracy, propriety and model risk.

- Monitors the Company s risk management performance and obtains reasonable assurance from management that the Company s risk management policies are effective and are being adhered to.

The review of the Company s overall risk appetites and the evaluation of the risk impact of any material strategic decision being contemplated, including consideration of whether such strategic decision is within the risk profile established by the Company, is conducted by the full Board. Risk appetites, as referred to above, are broad statements used to guide the Company s risk and reward preferences over time, all consistent with, among other factors, business prudence, market opportunities, the underwriting pricing cycle and investment climate. Risk appetites are regularly monitored and can change over time in light of the above. See Risk Appetite Management below.

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Management oversight of ERM is performed, in part, via a centralized management Enterprise Risk Committee (ERC), which is chaired by the CERO. The ERC is comprised of the Company s most senior management from its businesses and functions and is charged with developing and monitoring enterprise risk policies, risk appetites, risk limits and compliance with such limits, and risk aggregations, and identifying key emerging risks and ways to mitigate such risks.

In addition to the ERC, the Company has established a framework of separate yet complementary ERM subcommittees, each focusing on particular aspects of ERM. These subcommittees include:

Economic Capital Model Subcommittee: This subcommittee oversees the development of economic capital models that support ERM activities, and helps set priorities and manage resources related to such models. It reviews assumptions and related methodologies used within the Company s economic capital model, including assessments of model validation, model control and model risk.

Liability Subcommittee: This subcommittee supports and assists the ERC s identification, measurement, management, monitoring and reporting of key underwriting liability and emerging risks.

Asset Subcommittee: This subcommittee assists the ERC in its responsibilities in relation to governance and oversight of asset-related risks across the Company, including its Investment Portfolio. Among its activities are (a) involvement in policy decisions on modeling and quantification of risk measurements; and (b) providing an interpretation and assessment of asset-related risks, with a particular focus on market-related risks. Further, the subcommittee is responsible for coordinating on a regular basis with the Credit Subcommittee of the ERC on asset-related credit risks.

Credit Subcommittee: This subcommittee develops and implements the metrics and supporting framework for allocation of credit risk capacity across major business units, including the amount and types of credit exposure.

Operational Risk Subcommittee: This subcommittee supports the ERC s identification, measurement, management and oversight of key operational risks through its oversight over key operational risk management processes and through its review of related operational risk indicators, trends and metrics.

In addition to the above, risk management subcommittees within each of the Company s businesses function to ensure that risk is managed in accordance with the risk limits, guidelines and tolerances that have been allocated to them by the Company.

Risk Appetite Management

The Company s risk appetite framework guides its strategies relating to, among other things, capital preservation, earnings volatility, net worth at risk, operational loss, liquidity standards, capital rating and capital structure, with the objective of preserving the Company s capital base. This framework also addresses the Company s tolerance to risks from material individual events (e.g., natural or man-made catastrophes such as terrorism), the Company s investment portfolio and realistic disaster scenarios that cross multiple lines of business and risks related to some or all of the above that may occur concurrently.

In relation to event risk management, the Company establishes net underwriting limits for individual large events as follows:

1. The Company imposes limits for each peril region/event type at a 1% exceedance probability. If the Company was to deploy the full limit, for any given peril region/event type, there would be a 1% probability that an event would occur during the next year that would result in a net underwriting loss in excess of the limit.

2. The Company also imposes limits for each natural catastrophe peril region at a 1% tail value at risk (TVaR) probability. This statistic indicates the average amount of net loss expected to be incurred given that a loss above the 1% exceedance probability level has occurred.

3. The Company also imposes limits for certain other event types at a 0.4% exceedance probability as described in further detail below. If the Company were to deploy the full limit, for any such given event type, there would be a 0.4% probability that an event would occur during the next year that would result in a net underwriting loss in excess of the limit.

For planning purposes and to calibrate risk tolerances for business to be written from September 30, 2011 through September 30, 2012, the Company set its underwriting limits as a percent of September 30, 2011 Tangible Shareholders Equity (hereafter, Tangible Shareholders Equity). Tangible Shareholders Equity is defined as Total Shareholders Equity less Goodwill and Other Intangible Assets and gives effect for the exercise of the Company s contingent put option which resulted in the issuance of $350.0 million of preference ordinary shares in October 2011. For further information see Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Contingent Capital. These limits may be recalibrated, from time to time, to reflect material changes in Total Shareholders Equity that may occur after September 30, 2011, at the discretion of management and as overseen by the Board.

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Tier I event types (Tier 1 Events), which include natural catastrophes, terrorism and other realistic disaster scenarios, and Tier 2 event types (Tier 2 Events), which include country risk, longevity risk and pandemic risk, are internal risk classifications for the purposes of defining the Company s risk tolerances. In determining Tier 1 and Tier 2 Events the Company considers such factors as:

- Anticipated risk adjusted returns;
- Strategic risk preferences;
- Relativity to peers;
- Shareholder expectations;
- Robustness of exposure assessment methodology; and
- Projected enterprise loss potential.

Per event 1% exceedance probability underwriting limits for Tier 1 Events are set at a level not to exceed approximately 15% of Tangible Shareholders Equity.

Per event 1% TVaR underwriting limits for certain peak natural catastrophe peril regions approximate 20% of Tangible Shareholders Equity. 1% TVaR underwriting limits for non-peak natural catastrophe peril regions are set below the per event 1% TVaR limits described above.

The Company sets separate limits for North Atlantic Windstorm as events within the Atlantic Basin have the potential to cross multiple countries for which separate underwriting limits are established. In particular, per event 1% exceedance probability and per event 1% TVaR underwriting limits for North Atlantic Windstorm are set at a level not to exceed approximately 16.5% and 22.5 % of Tangible Shareholders Equity, respectively, of which no more than 15% and 20% of such exposures, respectively, can arise from U.S. Windstorm, the latter being deemed a Tier 1 Event.

Per event 1% exceedance probability underwriting limits for Tier 2 Events are set at a level not to exceed 7.5% of Tangible Shareholders Equity.

Per event 0.4% exceedance probability underwriting limits for Tier 2 Events are set at a level not to exceed 15% of Tangible Shareholders Equity. The 0.4% exceedance probability limit is used for Tier 2 Events rather than a TVaR measure due to the difficulty in estimating the full distribution of outcomes in the extreme tail of the distribution for these risk types as required for the TVaR measure.

In all instances, the above referenced underwriting limits reflect pre-tax losses net of reinsurance and include inwards and outwards reinstatement premiums related to the specific events being measured. The limits are not net of underwriting profits expected to be generated in the absence of catastrophic loss activity.

In setting underwriting limits, the Company also considers such factors as:

- Correlation of underwriting risk with other risks (e.g., asset/investment risk, operational risk, etc.);
- Model risk and robustness of data;
- Geographical concentrations;
- Exposures at lower return periods;
- Expected payback period associated with losses;
- Projected share of industry loss; and
- Annual aggregate losses at a 1% exceedance probability and at a 1% TVaR level on both a peril region/risk type basis as well as at the portfolio level.

Loss exposure estimates for all event risks are derived from a combination of commercially available and internally developed models together with the judgment of management, as overseen by the Board. Actual incurred losses may vary materially from the Company s estimates. Factors that can cause a deviation between estimated and actualized loss potential include:

Inaccurate assumption of event frequency and severity;

Inaccurate or incomplete data;

Changing climate conditions that may add to the unpredictability of frequency and severity of natural catastrophes in certain parts of the world and create additional uncertainty as to future trends and exposures;

Future possible increases in property values and the effects of inflation that may increase the severity of catastrophic events to levels above the modeled levels;

Natural catastrophe models that incorporate and are critically dependent on meteorological, seismological and other earth science assumptions and related statistical relationships that may not be representative of prevailing conditions and risks, and may therefore misstate how particular events actually materialize, causing a material deviation between forecasted and actual damages associated with such events; and

A change in the judicial climate.

For the above and other reasons, the incidence, timing and severity of catastrophes and other event types are inherently unpredictable and it is difficult to estimate the amount of loss any given occurrence will generate. As a consequence, there is material uncertainty around the Company s ability to measure exposures associated with individual events and combinations of events. This uncertainty could cause actual exposures and losses to deviate from those amounts estimated, which in turn can create a material adverse effect on the Company s financial condition and results of operations and may result in substantial liquidation of investments, possibly at a loss, and outflows of cash as losses are paid.

For a further discussion on risk appetite management see Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Other Key Focuses of Management.

Impact of ERM Processes

The Company believes that its ERM processes improve the quality and timeliness of strategic decisions, enhance the integration of strategic initiatives with the risks related to such initiatives and act as catalysts to improve risk awareness and informed action by and across the Company. The Company believes that the integration of ERM with existing business processes and controls improves the quality of strategic decisions, optimizes the risk/reward characteristics of business strategies, and enhances the Company s overall risk management culture.

In addition, the Company s ERM processes complement the Company s overall internal control framework by helping to manage the complexity that is inherent within an organization of the Company s size, the variety of its businesses and investment activities and geographical reach. However, internal controls and ERM can provide only reasonable, not absolute, assurance that control objectives will be met. As a result, the possibility of material financial loss remains in spite of the Company s ERM activities. An investor should carefully consider the risks and all information set forth in this report including the discussion included in Item 1A Risk Factors, Item 7A, Quantitative and Qualitative Disclosure About Market Risk, and Item 8, Financial Statements and Supplementary Data.

REGULATION

The Company s operating subsidiaries are subject to regulation and supervision in each of the jurisdictions where they are domiciled and licensed to conduct business. Generally, regulatory authorities can have broad supervisory and administrative powers over such matters as licenses, fitness of management, standards of solvency, material transactions between affiliates, premium rates, policy forms, investments, security deposits, methods of accounting, form and content of financial statements, reserves for unpaid losses and loss adjustment expenses, reinsurance, minimum capital and surplus requirements and/or risk based capital standards, dividends and other distributions to shareholders, periodic examinations and annual and other report filings. In general, such regulation is for the protection of policyholders rather than shareholders.

Bermuda Operations

The Insurance Act 1978 of Bermuda and related regulations, as amended (the Act), regulates the Company s (re)insurance operating subsidiaries in Bermuda, and it provides that no person may carry on any insurance business in or from within Bermuda unless registered as an insurer by the Bermuda Monetary Authority (the BMA) under the Act. The Act does not distinguish between insurers and reinsurers and the defined term Insurance business in the Act includes reinsurance business.

The Act imposes on Bermuda (re)insurance companies, solvency and liquidity standards, certain restrictions on the declaration and payment of dividends and distributions, certain restrictions on the reduction of statutory capital, auditing and reporting requirements, and grants the BMA powers to supervise, investigate and intervene in the affairs of insurance companies. Significant requirements include the appointment of an independent auditor, the appointment of a principal representative and a loss reserve specialist for general business and an actuary for long-term business. Class 4 (re)insurers are required to prepare and file with the BMA audited annual financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) or International Financial Reporting Standards (IFRS). The BMA publishes on its website each such Class 4 (re)insurer s GAAP or IFRS audited financial statements. In addition to the audited GAAP or IFRS financial statements, Class 4 (re)insurers are required to prepare and file with the BMA statutory financial statements which are not prepared in accordance with GAAP. The statutory financial statements and statutory financial return do not form part of the public records maintained by the BMA and the filing of the Annual Statutory Financial Return with the BMA. The Supervisor of Insurance is the chief administrative officer under the Act.

A (re)insurer engaged in general business is required to maintain the value of its relevant assets at not less than 75% of the amount of its relevant liabilities.

Currently, all Class 4 general business (re)insurers are required to maintain available statutory capital and surplus at a level equal to or in excess of their enhanced capital requirement (ECR). The applicable ECR is established by reference to either The Bermuda Solvency Capital Requirement (BSCR), which employs a standard mathematical model that can relate more accurately the risks taken on by (re)insurers to the capital that is dedicated to their business or a BMA-approved internal capital model. Beginning with the 2011 financial year end statutory filings, Class E long-term insurers will be required to maintain available statutory capital and surplus at a level equal to or in excess of an ECR which is established by reference to either the BSCR for long-term insurers model or a BMA-approved internal capital model.

Under the Bermuda Companies Act 1981, as amended, a Bermuda company may not declare or pay a dividend or make a distribution out of contributed surplus if there are reasonable grounds for believing that: (a) the company is, or would after the payment be, unable to pay its liabilities as they become due; or (b) the realizable value of the company s assets would thereby be less than its liabilities. For further information see Item 8, Note 23 to the Consolidated Financial Statements, Statutory Financial Data.

All Bermuda (re)insurers must comply with the BMA s Insurance Code of Conduct (ICIC), which came into force on July 1, 2011. The ICIC establishes duties, requirements and standards to be complied with under the Act. Failure to comply with the requirements of the ICIC will be a factor taken into account by the BMA in determining whether a (re)insurer is conducting its business in a sound and prudent manner under the Act. Under the provisions of the Act, the BMA may, from time to time, conduct on site visits at the offices of the (re)insurers it regulates.

The Insurance Amendment (No. 3) Act 2010 came into force on December 31, 2010 and created five new classes of long-term insurance licenses: Class A Class E. Prior to the enactment of this amendment, a (re)insurer carrying on long-term insurance was registered simply as a long-term (re)insurer. Existing long-term insurers were required to re-register under the appropriate new classification system. Effective December 31, 2011, further amendments were made to the Act to extend enhanced solvency reporting requirements to Class E (re)insurers. Class E insurers are now required to prepare and file with the BMA, in addition to statutory financial statements, financial statements prepared in accordance with GAAP or IFRS.

Amendments made in 2010 to the Act provide for written notification to be made to the BMA with respect to a person who becomes a holder of at least 10%, 20%, 33% or 50% of the voting shares of an insurer whose shares or the shares of its parent company are traded on any stock exchange which is recognized by the BMA for this purpose within 45 days of becoming such a shareholder controller. Where it appears to the BMA that a person who is a controller of any description is not or is no longer a fit and proper person to be such a controller, it may serve him with a written notice of objection to his continuing as a controller of the (re)insurer. Also, a (re)insurer must provide written notice to the BMA that a person has become, or ceased to be, a controller or officer of a (re)insurer within 45 days of becoming aware of such fact. An officer in relation to a (re)insurer includes a director, chief executive or senior executive performing duties of underwriting, actuarial, risk management, compliance, internal audit, finance or investment matters.

All registered (re)insurers are required to give notice to the BMA of certain measures that are likely to be of material significance to the BMA in the discharge of its functions under the Act. A material change includes (i) the transfer or acquisition of insurance business being part of a scheme falling under section 25 of the Act or section 99 of the Bermuda Companies Act 1981; (ii) the amalgamation with or acquisition of another firm; (iii) engaging in non-insurance business and activities related thereto where such business is not ancillary to its (re)insurance business; and (iv) engaging in unrelated business that is retail business.

In March 2011, the Exempted Undertaking Tax Protection Act 1966 was amended to extend the period from March 28, 2016 to March 31, 2035 for which the Minister of Finance may grant an assurance to an exempted undertaking, (which includes Bermuda exempted companies, permit companies, partnerships and unit trusts) that it will not be liable to pay certain taxes. These include any taxes computed on profits or income or computed on any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax.

United States

Within the United States, the Company s insurance and reinsurance subsidiaries are subject to regulation and supervision by their respective states of incorporation and by other jurisdictions in which they do business. The methods of regulation vary, but in general have their source in statutes that delegate regulatory and supervisory powers to an insurance official. The regulation and supervision relate primarily to approval of policy forms and rates, the standards of solvency that must be met and maintained including risk-based capital standards, material transactions between an insurer and its affiliates, the licensing of insurers, agents and brokers, restrictions on insurance policy terminations, the nature of and limitations on the amount of certain investments, restrictions and limitations on dividends paid to shareholders, limitations on the net amount of insurance of a single risk compared to the insurer s surplus, deposits of securities for the benefit of policyholders, methods of accounting, collateral requirements to obtain surplus credit for ceded reinsurance assets, periodic examinations of the financial condition and market conduct of insurance companies, the form and content of reports of financial condition required to be filed, and reserves for unearned premiums, losses, expenses and other obligations. All transactions between or among the insurance and reinsurance company subsidiaries must be fair and equitable. In general, such regulation is for the protection of policyholders rather than shareholders.

Regulations generally require insurance and reinsurance companies to furnish information to their domestic state insurance department concerning activities that may materially affect the operations, management or financial condition and solvency of the company. Regulations vary from state to state but generally require that each primary insurance company obtain a license or certificate of authority from the department of insurance of a state to conduct business in that state. An insurer may also earn accreditation as an approved surplus lines insurer in order to conduct business on an excess & surplus insurance basis within a particular state. A reinsurance company is not generally required to have an insurance license to reinsure a U.S. ceding company from outside the United States. However, for a U.S. ceding company to obtain financial statement credit for reinsurance ceded, the reinsurer must obtain an insurance license or achieve accredited status from the cedant s state of domicile or another U.S. state with equivalent insurance regulation, or must post collateral to support the liabilities ceded. In addition, regulations for reinsurers vary somewhat from primary insurers in that the form and rate of reinsurance contracts and the market conduct of reinsurers are not subject to regulator approval.

The Company s U.S. insurance and reinsurance subsidiaries are required to file detailed annual and, in most states, quarterly reports with state insurance regulators in each of the states in which they are licensed or accredited. Such annual and quarterly reports are required to be prepared on a calendar year basis. In addition, the U.S. insurance subsidiaries operations and accounts are subject to financial condition and market conduct examination at regular intervals by state regulators. Effective January 1, 2010, the Company s U.S. insurance subsidiaries were required to comply with expanded state model audit laws which require the filing of a Management s Report of Internal Control Over Financial Reporting. The report provides management s assertion that it has responsibility for establishing and maintaining a system of adequate internal controls over statutory financial reporting, and provides management s assessment that the system is effective. In addition, these laws also expanded the governance requirements of the insurance subsidiaries.

Statutory surplus is an important measure utilized by the regulators and rating agencies to assess the Company s U.S. insurance subsidiaries ability to support business operations and provide dividend capacity. The Company s U.S. insurance

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subsidiaries are subject to various state statutory and regulatory restrictions that limit the amount of dividends that may be paid, within any twelve-month period, from earned surplus without prior approval from regulatory authorities. These restrictions differ by state, but are generally based on a calculation of the lesser of 10% of statutory surplus or 100% of adjusted net investment income to the extent that it has not previously been distributed.

The National Association of Insurance Commissioners (the NAIC) promulgated, and all states have adopted, Risk-Based Capital (RBC) standards for property and casualty companies and life insurance companies as a means of monitoring certain aspects affecting the overall financial condition of insurance companies. RBC is designed to measure the adequacy of an insurer s statutory surplus in relation to the risks inherent in its business. The NAIC s RBC Model Law provides for four incremental levels of regulatory attention for insurers whose surplus is below the calculated RBC target. These levels of attention range in severity from requiring the insurer to submit a plan for corrective action to actually placing the insurer under regulatory control. The Company s current RBC ratios for its U.S. subsidiaries are satisfactory and such ratios are not expected to result in any adverse regulatory action. The Company is not aware of any such actions relative to it.

While the federal government currently does not directly regulate the insurance business in the U.S. (other than for flood, nuclear and reinsurance of losses from terrorism), federal legislation and administrative policies can affect the insurance industry.

In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) was passed into law. Dodd-Frank requires the creation of a Federal Insurance Office within the Treasury Department that will be focused on national coordination of the insurance sector, systemic risk mitigation and international regulatory cooperation. Although the Federal Insurance Office currently does not directly regulate the insurance industry, under Dodd-Frank it has the power to preempt state insurance regulations that are inconsistent with international agreements regarding insurance regulation, subject to certain exceptions. In addition, Dodd-Frank provides that the Federal Insurance Office must submit a report to Congress on improving U.S. insurance regulation, which must cover the feasibility of future federal regulation of the U.S. insurance industry.

The federal government has also undertaken initiatives in several areas that may impact the insurance industry including tort reform, corporate governance and the taxation of insurance companies. In addition, legislation has been introduced from time to time in recent years that, if enacted, could result in the federal government assuming a more direct role in the regulation of the insurance industry, primarily as respects federal licensing in lieu of state licensing.

Other International Operations

A substantial portion of the Company s property and casualty insurance business and a majority of its life reinsurance business are carried on in countries other than Bermuda and the United States. The degree of regulation in foreign jurisdictions can vary. Generally, the Company s subsidiaries must satisfy local regulatory requirements. Licenses issued by foreign authorities to subsidiaries of the Company are subject to modification or revocation for cause by such authorities. The Company s subsidiaries could be prevented, for cause, from conducting business in certain of the jurisdictions where they currently operate. While each country imposes licensing, solvency, auditing and financial reporting requirements, the type and extent of the requirements differ substantially. Key areas where country regulations may differ include: (i) the type of financial reports to be filed; (ii) a requirement to use local intermediaries; (iii) the amount of reinsurance permissible; (iv) the scope of any regulation of policy forms and rates; and (v) the type and frequency of regulatory examinations.

In addition to these requirements, the Company s foreign operations are also regulated in various jurisdictions with respect to currency, amount and type of security deposits, amount and type of reserves, amount and type of local investment and limitations on the share of profits to be returned to policyholders on participating policies. For further information see Item 8, Note 23 to the Consolidated Financial Statements, Statutory Financial Data.

European Union

Financial services including insurance, reinsurance and trading in the U.K. are regulated by the Financial Services Authority (FSA). The FSA s Handbook of Rules and Guidance (the FSA Rules) covers all aspects of regulation including capital adequacy, financial and non-financial reporting and certain activities of U.K.-regulated firms. The Company s subsidiaries carrying out regulated activities in the U.K. comply with the FSA Rules. The Company s Lloyd s managing agency, its managed syndicates and its associated corporate capital vehicles are subject to additional Lloyd s requirements.

FSA regulations also impact the Company as controller (an FSA defined term) of its U.K. regulated subsidiaries. Through the FSA s Approved Persons regime, certain employees and directors are subject to regulation by the FSA of their fitness and certain employees are individually registered at Lloyd s.

The Company s network of offices in the European Union consists mainly of branches of U.K. as well as Irish (regulated by the Central Bank of Ireland) companies that are principally regulated under European Directives from their home states, the U.K. and Ireland, rather than by each individual jurisdiction. Company law in the U.K. and Ireland prohibits the Company s U.K. and Irish entities from declaring a dividend to their respective shareholders unless the applicable entity has profits available for distribution.

The determination of whether a company has profits available for distribution is based on its accumulated realized profits less its accumulated realized losses. While the U.K. and Irish insurance regulatory laws impose no statutory restrictions on a general insurer s ability to declare a dividend, the regulatory rules require maintenance of each insurance company s solvency margin within its jurisdiction and, in addition, regulatory approval must be sought in advance of paying a distribution by an Irish or U.K. regulated company. In addition, as an Irish public limited company, XL-Ireland is also subject to additional reporting requirements under Irish company law.

An E.U. directive covering the capital adequacy and risk management of, and regulatory reporting for, insurers, known as Solvency II, was adopted by the European Parliament in April 2009. Insurers and reinsurers within the European Economic Area (EEA) will need to be compliant with Solvency II by January 1, 2014, although they may need to demonstrate to their regulators certain elements of the requirements are in place in advance, particularly when selecting internal model approval at the outset. Solvency II presents a number of risks to XL s European operations. Insurers across Europe are liaising closely with the regulators and undertaking a significant amount of work to develop their internal capital models and to ensure that they will meet the new requirements. This may divert resources from other business-related tasks. Final Solvency II guidance has yet to be published; consequently the Company s implementation plans are based on its current understanding of the Solvency II requirements which may change. Increases in capital requirements as a result of Solvency II may be required and may impact the Company s results of operations.

Swiss Operations

In Switzerland, the Company s operations are regulated under the Insurance Supervision Act of December 17, 2004. Both Insurance and Reinsurance operations are supervised under this Act. Reinsurance branches of foreign legal entities are not regulated. Insurance branches of foreign entities are subject to limited regulations. Supervision in Switzerland is exercised by the Federal Financial Market Supervisory Authority (FINMA). The supervisory regime currently comprises both Solvency I requirements and Solvency II type requirements (Swiss Solvency Test), the latter of which impose higher capital requirements, with which the entities operating in Switzerland comply. Furthermore, direct insurers and insurance branches operating in Switzerland have to comply with tied assets requirements.

FINMA may call for supervision of an Insurance group, based on certain qualitative and quantitative standards. XL s operations in Switzerland are currently not subject to this Group supervision. XL Company Switzerland GmbH, an intermediary holding company, is consequently not subject to FINMA regulations.

In its opinion dated July 2010, the European Insurance and Occupational Pensions Authority (EIOPA) made a proposal to the European Commission that the Swiss supervisory regime (together with the regime in Bermuda) should be considered in the first wave of the third country equivalence assessment with regard to all three articles on equivalence (Art. 172 Equivalence for reinsurance supervision, Art. 227 Calculating group solvability, Art. 260 Equivalence for third country group supervision).

EMPLOYEES

At December 31, 2011, the Company had 3,818 employees. At that date, 233 of the Company s employees were represented by workers councils and 402 of the Company s employees were subject to industry-wide collective bargaining agreements in several countries outside the United States.

AVAILABLE INFORMATION

The public can read and copy any materials the Company files with the U.S. Securities and Exchange Commission (SEC) at the SEC s Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public can obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers, including the Company, that file electronically with the SEC. The address of the SEC s website is *http://www.sec.gov*.

The Company s website address is *http://www.xlgroup.com*. The information contained on the Company s website is not incorporated by reference into this Annual Report on Form 10-K or any other of the Company s documents filed with or furnished to the SEC.

The Company makes available free of charge, including through the Company s website, the Company s Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC.

The Company adopted Corporate Governance Guidelines, as well as written charters for each of the Audit Committee, the Management Development and Compensation Committee, the Nominating, Governance and External Affairs Committee and the Risk and Finance Committee, as well as a Code of Conduct and a related Compliance Program. Each of these documents is posted on the Company s website at *http://www.xlgroup.com*, and each is available in print to any shareholder who requests it by writing to the Company at Investor Relations Department, XL Group plc, Seaview House, 70 Seaview Avenue, Stamford, CT 06902-6040 United States of America.

The Company intends to post on its website any amendment to, or waiver of, a provision of its Code of Conduct that applies to its Chief Executive Officer, Chief Financial Officer and Corporate Controller or persons performing similar functions and that relates to any element of the code of ethics definition set forth in Item 406 of Regulation S-K under the Securities Act of 1933, as amended.

The Company intends to use its website as a means of disclosing material non-public information and for complying with its disclosure obligations under Regulation FD. Such disclosures will be included on the website in the Investor Relations section. Accordingly, investors should monitor such portions of the Company s website, in addition to following its press releases, SEC filings and public conference calls and webcasts.

ITEM 1A. RISK FACTORS

Any of the following risk factors could have a significant or material adverse effect on our business, financial condition, results of operations and/or liquidity, in addition to the other information contained in this report. Additional risks not presently known to us or that we currently deem immaterial may also impair our business, financial condition and results of operations.

The occurrence of disasters could adversely affect our financial condition, results of operations, cashflows and prospects.

We have substantial exposure to losses resulting from natural and man-made disasters and other catastrophic events. Catastrophes can be caused by various events, including hurricanes, earthquakes, floods, hailstorms, explosions, severe weather, fires, war and acts of terrorism. Changing climate conditions may add to the unpredictability and frequency of natural disasters in certain parts of the world and create additional uncertainty as to future trends and exposures. The incidence and severity of catastrophes are inherently unpredictable, and it is difficult to predict the timing of such events with statistical certainty or estimate the amount of loss any given occurrence will generate.

The occurrence of claims from catastrophic events is likely to result in substantial volatility in our financial condition, results of operations and cash flows for the fiscal quarter or year in which a catastrophic event occurs, as well as subsequent fiscal periods, and could have a material adverse effect on our financial condition and results of operations and our ability to write new business. This risk is exacerbated due to accounting principles and rules that do not permit (re)insurers to reserve for such catastrophic events until they occur. We expect that future possible increases in the values and concentrations of insured property, the effects of inflation and changes in cyclical weather patterns may increase the severity of catastrophic events in the future. Although we attempt to manage our exposure to catastrophic events, a single catastrophic event could affect multiple geographic zones and lines of business and the frequency or severity of catastrophic events could exceed our estimates, in each case potentially having a material adverse effect on our financial condition, results of operations and cash flows. In addition, while we may, depending on market conditions, purchase catastrophe reinsurance and retrocessional protection, the occurrence of one or more major catastrophes in any given period could result in losses that exceed such reinsurance and retrocessional protection. This could have a material adverse effect on our financial condition and results of operations and may result in substantial liquidation of investments, possibly at a loss, and outflows of cash as losses are paid.

The failure of any of the underwriting risk management strategies that we employ could have a material adverse effect on our financial condition, results of operations and/or liquidity.

We seek to limit our loss exposure by, among other things, writing a number of our reinsurance or retrocession contracts on an excess of loss basis, adhering to maximum limitations on reinsurance written in defined geographical zones, limiting program size for each client and prudently underwriting each program written. In addition, in the case of proportional treaties, we generally seek to use per occurrence limitations or loss ratio caps to limit the impact of losses from any one event. We cannot be sure that all of these loss limitation methods will have the precise risk management impact intended. For instance, although we also seek to limit our loss exposure by geographic diversification, geographic zone limitations involve significant underwriting judgments, including the determination of the area of the zones and the inclusion of a particular policy within a particular zone s limits. Underwriting involves the exercise of considerable judgment and the making of important assumptions about matters that are inherently unpredictable and beyond our control, and for which historical experience and probability analysis may not provide sufficient guidance. The failure of any of the underwriting risk management strategies that we employ could have a material adverse effect on our financial condition, results of operations and cash flows. Also, we cannot provide assurance that various provisions of our policies, such as limitations or exclusions from coverage or choice of forum, will be enforceable in the manner that we intend and disputes relating to coverage and choice of legal forum may arise, which could materially adversely affect our financial condition and results of operations.

The insurance and reinsurance industries are historically cyclical and we may experience periods with excess underwriting capacity and unfavorable premium rates.

The insurance and reinsurance industries have historically been cyclical, characterized by periods of intense price competition due to excess underwriting capacity as well as periods when shortages of capacity permitted favorable premium levels. An increase in premium levels is often followed by an increasing supply of insurance and reinsurance capacity, either by capital provided by new entrants or by the commitment of additional capital by existing insurers or reinsurers, which may cause prices to decrease. Either of these factors could lead to a significant reduction in premium rates, less favorable policy terms and conditions and fewer submissions for our underwriting services. In addition to these considerations, changes in the frequency and severity of losses suffered by insureds and insurers may affect the cycles of the insurance and reinsurance industries significantly.

A downgrade or potential downgrade in our financial strength and credit ratings by one or more rating agencies could materially and negatively impact our business, financial condition, results of operations and/or cash flows.

As our ability to underwrite business is dependent upon the quality of our claims paying and financial strength ratings as evaluated by independent rating agencies, a downgrade by any of these institutions could cause our competitive position in the insurance and reinsurance industry to suffer and make it more difficult for us to market our products.

A downgrade below A of our principal insurance and reinsurance subsidiaries by either Standard & Poor s (S&P) or A.M. Best Company (A.M. Best), which is two notches below the current S&P and A.M. Best financial strength ratings of A (Stable) for our principal insurance and reinsurance subsidiaries, may trigger termination provisions in a significant amount of our assumed reinsurance agreements and may potentially require us to return unearned premium to cedants. Whether a client would exercise its termination rights after such a downgrade would likely depend on, among other things, the reasons for the downgrade, the extent of the downgrade, prevailing market conditions, the degree of unexpired coverage, and the pricing and availability of replacement reinsurance coverage. Based on premium value, approximately 70% of our in force reinsurance contracts at January 1, 2012 contained provisions allowing clients to terminate those contracts upon a decline in our ratings to below A . In the event of such a downgrade, we cannot predict whether or how many of our clients would actually exercise such termination rights or the extent to which any such terminations would have a material adverse effect on our financial condition, results of operations, cash flows or future prospects or the market price for our securities. A downgrade could also result in a substantial loss of business for us as ceding companies and brokers that place such business may move to other insurers and reinsurers with higher ratings and the loss of key employees. In addition, due to collateral posting requirements under our letter of credit and revolving credit facility agreements, such a downgrade may require the posting of cash collateral in support of certain in use portions of these facilities (see Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources under Part II, Item 7 of this report). Specifically, a downgrade below A by A.M. Best would constitute an event of default under the Company s three largest credit facilities and may trigger such collateral requirements. In certain limited instances, such downgrades may require us to return cash or assets to counterparties or to settle derivative and/or other transactions with the respective counterparties.

In addition to the financial strength ratings of our principal insurance and reinsurance subsidiaries, various rating agencies also publish credit ratings for XL-Cayman. Credit ratings are indicators of a debt issuer s ability to meet the terms of debt obligations in a timely manner are part of our overall funding profile and affect our ability to access certain types of liquidity. Downgrades in our credit ratings could have a material adverse effect on our financial condition and results of operations and cash flows in a number of ways, including adversely limiting our access to capital markets, potentially increasing the cost of debt or requiring us to post collateral.

The recent downgrade, or any future downgrading, of the United States credit rating could have a material adverse effect on our business, financial condition and results of operations.

Standard & Poor s Ratings Services lowered its long-term sovereign credit rating on the United States from AAA to AA+ in August 2011. In addition, Moody s Investor Services lowered its outlook on U.S. debt to negative upon affirming its AAA rating following passage of legislation that raised the debt ceiling. Because of the unprecedented nature of negative credit rating actions with respect to U.S. government obligations, the impact of these actions or any further downgrades to the U.S. government s sovereign credit rating by any rating agency is inherently unpredictable. Such actions could have material adverse impacts on financial markets and economic conditions on the United States and throughout the world. In turn, this could have a material adverse effect on our business, financial condition and results of operations, including with respect to assets in our investment portfolio, as well as assets in trusts or other collateral arrangements posted by or to us. In addition, further downgrades of the United States credit rating could create broader financial turmoil and uncertainty, and could negatively impact the average credit rating quality of our investment portfolio.

The sovereign debt crisis in Europe and concerns regarding the instability of Euro-zone countries could have a material adverse effect on our business, financial condition and results of operations.

Global markets and economic conditions have been negatively impacted by the uncertainty relating to the level of sovereign debt of numerous E.U. member states and the ability of those countries to service their sovereign debt obligations. This uncertainty has and could in the future result in volatile bond yields on the sovereign debt of E.U. member states and on other European-related corporate debt held within our investment portfolio and could have material adverse impacts on financial markets and economic conditions in the E.U. and throughout the world. In addition, continuing downgrades of sovereign debt could bring down the average credit rating quality of our investment portfolio.

The interdependencies among European economies and financial institutions and between such European economies and financial institutions and those of the rest of the world have also exacerbated concern regarding the stability of European financial markets generally and certain institutions in particular. One or more Euro-zone countries could come under increasing pressure to leave the European Monetary Union, or the Euro as the single currency of the Euro-zone could cease to exist if the European Monetary Union were dissolved. Any of these developments, or the perception that any of these developments are likely to occur, could lead to severe economic recession or depression. If one or more countries abandon the Euro or the European Monetary Union dissolves, it may result in uncertainty with respect to the terms, value or enforceability of these bonds, instruments or contracts, which could result in a material loss to us. Similarly, if a country leaving the Euro-zone imposes currency controls, such controls may have a material adverse impact on the value of and our ability to withdraw capital from a company domiciled in that country.

Given the extent of our European operations, including that XL-Ireland is domiciled in Ireland, investment holdings and clients and counterparties, persistent volatility in the European financial markets, or the failure of any significant European financial institution arising from the wider implications of the crisis, even if not an immediate counterparty to us, could have a material adverse impact on our business, investment portfolio, liquidity or financial performance. If the current Euro-zone sovereign debt crisis persists or worsens, it could lead to further political uncertainty, material changes to tax policies of Euro-zone countries, financial turmoil and social unrest, affecting the successful implementation of stability measures. Sovereigns, financial institutions and companies may become subject to liquidity shortages and be unable to obtain refinancing or new funding, leading to an increased risk of a default on their existing debt, and measures to reduce debt levels and fiscal deficits could result in a further slowdown of or negative economic growth.

For a discussion of the risks to our business during or following a financial market disruption and risks to our investment portfolio, see the risk factor entitled "We are exposed to significant capital markets risk related to changes in interest rates, credit spreads, equity prices and foreign exchange rates as well as other investment risks, which may adversely affect our results of operations, financial condition or cash flows." For a discussion of risks associated with the United States' credit rating, see the risk factor entitled "The recent downgrade, or any future downgrading, of the United States' credit rating could have a material adverse effect on our business, financial condition and results of operations."

Our efforts to develop new products or expand in targeted markets may not be successful and may create enhanced risks.

A number of our recent and planned business initiatives involve developing new products or expanding existing products in targeted markets. This includes the following efforts, from time to time, to protect or profitably grow market share:

- We may develop products that insure risks we have not previously insured or contain new coverage or coverage terms.
- We may refine our underwriting processes.
- We may seek to expand distribution channels.
- We may focus on geographic markets within or outside of the United States where we have had relatively little or no market share.

We may not be successful in introducing new products or expanding in targeted markets and, even if we are successful, these efforts may create enhanced risks. Among other risks:

- Demand for new products or in new markets may not meet our expectations.
- To the extent we are able to market new products or expand in new markets, our risk exposures may change, and the data and models we use to manage such exposures may not be as sophisticated as those we use in existing markets or with existing products. This, in turn, could lead to losses in excess of our expectations.
- Efforts to develop new products or markets have the potential to create or increase distribution channel conflict.
- In connection with the conversion of existing policyholders to a new product, some policyholders pricing may increase, while the pricing for other policyholders may decrease, the net impact of which could negatively impact retention and margins.
- To develop new products or markets, we may need to make substantial capital and operating expenditures, which may also negatively impact results in the near term.

If our efforts to develop new products or expand in targeted markets are not successful, our results could be materially and adversely affected.

We are exposed to significant capital markets risk related to changes in interest rates, credit spreads, equity prices and foreign exchange rates as well as other investment risks, which may adversely affect our results of operations, financial condition or cash flows.

Our operating results are affected by the performance of our investment portfolio. Our assets are invested by a number of investment management service providers under the direction of the Company s management within the Investment Group in accordance, in general, with detailed investment guidelines set by us under the oversight of the RFC, and established in accordance with our SAA framework for our P&C operations and Life operations. Although our investment policies stress diversification of risks and conservation of principal and liquidity, our investments are subject to market-wide risks, as noted below, and fluctuations, as well as to risks inherent in particular securities. We are exposed to significant capital markets risks related to changes in interest rates, credit spreads and defaults, market liquidity, equity prices and foreign currency exchange rates. If significant continued market volatility, changes in interest rates, changes in credit spreads and defaults, a lack of pricing transparency, a reduction in market liquidity, declines in equity prices, and the strengthening or weakening of foreign currencies against the U.S. dollar occur, individually or in tandem, this could have a material adverse effect on our consolidated results of operations, financial condition or cash flows through realized losses, impairments, and changes in unrealized positions. Levels of write-down or impairment are impacted by our assessment of the intent to sell securities that have declined in value as well as actual losses as a result of defaults or deterioration in estimates of cash flows. We periodically review our investment portfolio structure and strategy. If, as a result of such review, we determine to reposition or realign portions of the investment portfolio and sell securities in an unrealized loss position, we will incur an other than temporary impairment charge. Any such charge may have a material adverse effect on our results of operations and business.

For the year ended December 31, 2011, as a result of the prolonged and continued volatility and disruptions in the public debt and equity markets, we incurred realized and unrealized investment losses, as described in Management s Discussion and Analysis of Financial Condition and Results of Operations under Part II, Item 7 of this report. We continue to closely monitor current market conditions and evaluate the long term impact of this market volatility on all of our investment holdings. Depending on market conditions, we could incur additional realized and unrealized losses in future periods, which could have a material adverse effect on the Company s results of operations, financial condition and business.

Our exposure to interest rate risk relates primarily to the market price and cash flow variability of fixed income instruments that are associated with changes in interest rates. Our investment portfolio contains interest rate sensitive instruments, such as fixed income securities, which have been and may continue to be adversely affected by changes in interest rates from central bank monetary policies, domestic and international economic and political conditions and other factors beyond our control. A rise in interest rates would increase the net unrealized loss position of our investment portfolio, offset by our ability to earn higher rates of return on funds reinvested. Conversely, a decline in interest rates would decrease the net unrealized loss position of our investment portfolio, offset by lower rates of return on funds reinvested. We maintain a P&C investment portfolio with diversified maturities that has a weighted average duration that is determined in accordance with its SAA Benchmark based on a dynamic financial analysis of investment assets and liabilities, and that is intended to maximize the Company s enterprise value subject to accounting, regulatory, capital and risk tolerances. The SAA Benchmarks and portfolios supporting our Life operations are rebalanced regularly to reflect an explicit asset-liability management process. However, for both the P&C and Life investment portfolios our estimates of the time and size of estimated loss payment profile may be inaccurate and we may be forced to liquidate investments prior to maturity at a loss in order to cover liabilities. We are exposed to interest rate risk relative to our liabilities.

Our exposure to credit spread risk relates primarily to the market price associated with changes in prevailing market credit spreads and the impact on our holdings of spread products such as corporate and structured credit and credit-sensitive government-related securities. Approximately 2.3% of our aggregate fixed income portfolio consists of below investment-grade high yield fixed income securities. These securities have a higher degree of credit or default risk and a greater exposure to credit spread risk. Certain sectors within the investment and below investment grade fixed income market, such as structured and corporate credit, may be less liquid in times of economic weakness or market disruptions. While we have put in place procedures to monitor the credit risk and liquidity of our invested assets in general and those impacted by recent credit market issues specifically, it is possible that, in periods of economic weakness or periods of turmoil in capital markets, we may experience default losses in both our investment grade and below investment grade corporate and structured credit holdings. This may result in a material reduction of net income, capital and cash flows.

We invest a portion of our investment portfolio in common stock or equity-related securities, including alternative funds and private equity funds. The value of these assets fluctuates, due to changes in the equity and credit markets along with other factors. In times of economic weakness, the market value and liquidity of these assets may decline, and may impact net income, capital and cash flows. In addition, certain of the products offered by our Life operations offer fixed guaranteed returns while debt and equity yields may continue to decline. In addition, the amount of earnings from alternative funds and private investment funds are not earned evenly across the year, or even from year to year. As a result, the amount of earnings that we record from these investments may vary substantially from quarter to quarter. The timing of distributions from such private investment funds depends on particular events relating to the underlying investments. The ability of an alternative fund to satisfy any redemption request from its investors depends on the underlying liquidity of the alternative fund s investments. As a result, earnings, distributions and redemptions from these two asset classes may be more difficult to predict.

The functional currencies of our principal insurance and reinsurance subsidiaries include the U.S. dollar, U.K. sterling, the Euro, the Swiss franc and the Canadian dollar. Exchange rate fluctuations relative to the functional currencies may materially impact our financial position, results of operations and cash flows. Many of our non-U.S. subsidiaries maintain both assets and liabilities in currencies different than their functional currency, which exposes us to changes in currency exchange rates.

In addition, locally-required capital levels are invested in local currencies in order to satisfy regulatory requirements and to support local insurance operations regardless of currency fluctuations. Foreign exchange rate risk is reviewed as part of our risk management process. While we utilize derivative instruments such as futures, options and foreign currency forward contracts to, among other things, manage our foreign currency exposure, it is possible that these instruments will not effectively mitigate all or a substantial portion of our foreign exchange rate risk, which could adversely impact the Company s results of operations.

Certain of our investments may be illiquid or are in asset classes that have been experiencing significant market valuation fluctuations.

We hold certain investments that may lack liquidity or for which the observability of prices or inputs may be reduced in periods of market dislocation, such as non-agency residential mortgage-backed and collateralized debt obligations securities. Even some of our high quality assets have been more illiquid during periods of challenging market conditions. Generally, securities classified as Level 3 pursuant to the fair value hierarchy set forth in authoritative accounting guidance over fair value measurements may be less liquid, may be more difficult to value, requiring significant judgment, and may be more likely to result in sales at materially different amounts than the fair values determined by management.

If we require significant amounts of cash on short notice in excess of normal cash requirements or are required to post or return collateral in connection with certain of our reinsurance contracts, credit agreements, derivative transactions or our invested portfolio, we may have difficulty selling these investments in a timely manner, be forced to sell them for less than we otherwise would have been able to realize, or both.

The reported value of our relatively illiquid types of investments and, in certain circumstances, our high quality, generally liquid asset classes, does not necessarily reflect the lowest current market bid price for the asset. If we were forced to sell certain of our assets in the current market, there can be no assurance that we will be able to sell them for the prices at which we have recorded them and we may be forced to sell them at significantly lower prices, particularly at times of extreme market illiquidity. Any such sales could adversely impact the Company s financial position.

If actual claims exceed our loss reserves, or if changes in the estimated levels of loss reserves are necessary, our financial results and cash flows could be adversely affected.

Our results of operations and financial condition depend upon our ability to assess accurately the potential losses associated with the risks that we insure and reinsure. We establish reserves for unpaid losses and loss adjustment expense (LAE) liabilities, which are estimates of future payments of reported and unreported claims for losses and related expenses with respect to insured events that have occurred. The process of establishing reserves for property and casualty claims can be complex and is subject to considerable variability as it requires the use of informed estimates and judgments. Actuarial estimates of unpaid loss and LAE liabilities are subject to potential errors of estimation, which could be significant, due to the fact that the ultimate disposition of claims incurred prior to the date of such estimation, whether reported or not, is subject to the outcome of events that have not yet occurred. Examples of these events include the accuracy of the factual information on which the estimates were based, especially as this develops, jury decisions, court interpretations, legislative changes, changes in the medical condition of claimants, public attitudes, and economic conditions such as inflation.

Recent deficit spending by governments in the Company s major markets exposes the Company to heightened risk of inflation. Inflation in relation to medical costs, construction costs and tort issues in particular impact the property and casualty industry; however, broader market inflation also poses a risk of increasing overall loss costs. The impact of inflation on loss costs could be more pronounced for those lines of business that are considered long tail such as general liability, as they require a relatively long period of time to finalize and settle claims for a given accident year. Changes in the level of inflation also result in an increased level of uncertainty in our estimation of loss reserves, particularly for long tail lines of business. The estimation of loss reserves may also be more difficult during times of adverse economic conditions due to unexpected changes in behavior of claimants and policyholders, including an increase in fraudulent reporting of exposures and/or losses, reduced maintenance of insured properties or increased frequency of small claims.

Similarly, the actual emergence of claims for life business may vary from the assumptions underlying the policy benefit reserves, in particular, the future assumed mortality improvements on the blocks of in-payment annuities.

In relation to previously written financial guarantee business and related exposures, we establish reserves for losses and LAE on such business based on management s best estimate of the ultimate expected incurred losses. Establishment of such reserves requires the use and exercise of significant judgment by management, including with respect to estimates regarding the occurrence and amount of a loss on an insured or reinsured obligation. Estimates of losses may differ from actual results and such difference may be material, due to the fact that the ultimate dispositions of claims are subject to the outcome of events that have not yet occurred. Examples of these events include changes in the level of interest rates, credit deterioration of insured and reinsured obligations, and changes in the value of specific assets supporting insured and reinsured obligations. In general, guarantees on previously written credit default swaps are exposed to the same risks as noted above, except in events of default by the guarantor. Credit default swaps, however, do not qualify for the financial guarantee scope exception under authoritative accounting guidance over derivative instruments and hedging activities, and, therefore are reported at fair value with changes in the fair value included in earnings. Fair values for such swaps are determined based on methodologies further described in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates. Any estimate of future costs is subject to the inherent limitation on our ability to predict the aggregate course of future events. It should therefore be expected that the actual emergence of losses and LAE will vary, perhaps materially, from any estimate.

We have an actuarial staff in each of our operating segments and a Chief Actuary who regularly evaluates the levels of loss reserves, taking into consideration factors that may impact the ultimate losses incurred. Any such evaluation could result in future changes in estimates of losses or reinsurance recoverable and would be reflected in our results of operations in the period in which the estimates are changed. Losses and LAE, to the extent that they exceed the applicable reserves, are charged to income as incurred. The reserve for unpaid losses and LAE represents the estimated ultimate losses and LAE less paid losses and LAE, and comprises case reserves and IBNR. During the loss settlement period, which can span many years in duration for casualty business, additional facts regarding individual claims and trends often will become known and case reserves may be adjusted by allocation from IBNR without any change in the overall reserve. In addition, application of statistical and actuarial methods may require the adjustment of the overall reserves upward or downward from time to time. Accordingly, the ultimate settlement of losses may be significantly greater than or less than reported loss and loss expense reserves.

The effects of emerging claim and coverage issues on our business are uncertain.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected issues related to claims and coverage may emerge. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims, such as the effects that recent disruptions in the credit markets could have on the number and size of reported claims under directors and officers liability insurance (D&O) and professional liability insurance lines of business. In some instances, these changes may not become apparent until some time after we have issued the insurance or reinsurance contracts that are affected by the changes. Historically such claims and coverage issues have occurred at heightened levels during periods of very soft market conditions which often reflect an inflection point in the typical cycle of insurance industry market conditions. In addition, our actual losses may vary materially from our current estimate of the loss based on a number of factors, including receipt of additional information from insureds or brokers, the attribution of losses to coverages that had not previously been considered as exposed and inflation in repair costs due to additional demand for labor and materials. As a result, the full extent of liability under an insurance or reinsurance contract may not be known for many years after such contract is issued and a loss occurs.

There can be no assurance as to the effect that governmental and regulatory actions will have on financial markets generally or on us in particular.

In response to the financial crises affecting the banking system and financial markets and going concern threats to financial institutions, there have been numerous regulatory and governmental actions in the United States, the U.K. and the Euro-zone among other countries. The purpose of these legislative and regulatory actions is to stabilize the U.S. and international banking systems, improve the flow of credit and foster an economic recovery. However, there can be no assurance as to the success of such actions or the effect that any such governmental actions or future regulatory initiatives may have on certain investment instruments in our investment portfolio, or on our competitive position, business and financial position. If global economic and market conditions remain uncertain, persist, or deteriorate further, we may experience material adverse impacts on our business operations results and financial condition.

For example, we own a number of Tier 1 and Upper Tier 2 hybrid securities issued by financial institutions including those based in the U.S., Europe and the U.K. There is a risk that if the capital positions of financial institutions deteriorate further government intervention, particularly nationalization of such institutions, could occur. There is also a risk of regulatory imposed deferral of coupons or decisions by bank management not to call the capital or defer the coupon payments. This may result in losses on the hybrid securities we hold. There is also the risk of further downgrades of these securities as rating agencies re-evaluate their rating methodologies, which would negatively impact the regulatory capital of the Life operations.

In particular, the current sovereign debt crisis concerning European countries, including Greece, Italy, Ireland, Portugal and Spain, or GIIPS, and related European financial restructuring efforts, may cause the value of the European currencies, including the

Euro, to further deteriorate, which in turn could adversely impact Euro-denominated assets held in our investment portfolio or our European book of business. In addition, the European crisis is contributing to instability in global credit markets, as well as the widening of bond yield spreads. Rating agency downgrades on European sovereign debt and growing concern of the potential default of government issuers or of a possible break-up of the European Union has further contributed to this uncertainty. Should governments default on their obligations, there will be a negative impact on both our direct holdings, as well as on non-government issues and financials held within the country of default. See Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Balance Sheet Analysis European Sovereign Debt Crisis for an analysis of our fixed maturity portfolio s exposure to GIIPS.

We may be unable to purchase reinsurance and, even if we are able to successfully purchase reinsurance, we are subject to the possibility of uncollectability. The impairment of other financial institutions also could adversely affect us.

We purchase reinsurance for our own account in order to mitigate the volatility that losses impose on our financial condition. Our clients purchase reinsurance from us to cover part of the risk originally written by them. Retrocessional reinsurance involves a reinsurer ceding to another reinsurer, the retrocessionaire, all or part of the reinsurance that the first reinsurer has assumed. Reinsurance, including retrocessional reinsurance, does not legally discharge the ceding company from its liability with respect to its obligations to its insureds or reinsureds. A reinsurer s or retrocessionaire s insolvency, inability or refusal to make timely payments under the terms of its agreements with us, therefore, could have a material adverse effect on us because we remain liable to our insureds and reinsureds. At December 31, 2011, we had approximately $3.9 billion of reinsurance recoverables and reinsurance balances receivable, net of reserves for uncollectible recoverables. For further information regarding our reinsurance exposure, see Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations.

From time to time, market conditions may limit or prevent us from obtaining the types and amounts of reinsurance that we consider adequate for our business needs such that we may not be able to obtain reinsurance or retrocessional reinsurance from entities with satisfactory creditworthiness in amounts that we deem desirable or on terms that we deem appropriate or acceptable.

We also have exposure to counterparties in various industries, including banks, hedge funds and other investment vehicles, and in transactions in addition to reinsurance agreements, including derivative transactions. Many of these transactions expose us to credit risk in the event our counterparty fails to perform its obligations. Even if we are entitled to collateral when a counterparty defaults, such collateral may be illiquid or proceeds from such collateral when liquidated may not be sufficient to recover the full amount of the obligation. We also have exposure to financial institutions in the form of secured and unsecured debt instruments and equity securities.

Since we depend on a few brokers for a large portion of our revenues, loss of business provided by any one of them could adversely affect us.

We market our insurance and reinsurance products worldwide primarily through insurance and reinsurance brokers. Marsh & McLennan Companies, AON Corporation and the Willis Group and their respective subsidiaries each provided approximately 20%, 20% and 12% respectively, of our gross written premiums for property and casualty operations for the year ended December 31, 2011. Loss of all or a substantial portion of the business provided by one or more of these brokers could have a material adverse effect on our business.

Our reliance on brokers subjects us to credit risk.

In certain jurisdictions, when an insured or ceding insurer pays premiums for policies of insurance or contracts of reinsurance to brokers for further payment to us, such premiums might be considered to have been paid and the insured or ceding insurer will no longer be liable to us for such amounts, whether or not we have actually received the premiums from the broker. In addition, in accordance with industry practice, we generally pay amounts owed on claims under our reinsurance contracts to brokers, and these brokers, in turn, pay these amounts over to the clients that have purchased reinsurance from us. Although the law is unsettled and depends upon the facts and circumstances of the particular case, in some jurisdictions, if a broker fails to make such a claims payment to the insured or ceding insurer, we might remain liable to the insured or ceding insurer for that non-payment. Consequently, we assume a degree of credit risk associated with the brokers with whom we transact business. Due to the unsettled and fact-specific nature of the law governing these types of scenarios and our lack of historical experience with such risks, we are unable to quantify our exposure to this risk.

We are subject to a number of risks associated with our business in emerging markets.

Our insurance and reinsurance subsidiaries conduct business outside the United States primarily in the U.K., Bermuda, and Europe. We have also continued to pursue opportunities in other countries, including in emerging markets such as Asia, Africa and Latin America. In conducting such business we are subject to a number of significant risks. These risks include restrictions such as price controls, capital controls, exchange controls, ownership limits and other restrictive governmental actions, which could have an adverse effect on our business and our reputation. In addition, some countries, particularly emerging economies, have laws and regulations that lack clarity and, even with local expertise and effective controls, it can be difficult to determine the exact requirements

of the local laws. Failure to comply with local laws in a particular market could have a significant and negative effect not only on our business in that market but also on our reputation generally.

Additional discussion of the risks associated with our operations in Europe as a result of the sovereign debt crisis is included in the risk factor entitled The sovereign debt crisis in Europe and concerns regarding the instability of Euro-zone countries could have a material adverse effect on our business, financial condition and results of operations.

Our holding company structure and certain regulatory and other constraints affect our ability to pay dividends, make payments on our debt securities and make other payments.

As a holding company with no direct operations or significant assets other than the capital stock of our subsidiaries, we rely on investment income, cash dividends, loans and other permitted payments from our subsidiaries to make principal and interest payments on our debt, to pay operating expenses and ordinary and preferred shareholder dividends, to make capital investments in our subsidiaries and to pay certain of our other obligations that may arise from time to time. We expect future investment income, dividends and other permitted payments from these subsidiaries to be our principal source of funds to pay such expenses, preferred and ordinary share dividends and obligations. The payment of dividends to us by our insurance and reinsurance subsidiaries is regulated under the laws of various jurisdictions including Bermuda, the U.K., Ireland and Switzerland and certain insurance statutes of various states in the United States in which our insurance and reinsurance subsidiaries are licensed to transact business and the other jurisdictions where we have regulated subsidiaries. For further information regarding regulatory restrictions governing the payment of dividends by the Company s significant property and casualty subsidiaries in Ireland, Bermuda and the U.S., see Item 8, Note 23 to the Consolidated Financial Statements, Statutory Financial Data, and Item 1, Business Regulation.

XL-Ireland is subject to certain legal constraints that affect its ability to pay dividends on or redeem or buyback our ordinary shares. While XL-Ireland s articles of association authorize its board of directors to declare and pay dividends as justified from the profits, under Irish law, XL-Ireland may only pay dividends or buyback or redeem shares using distributable reserves. As of December 31, 2011, XL-Ireland had $4.1 billion in distributable reserves. In addition, no dividend or distribution may be made unless the net assets of XL-Ireland are not less than the aggregate of its share capital plus undistributable reserves and the distribution does not reduce XL-Ireland s net assets below such aggregate.

In addition, XL-Cayman is subject to certain constraints that affect its ability to pay dividends on its preferred shares. Under Cayman Islands law, XL-Cayman may not declare or pay a dividend if there are reasonable grounds for believing that XL-Cayman is, or would after the payment be, unable to pay its liabilities as they become due in the ordinary course of business. Also, the terms of XL-Cayman s preferred shares prohibit declaring or paying dividends on the ordinary shares unless full dividends have been declared and paid on the outstanding preferred shares. In addition, the ability to declare and pay dividends may be restricted by covenants in our letters of credit and revolving credit facilities.

We may require additional capital in the future, which may not be available to us on satisfactory terms, on a timely basis or at all.

Our future capital requirements depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover our losses. To the extent that the funds generated by our ongoing operations are insufficient to fund future operating requirements and cover claim payments, or that our capital position is adversely impacted by mark-to-market changes on the investment portfolio, catastrophe events or otherwise, we may need to raise additional funds through financings or curtail our growth and reduce our assets. As a result of the current severe economic conditions that persist in the capital markets, any future financing may not be available on terms that are favorable to us, if at all. Our letter of credit facilities are needed to a significant extent for U.S. cedants, and are effective for such cedants only if the banks issuing letters of credit are on the list of NAIC approved banks. If some or all of the issuing banks under our credit facilities cease to be NAIC approved, whether arising from macroeconomic or bank specific events, and we are unable to replace non-approved banks with NAIC approved banks, our letter of credit facility capacity could be significantly diminished. In addition, in the case of a macroeconomic event, such as dissolution of the European Monetary Union, the availability of alternative lending sources may be significantly reduced or non-existent, and the cost of replacement facilities may be significantly increased or prohibitive. Any future equity financings could be dilutive to our existing shareholders or could result in the issuance of securities that have rights, preferences and privileges that are senior to those of our other securities. Our inability to obtain adequate capital could have a material adverse effect on our business, financial condition and results of operations.

Competition in the insurance and reinsurance industries could reduce our operating margins.

The insurance and reinsurance industries are highly competitive. We compete on an international and regional basis with major U.S., Bermudian, European and other international insurers and reinsurers and with underwriting syndicates, some of which have greater financial and management resources and higher ratings than we have. We also compete with new companies that continue to be formed to enter the insurance and reinsurance markets. In addition, capital market participants have created alternative products that are intended to compete with reinsurance products. Increased competition could result in fewer submissions, lower premium rates and less favorable policy terms and conditions, which could reduce our margins.

Operational risks, including human or systems failures, are inherent in our business.

Operational risk and losses can result from, among other things, fraud, errors, failure to document transactions properly or to obtain proper internal authorization, failure to comply with regulatory requirements, information technology failures, failure to appropriately transition new hires or external events. Areas of operational risk can be heightened in discontinued or exited business as a result of reduced overall resource allocation and the loss of relevant knowledge and expertise by departing management. The Company has exited a number of businesses in recent years, potentially increasing operational risk in such businesses.

We believe that our modeling, underwriting and information technology and application systems are critical to our business. Moreover, our information technology and application systems have been an important part of our underwriting process and our ability to compete successfully. We have also licensed certain systems and data from third parties. We cannot be certain that we will have access to these, or comparable, service providers, or that our information technology or application systems will continue to operate as intended. An external cyber attack, or any ineffectiveness in or cyber attack on our internal controls or information technology and application systems could have a material adverse effect on our business or reputation.

In particular, we operate globally, and have two office locations in India that currently provide large portions of our back office support. Our global operations present significant operational risk due to the possibility of disruptions in communication or information processes, whether due to technical difficulties, power failures or destruction or damage to our offices for any reason. If any disruption occurs, our business continuity and disaster recovery plans may not be effective, particularly if natural or man-made catastrophic events occur, and such disruption could harm our results of operations or our reputation in the marketplace.

In addition, we have outsourced the day-to-day management, custody and record-keeping of our investment portfolio to third-party managers and custodians that we believe to be reputable. A major defect in those investment managers investment management strategy, or decision-making could result in management distraction and/or significant financial loss. We also rely on a few brokers for a large portion of our revenues. A major defect in our brokers , investment managers or custodians internal controls or information and technology systems could result in management distraction or significant financial loss.

Any ineffectiveness in our internal controls, information technology, application systems, investment management or custody and record keeping could have a material adverse effect on our business.

Unanticipated losses from terrorism and uncertainty surrounding the future of the TRIPRA could have a material adverse effect on our financial condition, results of operations and cash flows.

The U.S. Terrorism Risk Insurance Act of 2002 (TRIA), as amended, established the Terrorism Risk Insurance Program (TRIP), which became effective on November 26, 2002 and was a three-year federal program effective through 2005. On December 22, 2005, President George W. Bush signed a bill extending TRIA (TRIAE) for two more years, continuing TRIP through 2007. On December 26, 2007, President George W. Bush signed the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA) which further extended TRIP for seven years until December 31, 2014 and also eliminated the distinction between foreign and domestic acts of terrorism.

In response to the tightening of supply in certain insurance and reinsurance markets resulting from, among other things, the September 11 event, the TRIP was created upon the enactment of the TRIA of 2002 to ensure the availability of commercial insurance coverage for certain terrorist acts in the U.S. This law established a federal assistance program through the end of 2005 to help the commercial property and casualty insurance industry cover claims related to future terrorism-related losses and required that coverage for terrorist acts be offered by insurers.

TRIA voided in force terrorism exclusions as of November 26, 2002 for certified terrorism on all TRIA specified property and casualty business. TRIA required covered insurers to make coverage available for certified acts of terrorism on all new and renewal policies issued after TRIA was enacted. TRIA along with further extensions to TRIP, as noted above, allows us to assess a premium charge for terrorism coverage and, if the policyholder declines the coverage or fails to pay the buy-back premium, certified acts of terrorism may then be excluded from the policy, subject, however, to state specific requirements. Terrorism coverage cannot be excluded from workers compensation policies. Subject to a premium-based deductible and provided that we have otherwise complied with all the requirements as specified under TRIPRA, we are eligible for reimbursement by the Federal Government for up to 85% of our covered terrorism-related losses arising from a certified terrorist attack. Such payment by the government will, in effect, provide reinsurance protection on a quota share basis. The maximum liability during a program year, including both the Federal Government s and insurers shares, is capped on an aggregated basis at $100 billion. While regulations have been promulgated by the Department of the Treasury (Treasury) requiring that Treasury advise participating insurers, such as the Company, in advance of reaching the $100 billion aggregate limit that such aggregate limit could be reached during the program year, there is a risk that the Company will not be given adequate notice of the potential exhaustion of that aggregate limit. Accordingly, the Company could overpay with regard to such losses, and it is unlikely Treasury would reimburse the Company for such losses; moreover, it is unclear whether the Company, in the event of an overpayment, would be able to recover the amount of any such overpayment.

We believe that TRIP and the related legislation have been an effective mechanism to assist policyholders and industry participants with the extreme contingent losses that might be caused by acts of terrorism. Nevertheless, we cannot assure you that TRIPRA will be extended beyond 2014, and its expiration or a significant change in terms could have an adverse effect on us, our clients or the insurance industry.

The regulatory regimes under which we operate, and potential changes thereto, could have a material adverse effect on our business.

Our insurance and reinsurance subsidiaries operate in 24 countries around the world as well as in all 50 U.S. states. Our operations in each of these jurisdictions are subject to varying degrees of regulation and supervision. The laws and regulations of the jurisdictions in which our insurance and reinsurance subsidiaries are domiciled require, among other things, that these subsidiaries maintain minimum levels of statutory capital, surplus and liquidity, meet solvency standards, submit to periodic examinations of their financial condition and restrict payments of dividends, distributions and reductions of capital in certain circumstances. Statutes, regulations and policies that our insurance and reinsurance subsidiaries are subject to may also restrict the ability of these subsidiaries to write insurance and reinsurance policies, make certain investments and distribute funds.

In recent years, the U.S. insurance regulatory framework has come under increased federal scrutiny. In July 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act requires many federal agencies to adopt new rules and regulations that will apply to the financial services industry and also calls for many studies regarding various industry practices. In particular, the Dodd-Frank Act created a Federal Insurance Office within the Treasury that is focused on national coordination of the insurance sector, systemic risk mitigation and international regulatory cooperation. Although the Federal Insurance Office currently does not directly regulate the insurance industry, under the Dodd-Frank Act it has the power to preempt state insurance regulations that are inconsistent with international agreements regarding insurance regulation, subject to certain exceptions. In addition, the Dodd-Frank Act provides that the Federal Insurance Office must submit a report to Congress on improving U.S. insurance regulation, which must cover the feasibility of future federal regulation of the U.S. insurance industry. This study or another among the various studies required by the legislation could result in additional rulemaking or legislative action, which could negatively impact our business and financial results. While we have not yet been required to make material changes to our business or operations as a result of the Dodd-Frank Act, due to the complexity and broad scope of the Dodd-Frank Act and the time required for regulatory implementation, it is not certain what the scope of future rulemaking or interpretive guidance from the SEC, CFTC or other regulatory agencies may be, and what impact this will have on our compliance costs, business, operations and profitability.

In addition, some state legislatures have considered or enacted laws that may alter or increase state regulation of insurance and reinsurance companies and holding companies. Moreover, the NAIC, which is the organization of insurance regulators from the 50 U.S. states, the District of Columbia and the four U.S. territories, as well as state insurance regulators regularly reexamine existing laws and regulations.

In addition to these proposals and initiatives in the United States, new capital adequacy and risk management regulations called Solvency II are in the process of being implemented throughout the EU, introducing changes to the prudential regulation of European insurers, with a timeline to achieve full compliance by January 1, 2014. Similar legislation is also in the process of being developed or implemented in other jurisdictions, including Canada and Switzerland. In addition, regulations in countries in which we have operations are working with the International Association of Insurance Supervisors (and in the U.S., with the NAIC) to consider changes to insurance company supervision, including solvency requirements and group supervision. There remains significant uncertainty as to the impact of these efforts, however, such impacts could constrain our ability to move capital between subsidiaries or require that additional capital or security be provided in certain jurisdictions, which may impact profitability.

Our Bermuda-based operating subsidiaries are subject to the BMA s risk-based capital standards for (re)insurance companies, which impose required levels of statutory capital and surplus on our Bermuda-based operating standards. While our Bermuda-based operating subsidiaries currently have excess capital and surplus under these requirements, there can be no assurance that such requirements or similar regulations, in their current form or as may be amended in the future, will not have a material adverse effect on our business, financial condition or results of operations.

We may not be able to comply fully with, or obtain desired exemptions from, revised statutes, regulations and policies that govern the conduct of our business. Failure to comply with, or to obtain desired authorizations and/or exemptions under, any applicable laws could result in restrictions on our ability to do business or undertake activities that are regulated in one or more of the jurisdictions in which we operate and could subject us to fines and other sanctions. In addition, changes in the laws or regulations to which we are, or may become subject, or in the interpretations thereof by enforcement or regulatory agencies, could have a material adverse effect on our business, financial condition and results of operations.

Potential government intervention in our industry as a result of recent events and instability in the marketplace for insurance products could hinder our flexibility and negatively affect the business opportunities that may be available to us in the market.

Government intervention and the possibility of future government intervention have created uncertainty in the insurance and reinsurance markets. Government regulators are generally concerned with the protection of policyholders to the exclusion of other

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constituencies, including shareholders of insurers and reinsurers. While we cannot predict the exact nature, timing or scope of possible governmental initiatives, such proposals could adversely affect our business by, among other things:

- providing insurance and reinsurance capacity in markets and to consumers that we target, e.g., the creation or expansion of a state or federal catastrophe funds such as those in Florida;
- requiring our participation in industry pools and guarantee associations
- expanding the scope of coverage under existing policies;
- regulating the terms of insurance and reinsurance policies; or
- disproportionately benefiting the companies of one country over those of another.

Government intervention has in the recent past taken the form of financial support of certain companies in our industry. Governmental support of individual competitors can lead to increased pricing pressure, a distortion of market dynamics, and ultimately the prolonging of the current period of soft market conditions. The insurance industry is also affected by political, judicial and legal developments that may create new and expanded theories of liability, which may result in unexpected claims frequency and severity and delays or cancelations of products and services by insureds, insurers and reinsurers which could adversely affect our business.

For further information regarding government regulation and/or intervention in response to the financial and credit crises, see risk factor entitled There can be no assurance as to the effect that governmental actions will have on such markets generally or on us in particular above.

Consolidation in the insurance industry could adversely impact us.

Insurance industry participants may seek to consolidate through mergers and acquisitions. Continued consolidation within the insurance industry will further enhance the already competitive underwriting environment as we would likely experience more robust competition from larger, better capitalized competitors. These consolidated entities may use their enhanced market power and broader capital base to negotiate price reductions for our products and services, and reduce their use of reinsurance, and as such, we may experience rate declines and possibly write less business.

The loss of one or more key executives or the inability to attract, motivate and retain qualified personnel could adversely affect our ability to conduct business.

Our success depends on our ability to attract new, highly skilled individuals and to motivate and retain our existing key executives and qualified personnel. The loss of the services of any of our key executives or the inability to attract, motivate and retain other highly skilled individuals in the future could adversely affect our ability to conduct our business. In addition, we do not maintain key man life insurance policies with respect to our employees.

In addition, certain of our executives who work in our Bermuda operations are not Bermudian and our success in such operations may depend in part on the continued services of key employees working in Bermuda. The recently enacted Incentives for Job Makers Act 2011 (IJMA) permits employers to apply to the Bermuda Government for a designation to allow up to five senior executives at any one time to make a further application to be exempt from the provisions of current Bermuda work permit requirements. After ten years, eligible exempted senior executives may apply for a permanent resident s certificate. Currently, non-Bermudians (other than spouses of Bermudians and holders of permanent resident certificates) who are not able to avail themselves of the provisions of the IJMA may not engage in any gainful occupation in Bermuda without an appropriate governmental work permit. A work permit may be granted or renewed by the Bermuda government for a specific period of time, upon showing that, after proper public advertisement, no Bermudian (or spouse of a Bermudian or holder of a permanent resident certificate) is available who meets the minimum standards reasonably required by an employer with respect to a certain position. The government of Bermuda places term limits on individuals with work permits, subject to certain exemptions for key employees. No assurances can be given that any work permit will be issued or, if issued, renewed upon the expiration of the relevant term or that key employee status will be granted or revoked.

A decrease in the fair values of our reporting units may result in future goodwill impairments.

When we acquire an entity, the excess of the purchase price over the net identifiable assets acquired is allocated to goodwill. We conduct impairment tests on our reported goodwill at least annually or more frequently if impairment indicators exist. In performing a goodwill impairment test, we use various methods and make various assumptions to determine the fair value of our reporting units, including the determination of expected future cash flows and/or profitability of such reporting units, and we take into account market value multiples and/or cash flows of entities that we deem to be comparable in nature, scope or size to our reporting units. However, expected future cash flows and/or profitability may be materially and negatively impacted as a result of, among other things, a decrease in renewal activity and new business opportunities, a decrease in retention or our underwriting teams, lower-than-expected yields and/or cash flows from our investment portfolio, higher-than-expected claims activity and magnitude of incurred losses and general economic factors that impact the reporting unit. In addition, previously determined market value multiples and/or cash flows may no longer be relevant as a result of these potential factors. As a result of these potential changes, the estimated fair value of one or more of our reporting units may decrease, causing the carrying value of the net assets assigned to the reporting unit to exceed the fair value of such net assets. If we determine an impairment exists, we adjust the carrying value of goodwill to its implied fair value. The impairment charge is recorded in our income statement in the period in which the impairment is determined. If we are required in the future to write down additional goodwill, our financial condition and results of operations would be negatively affected. In connection with fair value measurements and the accounting for goodwill, the use of generally accepted accounting principles requires management to make certain estimates and assumptions. Significant judgment is required in making these estimates and assumptions, and actual results may ultimately be materially different from such estimates and assumptions. The Company completed an interim impairment test during the fourth quarter of 2011 which resulted in a non-cash goodwill impairment charge of $429.0 million. The charge related to the Insurance segment. The remaining goodwill balance carried in our consolidated financial statements at December 31, 2011 is $391.5 million.

Provisions in our Articles of Association may reduce the voting rights of our ordinary shares.

Our Articles of Association generally provide that shareholders have one vote for each ordinary share held by them and are entitled to vote, on a non-cumulative basis, at all meetings of shareholders. However, the voting power that may be exercised by certain persons or groups may not equal or exceed 10% or more of the voting power conferred by our shares.

In particular, our Articles of Association provide that if, and for so long as, the votes conferred by the Controlled Shares (as defined below) of any person constitute 10% or more of the votes conferred by all our issued shares, the voting rights with respect to the Controlled Shares of such person shall be limited, in the aggregate, to a voting power equal to approximately (but slightly less than) 10%, pursuant to a formula set forth in the our Articles of Association. Controlled Shares of a person (as defined in our Articles of Association) include (1) all of our shares owned directly, indirectly or constructively by that person (within the meaning of Section 958 of the Internal Revenue Code of 1986, as amended (the IRS Code), and (2) all of our shares owned directly, indirectly or constructively by that person or any group of which that person is a part, within the meaning of Section 13(d)(3) of the Exchange Act.

Provisions in our Articles of Association may restrict the ownership and transfer of our ordinary shares.

Our Articles of Association provide that our Board of Directors shall decline to register a transfer of shares if it appears to our Board of Directors, whether before or after such transfer, that the effect of such transfer would be to increase the number of Controlled Shares of any person to 10% or more of any class of our voting shares, of our total issued shares, or of the total voting power of our total issued shares.

Certain provisions in our charter documents could, among other things, impede an attempt to replace our directors or imposes restrictions with respect to a change of control, which could diminish the value of our ordinary shares.

Our Articles of Association contain provisions that may make it more difficult for shareholders to replace directors and could delay or prevent a change of control that a shareholder may consider favorable. These provisions include a staggered board of directors, limitations on the ability of shareholders to remove directors, limitations on voting rights and certain transfer restrictions on our ordinary shares.

As an Irish company, we are subject to the Irish Takeover Rules, under which our Board of Directors is not permitted to take any action that might frustrate an offer for our shares once the Board of Directors has received an offer or has reason to believe an offer is or may be imminent without the approval of more than 50% of shareholders entitled to vote at a general meeting of shareholders and/or the consent of the Irish Takeover Panel. This could limit the ability of the Board of Directors to take defensive actions even if the Board of Directors believes that such defensive actions would be in the best interests of the Company and its shareholders.

The Irish Takeover Rules also could discourage an investor from acquiring 30% or more of our outstanding ordinary shares unless such investor was prepared to make a bid to acquire all outstanding ordinary shares. Further, it could be more difficult for us to obtain shareholder approval for a merger or negotiated transaction because of heightened shareholder approval requirements for certain types of transactions under Irish law.

In addition, insurance regulations in certain jurisdictions may also delay or prevent a change of control or limit the ability of a shareholder to acquire in excess of specified amounts of our ordinary shares.

Irish shareholder voting requirements may limit flexibility with respect to certain aspects of capital management.

Irish law allows shareholders to authorize a board of directors to issue shares subsequent to receipt of authorization without further shareholder approval, but this authorization must be renewed after five years. Additionally, subject to specified exceptions, Irish law grants statutory pre-emption rights to existing ordinary shareholders to subscribe for new issuances of shares for cash, but

allows such shareholders to authorize the waiver of such statutory pre-emption rights for five years. Our Articles of Association currently provide authority to the Board of Directors to issue shares without further shareholder approval and to waive ordinary shareholders statutory pre-emption rights. However, these authorizations expire in 2015, unless renewed by XL-Ireland s shareholders, and we can provide no assurance that these authorizations and waivers will always be renewed, which could limit our ability to issue equity in the future.

It may be difficult to enforce judgments against XL-Ireland, XL-Cayman or their directors and executive officers.

XL-Ireland is incorporated pursuant to the laws of Ireland. In addition, certain of our directors and officers reside outside the United States and a substantial portion of our assets and the assets of such directors and officers are located outside the United States. As such, it may be difficult or impossible to effect service of process within the United States upon those persons or to recover on judgments of U.S. courts against us or our directors and officers, including judgments predicated upon civil liability provisions of U.S. federal securities laws. We have been advised that there is no treaty between Ireland and the United States providing for the reciprocal enforcement of foreign judgments. The following requirements must be met before the foreign judgment will be deemed to be enforceable in Ireland:

- the judgment must be for a definite sum;
- the judgment must be final and conclusive; and
- the judgment must be provided by a court of competent jurisdiction.

An Irish court will also exercise its right to refuse judgment if the foreign judgment was obtained by fraud, if the judgment violated Irish public policy, if the judgment is in breach of natural justice or if it is irreconcilable with an earlier foreign judgment.

In addition, XL-Cayman is incorporated pursuant to the laws of the Cayman Islands and is an Irish tax resident. Requirements for enforceability of foreign judgments in Ireland are summarized above. We have been advised that there is doubt as to whether the courts of the Cayman Islands would enforce:

- judgments of U.S. courts based upon the civil liability provisions of U.S. federal securities laws obtained in actions against XL-Cayman or its directors and officers who reside outside the United States; or
- original actions brought in the Cayman Islands against these persons or XL-Cayman predicated solely upon U.S. federal securities laws.

We have also been advised that there is no treaty in effect between the United States and the Cayman Islands providing for such enforcement and there are grounds upon which Cayman Islands courts may not enforce judgments of U.S. courts. Some remedies available under the laws of U.S. jurisdictions, including some remedies available under U.S. federal securities laws, may not be allowed in Cayman Islands courts as contrary to public policy.

The ultimate outcome of lawsuits, including putative class action lawsuits, that have been filed against us by policyholders and security holders could have a material adverse effect on our consolidated financial condition, future operating results and/or liquidity.

We are subject to lawsuits and arbitrations in the regular course of our business. See Item 3, Legal Proceedings. In addition, lawsuits have been filed against us as discussed in Item 8, Note 17(g) to the Consolidated Financial Statements, Commitments and Contingencies Claims and Other Litigation. An adverse resolution of one or more of these items could have a material adverse effect on our results of operations in a particular fiscal quarter or year.

Changes in current accounting practices and future pronouncements may materially impact our reported financial results.

Unanticipated developments in accounting practices may require us to incur considerable additional expenses to comply with such developments, particularly if we are required to prepare information relating to prior periods for comparative purposes or to apply the new requirements retroactively. The impact of changes in current accounting practices and future pronouncements cannot be predicted but may affect the calculation of net income, net equity and other relevant financial statement line items and the timing of when impairments and other charges are tested or taken. In particular, recent guidance and ongoing projects put in place by standard setters globally have indicated a possible move away from the current insurance accounting models toward more fair value based models which could introduce significant volatility in the earnings of insurance industry participants.

There is a possibility that the Master Agreement entered into at the time of the sale of Syncora and the related commutations and releases could be challenged or that we could be subject to litigation as a result of the Master Agreement. Any such challenge could have a material adverse effect on our financial condition, results of operations, liquidity or the market price of our securities.

We provided certain reinsurance protections (the Reinsurance Agreements) with respect to adverse development on certain transactions as well as indemnification under specific facultative and excess of loss coverages for subsidiaries of Syncora: Syncora

Guarantee Re and Syncora Guarantee. At June 30, 2008, our total net exposure under facultative agreements with Syncora subsidiaries was approximately $6.4 billion of net par value outstanding. Pursuant to the closing of the Master Agreement, all of these Reinsurance Agreements were commuted.

In addition, through one or more of our subsidiaries, we entered into certain agreements with subsidiaries of Syncora pursuant to which we guaranteed certain obligations of Syncora Guarantee Re and Syncora Guarantee under specific agreements (the Guarantee Agreements). At June 30, 2008, the total net par value outstanding of business written by subsidiaries of Syncora which fell under the Guarantee Agreements was approximately $60 billion. Pursuant to the terms of, and required conditions under, the Master Agreement, Syncora Guarantee Re s facultative quota share reinsurance agreement with Syncora Guarantee, and all individual risk cessions thereunder, and the Financial Security Master Facultative Agreement, and all individual risk cessions thereunder, were commuted, thereby rendering the Syncora Guarantee Re guarantee and Financial Security guarantee of no further force and effect.

Following the closing of the Master Agreement, Syncora and its applicable subsidiaries were required to use commercially reasonable efforts to commute the underlying financial guarantees that are the subject of the EIB Guarantees, which was completed in June 2010.

While the New York Department of Financial Services (NYDFS) and the BMA approved the Master Agreement and related agreements and transactions, including the commutation of the agreements described above, and the Delaware Insurance Department (DID) approved the Master Agreement and the commutation of the Syncora Guarantee Re/Syncora Guarantee Quota Share, and although we believe the effect of the Master Agreement and subsequent commutation of the EIB Guarantee relieved us of all of our obligations under the Reinsurance Agreements and the Guarantee Agreements no assurance can be given that the enforceability of the Master Agreement, the agreements relating thereto and the transactions contemplated thereunder will not be challenged, including under applicable fraudulent transfer laws (described in the following paragraph) and/or by asserting any number of other theories for recovery, including third-party beneficiary rights, or that other litigation will not be commenced against us as a result of the Master Agreement and such related agreements and transactions. We believe that we would have significant defenses to any such challenges and would vigorously defend against any such claims. However, we cannot assure you that any such claims would not be made or, that any such claims would not ultimately be successful.

Under federal bankruptcy law and comparable provisions of state fraudulent transfer laws (including those applicable in any state insurance insolvency proceeding) Syncora s commutation and release of our obligations pursuant to the Master Agreement and related agreements would constitute a voidable fraudulent transfer if it was determined that Syncora or any applicable subsidiary thereto, at the time it entered into the Master Agreement or such related agreement:

- intended to hinder, delay or defraud its creditors; or
- received less than reasonably equivalent value or fair value consideration for such release; and either:
  - was insolvent or rendered insolvent by reason of such occurrence; or
  - was engaged in a business or transaction for which its remaining assets constituted unreasonably small capital; or
  - intended to incur, or believed that it would incur, debts beyond its ability to pay such debts as they mature.

Among other regulatory approvals obtained in connection with the Master Agreement, the NYDFS issued an approval letter to Syncora Guarantee under Section 1505 of the New York Insurance Law and the DID issued an approval letter to Syncora Guarantee Re under Section 5005(a) of the Delaware Insurance Code (effective upon Syncora Guarantee Re s redomestication to Delaware) (both of which require that the terms of a transaction between an issuer and one or more of its affiliates be fair and equitable) stating, in the case of NYDFS, that the terms of the Master Agreement and each of the commutations are fair and equitable to Syncora Guarantee and do not adversely affect policyholders of Syncora Guarantee and, in the case of the DID, stating that the terms of the Master Agreement and the commutation of the Syncora Guarantee Re/Syncora Guarantee Quota Share were fair and equitable to Syncora Guarantee. The BMA (the domiciliary regulator of Syncora Guarantee Re) also issued an approval letter approving the Master Agreement and each commutation to which Syncora Guarantee Re is a party, including the Syncora Guarantee Re/Syncora Guarantee Quota Share. There can be no assurance that a court would agree with our, the NYDFS s, the DID s, the BMA s or Syncora s conclusions, or as to what law or standard a court would ultimately apply in making any such determination or as to how such court would ultimately rule. Additionally, in the event of any liquidation or rehabilitation or similar proceeding of any insurance subsidiary of Syncora, there can be no assurance that any insurance regulator or regulators responsible for such proceedings, in their capacity as liquidator or rehabilitator, would respect the insurance regulatory approvals obtained in connection with the Master Agreement.

We and our non-U.S. insurance subsidiaries may become subject to U.S. tax, which may have a material adverse effect on our results of operations and your investment.

We take the position that neither we nor any of our non-U.S. insurance subsidiaries are engaged in a U.S. trade or business through a U.S. permanent establishment. Accordingly, we take the position that none of our non-U.S. insurance subsidiaries should be

subject to U.S. tax (other than U.S. excise tax on insurance and reinsurance premium income attributable to insuring or reinsuring U.S. risks and U.S. withholding tax on some types of U.S. source investment income). However, because there is considerable uncertainty as to the activities that constitute being engaged in a trade or business within the United States, we cannot be certain that the U.S. Internal Revenue Service (the IRS) will not contend successfully that we or any of our non-U.S. insurance subsidiaries are engaged in a trade or business in the United States. If we or any of our non-U.S. insurance subsidiaries were considered to be engaged in a trade or business in the United States, any such entity could be subject to U.S. corporate income and additional branch profits taxes on the portion of its earnings effectively connected to such U.S. business, in which case our financial condition and results of operations could be materially adversely affected.

Changes in U.S. tax law might adversely affect an investment in our shares.

The tax treatment of non-U.S. companies and their U.S. and non-U.S. insurance subsidiaries has been the subject of Congressional discussion and legislative proposals. For example, one legislative proposal would impose additional limits on the deductibility of interest by foreign-owned U.S. corporations. Another legislative proposal would modify the standards that indicate when a non-U.S. corporation might be treated as a U.S. corporation for U.S. federal income tax purposes if it were considered to be primarily managed and controlled in the U.S. In addition, legislation has been proposed in the U.S. that would severely restrict the ability of a company to utilize affiliate reinsurance to manage its U.S. risks and its capital position. Various proposals have been made that would effectively disallow (in some cases permanently and in others temporarily) part or all of the deduction for premiums ceded to affiliates If any of these proposals, or a similar proposal using the same underlying principles, is enacted, the resulting impact to the Company could have an adverse impact on us or our shareholders. It is possible that other legislative proposals could emerge in the future that could also have an adverse impact on us or our shareholders.

Additionally, the U.S. federal income tax laws and interpretations, including those regarding whether a company is engaged in a trade or business (or has a permanent establishment) within the United States or is a Passive Foreign Investment Company (PFIC), or whether U.S. holders would be required to include in their gross income subpart F income or the related person insurance income, which we refer to as RPII of a Controlled Foreign Corporation (CFC), are subject to change, possibly on a retroactive basis. There are currently no regulations regarding the application of the PFIC rules to insurance companies and the regulations regarding RPII are still in proposed form. New regulations or pronouncements interpreting or clarifying such rules may be forthcoming. We cannot be certain if, when or in what form such regulations or pronouncements may be provided and whether such guidance will have a retroactive effect.

We cannot assure you that future legislative action will not increase the amount of U.S. tax payable by us. If an increase occurs, our financial condition and results of operations could be materially adversely affected.

There is U.S. income tax risk associated with reinsurance between U.S. insurance companies and their Bermuda affiliates.

As discussed above, Congress has periodically considered legislation intended to eliminate certain perceived tax advantages of non-U.S. insurance companies and U.S. insurance companies with non-U.S. affiliates, including perceived tax benefits resulting principally from reinsurance between or among U.S. insurance companies and their non-U.S. affiliates. In this regard, section 845 of the IRS Code was amended in 2004 to permit the IRS to reallocate, recharacterize or adjust items of income, deduction or certain other items related to a reinsurance agreement between related parties to reflect the proper amount, source or character for each item (in contrast to prior law, which only covered source and character). If the IRS were to successfully challenge our reinsurance arrangements under section 845, our financial condition and results of operations could be materially adversely affected and the price of our ordinary shares could be adversely affected.

The Organisation for Economic Co-operation and Development has implemented measures (on Attribution of profits to Permanent Establishments) that might change the manner in which we are taxed.

On July 17, 2008, the Organisation for Economic Co-operation and Development (the OECD) issued the final version of its Report on the Attribution of Profits to Permanent Establishments (the Report). The Report is the final report on the OECD s project to establish a broad consensus regarding the interpretation and practical application of Article 7 of the OECD Model Tax Convention on Income and on Capital (Article 7). Article 7 sets forth international tax principles for attributing profits to a permanent establishment and forms the basis of an extensive network of bilateral income tax treaties between OECD member countries and between many OECD member and non-member countries. Part IV of the Report addresses the attribution of profits to a permanent establishment of an enterprise that conducts insurance activities.

The OECD implemented the conclusions of the Report in two phases. First, to provide improved certainty for the interpretation of existing treaties based on the current text of Article 7, the OECD revised the commentary to the current version of Article 7 to take into account the conclusions of the Report that did not conflict with the existing interpretation of Article 7 reflected in the previous commentary. Second, to reflect the full conclusions of the Report, the OECD issued, on July 22, 2010, a new version of Article 7 and related commentary to be used in the negotiation of new treaties and amendments to existing treaties. The provisions of the final version of new Article 7 and related commentary are not expected to change materially the manner in which we are taxed.

If an investor acquires 10% or more of our ordinary shares, it may be subject to taxation under the controlled foreign corporation rules.

Under certain circumstances, a U.S. person who owns 10% or more of the voting power of a foreign corporation that is a CFC (a foreign corporation in which 10% U.S. shareholders own more than 50% of the voting power of the foreign corporation or more than 25% of a foreign insurance company) for an uninterrupted period of 30 days or more during a taxable year must include in gross income for U.S. federal income tax purposes such 10% U.S. Shareholder s pro rata share of the CFC s subpart F income, even if the subpart F income is not distributed to such 10% U.S. Shareholder, if such 10% U.S. Shareholder owns (directly or indirectly through foreign entities) any shares of the foreign corporation on the last day of the corporation s taxable year. Subpart F income of a foreign insurance corporation typically includes foreign personal holding company income (such as interest, dividends and other types of passive income), as well as insurance and reinsurance income (including underwriting and investment income) attributable to the insurance of risks situated outside the CFC s country of incorporation.

While provisions in our organizational documents limit voting power on our ordinary shares, it is possible, that the IRS could challenge the effectiveness of these provisions and that a court could sustain such a challenge, in which case an investor s investment could be materially adversely affected, if the investor is considered to own 10% or more of our shares.

U.S. Persons who hold shares will be subject to adverse tax consequences if we are considered to be a PFIC for U.S. federal income tax purposes.

If we are considered a PFIC for U.S. federal income tax purposes, a U.S. person who owns any of our shares will be subject to adverse tax consequences, including a greater tax liability than might otherwise apply and tax on amounts in advance of when tax would otherwise be imposed, in which case an investor s investment could be materially adversely affected. In addition, if we were considered a PFIC, upon the death of any U.S. individual owning shares, such individual s heirs or estate would not be entitled to a step-up in the basis of the shares that might otherwise be available under U.S. federal income tax laws. We believe that we are not, have not been, and currently do not expect to become, a PFIC for U.S. federal income tax purposes. We cannot provide assurance, however, that we will not be deemed a PFIC by the IRS in the future. If we were considered a PFIC, it could have material adverse tax consequences for an investor that is subject to U.S. federal income taxation. There are currently no regulations regarding the application of the PFIC provisions to an insurance company. New regulations or pronouncements interpreting or clarifying these rules may be forthcoming. We cannot predict what impact, if any, such guidance would have on an investor that is subject to U.S. federal income taxation.

There are U.S. income tax risks associated with the related person insurance income of our non-U.S. insurance subsidiaries.

If (i) the related person insurance income, which we refer to as RPII, of any one of our non-U.S. insurance subsidiaries were to equal or exceed 20% of that subsidiary s gross insurance income in any taxable year and (ii) U.S. persons were treated as owning 25% or more of the subsidiary s stock (by vote or value), a U.S. person who owns any ordinary shares, directly or indirectly, on the last day of such taxable year on which the 25% threshold is met would be required to include in its income for U.S. federal income tax purposes that person s ratable share of that subsidiary s RPII for the taxable year, determined as if that RPII were distributed proportionately only to U.S. holders at that date, regardless of whether that income is distributed. The amount of RPII earned by a subsidiary (generally premium and related investment income from the direct or indirect insurance or reinsurance of any direct or indirect U.S. holder of shares of that subsidiary or any person related to that holder) would depend on a number of factors, including the identity of persons directly or indirectly insured or reinsured by that subsidiary. Although we do not believe that the 20% threshold will be met in respect of any of our non-U.S. insurance subsidiaries, some of the factors that may affect the result in any period may be beyond our control. Consequently, we cannot provide absolute assurance that we will not exceed the RPII threshold in any taxable year.

The RPII rules provide that if a holder who is a U.S. person disposes of shares in a non-U.S. insurance corporation that had RPII (even if the 20% gross income threshold was not met) and met the 25% ownership threshold at any time during the five-year period ending on the date of disposition, and the holder owned any stock at such time, any gain from the disposition will generally be treated as a dividend to the extent of the holder s share (taking into account certain rules for determining a U.S. holder s share of RPII) of the corporation s undistributed earnings and profits that were accumulated during the period that the holder owned the shares (possibly whether or not those earnings and profits are attributable to RPII). In addition, such a shareholder will be required to comply with specified reporting requirements, regardless of the amount of shares owned. We believe that these rules should not apply to dispositions of our ordinary shares because XL-Ireland is not itself directly engaged in the insurance business. We cannot provide absolute assurance, however, that the IRS will not successfully assert that these rules apply to dispositions of our ordinary shares.

We and our Bermuda insurance subsidiaries may become subject to taxes in Bermuda in the future, which may have a material adverse effect on our financial condition, results of operations and your investment.

Our Bermuda insurance subsidiaries have received from the Ministry of Finance in Bermuda exemptions from any Bermuda taxes that might be imposed on profits, income or any capital asset, gain or appreciation until March 31, 2035.

The exemptions are subject to the proviso that they are not construed so as to prevent the application of any tax or duty to such persons as are ordinarily resident in Bermuda (the Company and our Bermuda insurance subsidiaries are not so currently designated) and to prevent the application of any tax payable in accordance with the provisions of The Land Tax Act 1967 or otherwise payable in relation to the land leased to us and our Bermuda insurance subsidiaries. XL-Ireland and other Bermuda-based subsidiaries not incorporated in Bermuda, as permit companies under The Companies Act 1981 of Bermuda, have also received similar exemptions, which are also expected to be extended to 2035. Our Bermuda insurance subsidiaries are required to pay certain annual Bermuda government fees and certain business fees as an insurer under The Insurance Act 1978 of Bermuda. Currently there is no Bermuda withholding tax on dividends paid by our Bermuda insurance subsidiaries to us.

XL-Cayman may become subject to taxes in the Cayman Islands after June 2, 2018, which may have a material adverse effect on our results of operations and your investment.

For tax purposes, XL-Cayman is resident in Ireland by virtue of central management and control. In the event Cayman introduces a corporate income tax based on place of incorporation, XL-Cayman would be a dual resident company and potentially subject to tax in both Ireland and Cayman. As there is no double tax treaty between the Cayman Islands and Ireland, XL-Cayman could become subject to taxation in both Ireland and Cayman. Under current Cayman Islands law, we are not obligated to pay any taxes in the Cayman Islands on our income or gains. We have received an undertaking from the Governor-in-Council of the Cayman Islands pursuant to the provisions of the Tax Concessions Law, as amended, that until June 2, 2018, (i) no subsequently enacted law imposing any tax on profits, income, gains or appreciation shall apply to us and (ii) no such tax and no tax in the nature of an estate duty or an inheritance tax shall be payable on any of our ordinary shares, debentures or other obligations. Given the limited duration of the undertaking from the Governor-in-Council of the Cayman Islands, we cannot be certain that we will not be subject to any Cayman Islands tax after June 2, 2018. Such taxation could have a material adverse effect on our financial condition, results of operations and your investment.

Our tax position could be adversely impacted by changes in tax laws, tax treaties or tax regulations or the interpretation or enforcement thereof.

Our tax position could be adversely impacted by changes in tax laws, tax treaties or tax regulations or the interpretation or enforcement thereof by the tax authorities in Ireland, the United States and other jurisdictions, and such changes may be more likely or become more likely in view of recent economic trends in such jurisdictions, particularly if such trends continue. For example, Ireland has suffered from the consequences of worldwide adverse economic conditions and the credit ratings on its debt have been downgraded. Such tax law changes could cause a material and adverse change in our worldwide effective tax rate and we may have to take further action, at potentially significant expense, to seek to mitigate the effect of such changes. Any future amendments to the current income tax treaties between Ireland and other jurisdictions, including the United States, could subject us to increased taxation and/or potentially significant expense.

Dividends you receive may be subject to Irish dividend withholding tax and Irish income tax.

Dividend withholding tax (currently at a rate of 20%) may arise in respect of dividends paid on the Company s ordinary shares. However, a number of exemptions from dividend withholding tax exist such that ordinary shareholders resident in the United States and ordinary shareholders resident in other specified countries (listed in Annex F attached to the Redomestication Proxy Statement filed with the SEC on March 10, 2010) may be entitled to exemptions from dividend withholding tax if they complete and file certain dividend withholding tax forms. Ordinary shareholders resident in the U.S. that hold their ordinary shares through DTC will not be subject to dividend withholding tax provided the addresses of the beneficial owners of such ordinary shares in the records of the brokers holding such ordinary shares are in the United States (so that such brokers can further transmit the relevant information to a qualifying intermediary appointed by the Company). Similarly, ordinary shareholders resident in the U.S. that hold their ordinary shares outside of DTC are not subject to dividend withholding tax if such ordinary shareholders held ordinary shares in the Company on January 12, 2010 and they provided a valid Form W-9 showing a U.S. address to the Company s transfer agent. However, other ordinary shareholders may be subject to dividend withholding tax, which could adversely affect the price of our ordinary shares.

In addition, ordinary shareholders entitled to an exemption from Irish dividend withholding tax on dividends received from the Company should not be subject to Irish income tax in respect of those dividends, unless they have some connection with Ireland other than their ordinary shareholdings in the Company. Ordinary shareholders who receive dividends subject to Irish dividend withholding tax will generally have no further liability to Irish income tax on those dividends unless they have some connection with Ireland other than their ordinary shareholding in the Company.

A future transfer of your ordinary shares, other than one effected by means of the transfer of book entry interests in DTC, may be subject to Irish stamp duty.

Transfers of our ordinary shares effected by means of the transfer of book entry interests in DTC will not be subject to Irish stamp duty. The majority of our ordinary shares will be traded through DTC, either directly or through brokers who hold such ordinary shares on behalf of customers through DTC. However, if you hold your ordinary shares directly rather than beneficially through DTC (or through a broker that holds your ordinary shares through DTC), any transfer of your ordinary shares could be subject to Irish stamp duty (currently at the rate of 1% of the higher of the price paid or the market value of the ordinary shares acquired). Payment of Irish stamp duty is generally a legal obligation of the transferee. The potential for stamp duty could adversely affect the price of our ordinary shares.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company operates in Bermuda, the United States, Europe and various other locations around the world. In 1997, the Company acquired commercial real estate in Hamilton, Bermuda for the purpose of securing long-term office space for its worldwide headquarters. The development was completed in April 2001. The total cost of this development, including land, was approximately $126.6 million. The Company has subsequently sub-leased portions of this property as a part of its broader expense reduction initiatives.

In July 2003, the Company acquired new offices at 70 Gracechurch Street, London, which have become the Company s London headquarters. The acquisition was made through a purchase, sale and leaseback transaction. The move to the new offices was completed in 2004 and consolidated the Company s London businesses in one location. The capital lease asset and liability associated with this transaction totaled $100.7 million at December 31, 2011.

The majority of all other office facilities throughout the world that are occupied by the Company and its subsidiaries are leased.

Total rent expense for the years ended December 31, 2011, 2010 and 2009 was $32.9 million, $31.8 million and $34.4 million, respectively. See Item 8, Note 17(d) to the Consolidated Financial Statements, Commitments and Contingencies Properties, for discussion of the Company s lease commitments for real property.

ITEM 3. LEGAL PROCEEDINGS

In November 2006, a subsidiary of the Company received a grand jury subpoena from the Antitrust Division of the U.S. Department of Justice (DOJ) and a subpoena from the SEC, both of which sought documents in connection with an investigation into the municipal GICs market and related products. In June 2008, subsidiaries of the Company also received a subpoena from the Connecticut Attorney General and an Antitrust Civil Investigative Demand from the Office of the Florida Attorney General in connection with a coordinated multi-state Attorneys General investigation into the matters referenced in the DOJ and SEC subpoenas. The Company is fully cooperating with these investigations.

In August 2005, plaintiffs in a proposed class action (the Class Action) that was consolidated into a multidistrict litigation in the United States District Court for the District of New Jersey, captioned In re Brokerage Antitrust Litigation, MDL No. 1663, Civil Action No. 04-5184 (the MDL), filed a consolidated amended complaint (the Amended Complaint), which named as new defendants approximately 30 entities, including Greenwich Insurance Company, Indian Harbor Insurance Company and XL-Cayman (the XL Defendants). In the MDL, the Class Action plaintiffs asserted various claims purportedly on behalf of a class of commercial insureds against approximately 113 insurance companies and insurance brokers through which the named plaintiffs allegedly purchased insurance. The Amended Complaint alleged that the defendant insurance companies and insurance brokers conspired to manipulate bidding practices for insurance policies in certain insurance lines and failed to disclose certain commission arrangements and asserted statutory claims under the Sherman Act, various state antitrust laws and the Racketeer Influenced and Corrupt Organizations Act (RICO), as well as common law claims alleging breach of fiduciary duty, aiding and abetting a breach of fiduciary duty and unjust enrichment. By Opinion and Order dated August 31, 2007, the District Court dismissed the Sherman Act claims with prejudice and, by Opinion and Order dated September 28, 2007, the District Court dismissed the RICO claims with prejudice. The plaintiffs then appealed both Orders to the U.S. Court of Appeals for the Third Circuit. On August 16, 2010, the Third Circuit affirmed in large part the District Court s dismissal. The Third Circuit reversed the dismissal of certain Sherman Act and RICO claims alleged against several defendants including the XL Defendants but remanded those claims to the District Court for further consideration of their adequacy. In light of its reversal and remand of certain of the federal claims, the Third Circuit also reversed the District Court s dismissal (based on the District Court s declining to exercise supplemental jurisdiction) of the state-law claims against all defendants. On October 1, 2010, the remaining defendants, including the XL Defendants, filed motions to dismiss the remanded federal claims and the state-law claims. The motions were fully briefed in November 2010. In May 2011, a majority of the remaining defendants, including the XL Defendants, executed a formal Settlement Agreement with the Class Action plaintiffs to settle the Class Action and dismiss all claims with prejudice. The settlement was preliminarily approved by the District

Court in June 2011 and a final fairness hearing was held on September 14, 2011; the District Court has not yet decided the Class Action plaintiffs motion for approval of the settlement. The XL Defendants portion of the defendants aggregate settlement payment is $6.75 million.

Various XL entities have been named as defendants in three of the many tag-along actions that have been consolidated into the MDL for pretrial purposes. The complaints in these tag-along actions make allegations similar to those made in the Amended Complaint but do not purport to be class actions. On April 4, 2006, a tag-along complaint was filed in the U.S. District Court for the Northern District of Georgia on behalf of New Cingular Wireless Headquarters LLC and several other corporations and remains pending against approximately 100 defendants, including Greenwich Insurance Company, XL Specialty Insurance Company, XL Insurance America, Inc., XL Insurance Company Limited and XL-Cayman. On or about May 21, 2007, a tag-along complaint was filed in the U.S. District Court for the District of New Jersey on behalf of Henley Management Company, Big Bear Properties, Inc., Northbrook Properties, Inc., RCK Properties, Inc., Kitchens, Inc., Aberfeldy LP and Payroll and Insurance Group, Inc. against multiple defendants, including XL Winterthur International. On October 12, 2007, a complaint in a third tag-along action was filed in the U.S. District Court for the Northern District of Georgia by Sears, Roebuck & Co., Sears Holdings Corporation, Kmart Corporation and Lands End Inc. against many named defendants including X.L. America, Inc., XL Insurance America, Inc., XL Specialty Insurance Company and XL Insurance (Bermuda) Ltd. At a teleconference hearing on October 17, 2011, the District Court lifted the stay of the tag-along actions, including the three in which the XL entities are named defendants, and directed the parties to submit a proposed Scheduling Order that will include, among other things, deadlines for amending the Complaints in the tag-along actions and filing motions to dismiss the existing or amended Complaints.

XL-Cayman and one of its subsidiaries, Syncora, four Syncora officers, and various underwriters of Syncora securities were named in a Consolidated Amended Complaint filed in August 2008 in the Southern District of New York purportedly on behalf of a class of shareholders of Syncora. On September 27, 2011, the court entered a judgment dismissing the action with prejudice in its entirety, and the time for seeking rehearing or for filing a notice of appeal has now run without plaintiffs taking any action.

The Company and its subsidiaries are subject to litigation and arbitration in the normal course of its business. These lawsuits and arbitrations principally involve claims on policies of insurance and contracts of reinsurance and are typical for the Company and for the property and casualty insurance and reinsurance industry in general. Such legal proceedings are considered in connection with the Company s loss and loss expense reserves. Reserves in varying amounts may or may not be established in respect of particular claims proceedings based on many factors, including the legal merits thereof. In addition to litigation relating to insurance and reinsurance claims, the Company and its subsidiaries are subject to lawsuits and regulatory actions in the normal course of business that do not arise from or directly relate to claims on insurance or reinsurance policies. This category of business litigation typically involves, among other things, allegations of underwriting errors or misconduct, employment claims, regulatory activity, shareholder disputes or disputes arising from business ventures. The status of these legal actions is actively monitored by management.

Legal actions are subject to inherent uncertainties, and future events could change management s assessment of the probability or estimated amount of potential losses from pending or threatened legal actions. Based on available information, it is the opinion of management that the ultimate resolution of pending or threatened legal actions, both individually and in the aggregate, will not result in losses in amounts exceeding recognized reserves having a material adverse effect on the Company s position or liquidity at December 31, 2011. For further information in relation to legal proceedings, see Item 8, Note 17(g) to the Consolidated Financial Statements, Commitments and Contingencies Claims and Other Litigation.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

Executive Officers of the Registrant

The table below sets forth the names, ages and titles of the persons who were the executive officers of the Company at February 27, 2012:

Name	Age	Position
Michael S. McGavick	54	Chief Executive Officer and Director
Susan L. Cross	51	Executive Vice President and Global Chief Actuary
Kirstin Gould	45	Executive Vice President, General Counsel and Secretary
Gregory S. Hendrick	46	Executive Vice President and Chief Executive of Insurance Operations
W. Myron Hendry	63	Executive Vice President and Chief Platform Officer
Peter R. Porrino	55	Executive Vice President and Chief Financial Officer
Elizabeth L. Reeves	58	Executive Vice President, Chief Human Resources Officer
Jacob D. Rosengarten	56	Executive Vice President and Chief Enterprise Risk Officer
Sarah E. Street	50	Executive Vice President and Chief Investment Officer
James H. Veghte	55	Executive Vice President and Chief Executive of Reinsurance Operations

Michael S. McGavick, was appointed as Director of the Company in April 2008 and shortly prior to his commencement as the Company s Chief Executive Officer on May 1, 2008. Previously, Mr. McGavick was President & CEO of the Seattle-based Safeco Corporation from January 2001 to December 2005. Prior to joining Safeco, Mr. McGavick spent six years with the Chicago-based CNA Financial Corporation, where he held various senior executive positions before becoming President and Chief Operating Officer of the company s largest commercial insurance operating unit. Mr. McGavick s insurance industry experience also includes two years as Director of the American Insurance Association s Superfund Improvement Project in Washington D.C. where he became the Association s lead strategist in working to transform U.S. Superfund environmental laws.

Susan L. Cross was appointed to the Company s senior leadership team in August 2008, serving as Executive Vice President and Global Chief Actuary. Ms. Cross has served as Global Chief Actuary since 2006 and previously was Chief Actuary of the Company s reinsurance operations from 2004 to 2006 and Chief Actuary of XL Re Bermuda from 2002 to 2004. She also held various actuarial positions in the insurance and reinsurance operations of the Company from 1999 to 2002. Prior to joining the Company, Ms. Cross was Principal and Consulting Actuary at Tillinghast Towers Perrin.

Peter R. Porrino was appointed Executive Vice President, Chief Financial Officer in August 2011. Previously, Mr. Porrino served as Ernst & Young s Global Director of Insurance Industry Services from 1999 to August 2011. Mr. Porrino first joined Ernst & Young in 1978 and served in the firm s New York and National insurance practices for 15 years before leaving to serve in senior management positions with several insurance companies. This experience includes Zurich Financial Services, where Mr. Porrino served as CFO of Zurich s NYSE listed subsidiary, Zurich Reinsurance Centre, Inc. He rejoined Ernst & Young in 1999.

Kirstin Gould was appointed to the position of Executive Vice President, General Counsel in September 2007, which position includes her prior responsibilities as General Counsel, Corporate Affairs and Corporate Secretary. In 2008, Ms. Gould also assumed leadership of the Communications, Marketing and Public Affairs department. Ms. Gould was previously Executive Vice President, General Counsel, Corporate Affairs from July 2006 to September 2007 and also served as Chief Corporate Legal Officer from November 2004 to July 2006, and Associate General Counsel from July 2001 to November 2004. Prior to joining the Company in 2000, Ms. Gould was associated with the law firms of Clifford Chance and Dewey Ballantine in New York and London.

Gregory S. Hendrick was appointed Executive Vice President and Chief Executive of Insurance Operations in January 2012. From October 2010 to January 2012 Mr. Hendrick served as Executive Vice President, Strategic Growth. From 2004 to October 2010, Mr. Hendrick served as President and Chief Underwriting Officer of XL Re Ltd. Previously, he served as Lead for U.S. Property Treaty underwriting at XL Re Ltd and Vice President responsible for U.S. Property Underwriting for XL Mid Ocean Reinsurance Ltd. Prior to joining XL, Mr. Hendrick was Assistant Vice President of Treaty Underwriting for the Winterthur Reinsurance Corporation of America.

W. Myron Hendry joined the Company s senior leadership team upon his appointment as Executive Vice President, Chief Platform Officer in December 2009. Prior to joining the Company, from 2006 to December 2009 Mr. Hendry served as Business Operations Executive of Bank of America s Insurance Group, joining there from a merger with Countrywide Insurance Services Group. Prior to the merger, Mr. Hendry served as Managing Director and Chief Operating Officer for Countrywide and prior to this, from 2004 to 2006, Mr. Hendry served as Senior Vice President, Property and Casualty Services at Safeco. From 1971 to 2004, Mr. Hendry held various leadership roles with CNA Insurance, with his last assignment being the Senior Vice President of Worldwide Operations.

Elizabeth L. Reeves was appointed to the Company s senior leadership team in June 2009, serving as Executive Vice President, Chief Human Resources Officer, where she is responsible for global compensation, employee benefits, employee relations, recruiting, learning, organizational development, performance management, talent development, succession planning, HR information

systems and Payroll. Prior to joining the Company, from August 2008 to May 2009, Ms. Reeves served as Senior Vice President and Chief Human Resources Officer at Liz Claiborne, Incorporated. Prior to that, from January 2005 to May 2008, Ms. Reeves served as Senior Vice President of Human Resources at Lincoln Financial Group.

Jacob D. Rosengarten joined the Company s senior leadership team and was appointed Executive Vice President, Chief Enterprise Risk Officer in September 2008. Prior to joining the Company, Mr. Rosengarten served as Managing Director of Risk Management and Analytics for Goldman Sachs Asset Management from 1998 to 2008. From 1993 to 1997, Mr. Rosengarten served as Director of Risk and Quantitative Analysis at Commodities Corporation and prior to this, from 1983 to 1992 held progressively senior finance positions at Commodities Corporation.

Sarah E. Street was appointed to the position of Executive Vice President and Chief Investment Officer in October 2006. Ms. Street has also served as the Chief Executive Officer of XL Capital Investment Partners Inc. since April 2001. Prior to joining XL in 2001, Ms. Street held numerous leadership positions at JPMorganChase and its predecessor organizations, working in a number of corporate finance units as well as in the capital markets business of the bank.

James H. Veghte was appointed Executive Vice President, Chief Executive of Reinsurance Operations in January 2006. Mr. Veghte had served as the Chief Executive Officer of XL Reinsurance America Inc. (XLRA) since 2004, having previously served as Chief Operating Officer of the Company s reinsurance operations and President, Chief Operating Officer & Chief Underwriting Officer of XL Re Ltd. Additional previously held roles with the Company include President of XL Re Latin America Ltd., Chief Operating Officer of Le Mans Re (now the French branch of XL Re Europe Ltd.), General Manager of XL Re Ltd s London branch and Executive Vice President and Underwriter of XL Mid Ocean Reinsurance Ltd in Bermuda. Prior to joining XL, Mr. Veghte was Senior Vice President and Chief Underwriting Officer of Winterthur Reinsurance Corporation of America.

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company s ordinary shares, $0.01 par value per share, are listed on the NYSE under the symbol XL.

The following table sets forth the high, low and closing sales prices per share of the Company s ordinary shares per fiscal quarter, as reported on the New York Stock Exchange Composite Tape:

	High	Low	Close
2011:			
1st Quarter	$ 24.82	21.17	24.60
2nd Quarter	25.43	20.53	21.98
3rd Quarter	22.65	17.94	18.80
4th Quarter	23.00	17.69	19.77
2010:			
1st Quarter	$ 19.54	15.91	18.90
2nd Quarter	20.39	15.63	16.01
3rd Quarter	22.14	15.59	21.66
4th Quarter	22.52	19.36	21.82

The number of record holders of ordinary shares as of February 24, 2011 was 175. This figure does not represent the actual number of beneficial owners of the Company s ordinary shares because such shares are frequently held in street name by securities dealers and others for the benefit of individual owners who may vote the shares.

In 2011, four quarterly dividends of $0.11 per share were paid to all ordinary shareholders of record as of March 15, June 15, September 15 and December 15. In 2010, four quarterly dividends were paid at $0.10 per share to all ordinary shareholders of record as of March 15, June 15, September 15 and December 15.

The declaration and payment of future dividends by the Company will be at the discretion of the Board of Directors and will depend upon many factors, including the Company s earnings, financial condition, business needs, capital and surplus requirements of the Company s operating subsidiaries and regulatory and contractual restrictions.

As a holding company, the Company s principal source of income is dividends or other statutorily permissible payments from its subsidiaries. The ability to pay such dividends is limited by the applicable laws and regulations of the various countries in which the Company s subsidiaries operate, including Bermuda, the U.S. and the U.K., applicable requirements of the Society of Lloyd s, and certain contractual provisions. See Item 1, Business Regulation, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Note 23 to the Consolidated Financial Statements, Statutory Financial Data, for further discussion.

Information concerning securities authorized for issuance under equity compensation plans is incorporated by reference to Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Purchases of Equity Securities by the Issuer and Affiliate Purchases

The following table provides information about purchases by the Company during the quarter ended December 31, 2011 of equity securities that are registered by the Company pursuant to Section 12 of the Exchange Act:

Period	Total Number of Shares Purchased	Average Price Paid per share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1) (2)
October		$		$ 290.4 million
November	1,867,423	$ 19.29	1,865,000	$ 254.4 million
December	3,080,820	$ 20.76	3,080,820	$ 190.5 million
Total	4,948,243	$ 20.21	4,945,820	$ 190.5 million

(1) Shares purchased in connection with the vesting of restricted shares granted under the Company s restricted stock plan do not represent shares purchased as part of publicly announced plans or programs. All such purchases were made in connection with satisfying tax withholding obligations of those employees. These shares were not purchased as part of the Company s share buyback program noted below.

(2) On November 2, 2010, the Company announced that its Board of Directors approved a share buyback program, authorizing the Company to purchase up to $1.0 billion of its ordinary shares. During 2010, the Company purchased and canceled 6.9 million ordinary shares under this program for $144.0 million. During 2011, the Company purchased and canceled 31.7 million ordinary shares under this program for $665.5 million. All share buybacks were carried out by way of redemption in accordance with Irish law and the Company s constitutional documents. All shares so redeemed were canceled upon redemption. At both December 31, 2011 and February 24, 2012, $190.5 million remained available to be used for purchases under this program.

Ordinary Share Performance Graph

Set forth below is a line graph comparing the yearly dollar change in the cumulative total shareholder return over a five-year period on the Company s ordinary shares from December 31, 2006 through December 31, 2011 as compared to the cumulative total return of the Standard & Poor s 500 Stock Index and the cumulative total return of the Standard & Poor s Property & Casualty Insurance Index. The companies included in these indices or noted as competitors under Item 1, Business, may not be included in the Company s compensation peer group.

The graph shows the value on December 31, 2007, 2008, 2009, 2010 and 2011, of a $100 investment made on December 31, 2006, with all dividends reinvested.

ITEM 6. SELECTED FINANCIAL DATA

The selected consolidated financial data below is based upon the Company s fiscal year end of December 31. The selected consolidated financial data should be read in conjunction with the Consolidated Financial Statements and the Notes thereto presented under Item 8.

	2011	2010	2009	2008	2007
	(U.S. dollars in thousands, except per share amounts)				
Income Statement Data:					
Net premiums earned	$ 5,690,130	$ 5,414,061	$ 5,706,840	$ 6,640,102	$ 7,205,356
Net investment income	1,137,769	1,198,038	1,319,823	1,768,977	2,248,807
Net realized (losses) gains on investments	(188,359)	(270,803)	(921,437)	(962,054)	(603,268)
Net realized and unrealized gains (losses) on derivative instruments	(10,738)	(33,843)	(33,647)	(73,368)	(55,451)
Net income (loss) from investment fund affiliates (1)	26,253	51,102	78,867	(277,696)	326,007
Fee income and other	41,748	40,027	43,201	52,158	14,271
Net losses and loss expenses incurred (2)	4,078,391	3,211,800	3,168,837	3,962,898	3,841,003
Claims and policy benefits life operations	535,074	513,833	677,562	769,004	888,658
Acquisition costs, operating expenses and foreign exchange gains and losses	1,868,250	1,749,202	1,994,194	1,921,940	2,188,889
Interest expense	205,592	213,643	216,504	351,800	621,905
Loss on settlement of guarantee		23,500			
Extinguishment of debt				22,527	
Impairment of goodwill	429,020			989,971	
Amortization of intangible assets	1,438	1,858	1,836	2,968	1,680
Income (loss) before non-controlling interests, net income from operating affiliates and income tax expense	(420,962)	684,746	134,714	(872,989)	1,593,587
Income (loss) from operating affiliates (1)(2)	76,786	121,372	60,480	(1,458,246)	(1,059,848)
Preference share dividends (3)	72,278	74,521	80,200	78,645	69,514
Net income (loss) attributable to ordinary shareholders	(474,760)	585,472	206,607	(2,632,458)	206,375

	2011	2010	2009	2008	2007
	(U.S. dollars in thousands, except per share amounts)				
Per Share Data:					
Net income (loss) per ordinary share basic (4)(8)	$ (1.52)	$ 1.74	$ 0.61	$ (10.94)	$ 1.14
Net income (loss) per ordinary share diluted (4)(8)	$ (1.52)	$ 1.73	$ 0.61	$ (10.94)	$ 1.14
Weighted average ordinary shares outstanding diluted (4)	312,896	337,709	340,966	240,657	181,209
Cash dividends per ordinary share	$ 0.44	$ 0.40	$ 0.40	$ 1.14	$ 1.52
Balance Sheet Data:					
Total investments available for sale	$ 27,017,285	$ 27,677,553	$ 29,307,171	$ 27,464,510	$ 36,265,803
Total investments held to maturity	2,688,978	2,728,335	546,067		
Cash and cash equivalents	3,825,125	3,022,868	3,643,697	4,353,826	3,880,030
Investments in affiliates	1,052,729	1,127,181	1,242,810	1,552,789	2,611,149
Unpaid losses and loss expenses recoverable	3,654,948	3,671,887	3,584,028	3,997,722	4,697,471
Premiums receivable	2,411,611	2,414,912	2,597,602	3,135,985	3,637,452
Total assets	44,626,077	45,015,944	45,655,391	45,693,015	57,785,867
Unpaid losses and loss expenses	20,613,901	20,531,607	20,823,524	21,650,315	23,207,694
Future policy benefit reserves	4,845,394	5,075,127	5,490,119	5,452,865	6,772,042
Unearned premiums	3,555,310	3,484,830	3,651,310	4,217,931	4,681,989
Notes payable and debt	2,275,327	2,457,003	2,442,914	3,179,963	2,860,598
Shareholders equity	10,769,410	10,613,049	9,432,417	6,116,831	9,950,561
Fully diluted book value per ordinary share	$ 29.64	$ 29.78	$ 24.60	$ 15.46	$ 50.29
Operating Ratios:					
Loss and loss expense ratio (5)	76.6%	63.8%	61.5%	66.2%	59.8%
Underwriting expense ratio (6)	30.9%	31.0%	32.1%	28.7%	29.0%
Combined ratio (7)	107.5%	94.8%	93.6%	94.9%	88.8%

(1) The Company generally records the income related to alternative fund affiliates on a one month lag and the private investment fund affiliates on a three month lag in order for the Company to meet the filing deadlines for its periodic reports. The Company generally records the income related to operating affiliates on a three month lag.

(2) In 2008, net loss from operating affiliates includes losses totaling approximately $1.4 billion related to the closing of the Master Agreement as well as losses recorded throughout 2008 and up until the closing of the Master Agreement that were associated with previous reinsurance and guarantee agreements with Syncora. In 2007, $351.0 million of financial guarantee reserves related to reinsurance agreements with Syncora were recorded within net loss from operating affiliates. In 2010, net income from operating affiliates included $50.2 million relating to sale of a majority of the Company s shareholding in Primus Guaranty Ltd.

(3) Preference dividends represent dividends on the Redeemable Series C preference ordinary shares and the Series D and E preference ordinary shares. Following the Company s redomestication, subsequent to July 1, 2010, the Redeemable Series C preference ordinary shares and the Series E preference ordinary shares represent non-controlling interests in the consolidated financial statements of the Company. For additional information see Item 8, Note 1 to the Consolidated Financial Statements, General.

(4) Effective for the fiscal year beginning January 1, 2009 and for all interim periods within 2009, the Company adopted final authoritative guidance that addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing basic earnings per share (EPS) pursuant to the two-class method described in EPS guidance. A share-based payment award that contains a non-forfeitable right to receive cash when dividends are paid to ordinary shareholders irrespective of whether that award ultimately vests is considered a participating security as these rights to dividends provide a non-contingent transfer of value to the holder of the share-based payment award. Accordingly, these awards are included in the computation of basic EPS pursuant to the two-class method. Under the terms of the Company s restricted stock awards, grantees are entitled to receive dividends on the unvested portions of their awards. There is no requirement to return these dividends in the event the unvested awards are forfeited in the future. Accordingly, this guidance had an impact on the Company s EPS calculations. All prior period EPS data presented has been adjusted retrospectively to conform to the provisions of this guidance. The adoption of this guidance reduced basic loss per ordinary share for fiscal 2008 by $0.08, and reduced basic earnings per ordinary share by $0.02, for fiscal 2007, and reduced diluted loss per ordinary share for fiscal 2008 by $0.08 and reduced diluted earnings per ordinary share by $0.01 for fiscal 2007.

(5) The loss and loss expense ratio related to the property and casualty operations is calculated by dividing the losses and loss expenses incurred by the net premiums earned for the Insurance and Reinsurance segments.

(6) The underwriting expense ratio related to the property and casualty operations is the sum of acquisition expenses and operating expenses for the Insurance and Reinsurance segments divided by net premiums earned for the Insurance and Reinsurance segments. See Item 8,

Note 4 to the Consolidated Financial Statements, Segment Information, for further information.

(7) The combined ratio related to the property and casualty operations is the sum of the loss and loss expense ratio and the underwriting expense ratio. A combined ratio under 100% represents an underwriting profit and over 100% represents an underwriting loss.

(8) Effective April 1, 2009, the Company adopted final authoritative guidance that addressed the treatment of credit losses on investments. This guidance was not applied retroactively. For additional information see Item 8, Note 2(r) to the Consolidated Financial Statements, Recent Accounting Pronouncements.

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management s Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements which involve inherent risks and uncertainties. Statements that are not historical facts, including statements about the Company s beliefs and expectations, are forward-looking statements. These statements are based upon current plans, estimates and expectations. Actual results may differ materially from those projected in such forward-looking statements, and therefore undue reliance should not be placed on them. See Cautionary Note Regarding Forward-Looking Statements, for a list of additional factors that could cause actual results to differ materially from those contained in any forward-looking statement.

This discussion and analysis should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto presented under Item 8.

Certain aspects of the Company s business have loss experience characterized as low frequency and high severity. This may result in volatility in both the Company s results of operations and financial condition.

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EXECUTIVE OVERVIEW

Background

The Company, through its subsidiaries, is a global insurance and reinsurance company providing property, casualty and specialty products to industrial, commercial and professional firms, insurance companies and other enterprises on a worldwide basis. The Company operates in markets where it believes its underwriting expertise and financial strength represent a relative advantage.

The Company has grown through acquisitions and development of new business opportunities. Acquisitions included Global Capital Re in 1997, Mid Ocean Limited in 1998, ECS, Inc. and NAC Re Corp. in 1999, Winterthur International in 2001 and Le Mans Re in 2002. All acquisitions were entered into in order to further support the Company s strategic plan to develop a global platform in insurance and reinsurance. The Company competes as an integrated global business and at December 31, 2011 employed 3,818 employees in 24 countries. For further information in relation to the Company s Operations, see Item 1, Business.

Impact of Recent Natural Catastrophes

In 2011, the global insurance and reinsurance markets experienced significant losses from natural catastrophes, including the 2011 flooding events in Australia (the Australia floods), the earthquake that struck Christchurch, New Zealand on February 22, 2011 (the New Zealand earthquake), the March 11, 2011 earthquake and tsunami in Japan (the Japan earthquake and tsunami), the severe weather occurrences, including tornado activity, in the United States over the periods April 22-28 and May 20-23, 2011 (the U.S. Storms), third quarter Atlantic storm activity, particularly Hurricane Irene and Tropical Storm Lee (the Atlantic Hurricanes) and the widespread flooding in Thailand that reached its highest point during the fourth quarter (the Thailand floods). See Significant Items Affecting Results of Operations 1) The impact of significant large natural catastrophe activity below for a discussion of the Company s loss estimates for the three months and year ended December 31, 2011 from natural catastrophes.

Underwriting Environment

The Company earns its revenue primarily from net premiums written and earned. The property and casualty insurance and reinsurance markets have historically been cyclical, meaning that based on market conditions, there have been periods where premium rates are high and policy terms and conditions are more favorable to the Company (a hard market) and there have been periods where premium rates decline and policy terms and conditions are less favorable to the Company (a soft market). Market conditions are driven primarily by competition in the marketplace, the supply of capital in the industry, investment yields and the frequency and severity of loss events. Management s goal is to build long-term shareholder value by capitalizing on current opportunities and managing through any cyclical downturns by reducing its property and casualty book of business and exposures if and when rates deteriorate during soft market periods.

Insurance - Underwriting Environment

The trading environment for the core lines of insurance business written by the Company remains difficult as competitive pressures continue, although there have been signs of improvement during the second half of 2011. The Company continues its disciplined underwriting approach to grow on a very selective basis and exit lines where margins are unacceptable. Overall, retention ratios have continued to improve while premium rates were broadly flat for the year. The Insurance segment experienced rate increases in the North America P&C and Specialty lines which were offset by declines in the highly competitive U.S. professional lines while the International P&C line was effectively flat for the year.

The Company continues to develop new business opportunities in several areas, including its North American construction and surety businesses, which were announced in 2010 and its political risk and North America inland marine businesses, which were announced during the fourth quarter of 2011. Geographic expansion also continues with the opening of an office in China in April 2011 and the recent approval from the Brazilian regulators to expand the Company s presence there complementing the Reinsurance operation with an Insurance segment branch offering Casualty, Property, Professional and Specialty products.

Reinsurance - Underwriting Environment

The January 1 renewals for the Reinsurance segment saw positive pricing across the catastrophe books of business and certain Specialty lines, while Casualty rates overall were broadly flat. U.S. D&O continued to show rate deterioration in this very competitive line of business.

Given the level of global catastrophe losses this year, both loss impacted and non-loss impacted programs in the U.S. and International books of business experienced significant rate increases, particularly in International, while the increases on European catastrophe books were more modest, in the single digit percentages.

The following sets forth potential trends relevant to the Company s property and casualty operations:

2012 Underwriting Outlook

Throughout 2009 and 2010, the Company was focused on selective growth initiatives, emphasizing short-tail lines, where applicable, in the Company s reinsurance operations, exiting other businesses, such as Casualty facultative business and non-renewing certain insurance programs, as well as continuing to reduce long-term agreements within the insurance operations in order to take advantage of improvements in market conditions when and where they occur.

In 2011, while several of these initiatives continued, the Company also shifted its focus to concentrate on strategic growth and investment in areas where the Company believes it can achieve appropriate future returns. Recent strategic growth initiatives included the continued expansion of the U.S. construction and surety lines, the addition of political risks and North America inland marine businesses, new innovative products, including further build-out of a product recall policy for the food and beverage industry, the establishment of a Middle East team in the U.K. and an Accident and Health team in the U.S., and the continued move into emerging markets, including China and Brazil. The Company also made significant investment in 2011 to improve systems to both achieve greater efficiency and to create a platform from which the Company can grow as markets allow. In 2012 and beyond, this focus on strategic growth and investment will continue.

The following is a summary of the January 2012 rate indications and recent renewal activity for each of the Insurance and Reinsurance segments of the Company:

Insurance - 2012 Underwriting Outlook

With regard to market conditions, within the Insurance segment s core lines of business, fourth quarter and full year 2011 renewals reflected broadly flat premium rates in aggregate, however, there were several favorable signs of improvement. For the third consecutive quarter, the segment experienced positive pricing in its North America P&C business unit at an increase of 2%. Specialty pricing was also positive for the year at 2% and there was material improvement in the U.S. D&O book during the fourth quarter as rate decreases slowed and certain 2012 renewals are yielding rate increases. For the year the segment experienced percentage rate decline in the low single digits.

The Company continues to focus on those lines of business that it believes provide the best return on capital, including the writing of selective new business and remaining committed to the underwriting actions initially taken in 2009. For 2012, initial indications are consistent with current market conditions described above. In the International P&C business unit, where nearly 40% of the book renews on January 1, the Company s initial pricing indications are broadly stable. Casualty rates were flat to slightly down and property rates were showing increases in the low to mid single digits.

Reinsurance - 2012 Underwriting Outlook

As noted above, the pricing environment on the primary side is showing rate growth with the exception of Professional lines. This generally positive pricing momentum should benefit the U.S. and International casualty books where a significant amount of proportional reinsurance is written. In addition, the Reinsurance segment continues to develop new business opportunities in several areas, including in an improving U.K. motor market pricing environment, and in marine and energy following Deepwater Horizon and other recent industry loss events in these lines. For 2012, the Reinsurance segment expects to continue to build upon the strategic growth achieved in 2011 and will utilize the Company s broad market relationships and experience to seek opportunities to achieve this.

There can be no assurance, however, that such (re)insurance rate conditions or growth opportunities will be sustained or further materialize, or lead to improvements in our books of business. See Cautionary Note Regarding Forward-Looking Statements.

Investment Environment

The Company seeks to generate income and book value growth from investment activities through returns on its investment portfolio. The Company s current investment strategy seeks to support the liabilities arising from the operations of the Company, generate investment income and build book value over the longer term. During the year ended December 31, 2011, interest rates declined in the Company s major markets and credit spreads widened, particularly in the Euro-zone. The Company s results of operations and investment portfolio during the year ended December 31, 2011 were impacted by these trends. Net investment income yields were negatively impacted by lower interest rates which in turn reduced prevailing yields on reinvestment income. Net realized losses resulted from sales transactions primarily on European financials including hybrid securities and non-Agency RMBS offset partially by gains on Agency MBS and Government and Government Related and Supported securities. The impact of decreasing government rates offset by widening credit spreads during the year ended December 31, 2011 was the primary reason for the improvement in the net unrealized position on fixed maturities and short-term investments over the course of the year. For further information, see Investment Activities below.

RESULTS OF OPERATIONS AND KEY FINANCIAL MEASURES

Results of Operations

The following table presents an analysis of the Company s net income (loss) attributable to ordinary shareholders and other financial measures (described below) for the years ended December 31, 2011, 2010 and 2009:

(U.S. dollars in thousands, except share and per share amounts)	2011	2010	2009
Net income (loss) attributable to ordinary shareholders	$ (474,760)	$ 585,472	$ 206,607
Earnings (loss) per ordinary share basic	$ (1.52)	$ 1.74	$ 0.61
Earnings (loss) per ordinary share diluted	$ (1.52)	$ 1.73	$ 0.61
Weighted average number of ordinary shares and ordinary share equivalents basic	312,896	336,283	340,612
Weighted average number of ordinary shares and ordinary share equivalents diluted	312,896	337,709	340,966

Key Financial Measures

The following are some of the financial measures management considers important in evaluating the Company s operating performance in the Company s P&C operations:

(U.S. dollars in thousands, except ratios and per share amounts)	2011	2010	2009
Underwriting profit P&C operations	$ (397,353)	$ 262,494	$ 327,306
Combined ratio P&C operations	107.5%	94.8%	93.6%
Net investment income P&C operations (1)	$ 819,708	$ 884,866	$ 987,398
Book value per ordinary share (2)	$ 29.85	$ 30.37	$ 24.64
Fully diluted book value per ordinary share (3)	$ 29.64	$ 29.78	$ 24.60
Return on average ordinary shareholders equity (4)	(5.0)%	6.5%	3.1%

(1) Net investment income relating to P&C operations includes the net investment income related to the net results from structured products.

(2) Book value per ordinary share, a non-GAAP financial measure, is calculated by dividing ordinary shareholders equity (total shareholders equity less preference shareholders equity and non-controlling interest in equity of consolidated subsidiaries) by the number of outstanding ordinary shares at any period end. Book value per ordinary share is affected primarily by the Company s net income (loss), by any changes in the net unrealized gains and losses on its investment portfolio, currency translation adjustments and also the impact of any share buyback or issuance activity. Ordinary shareholders equity was $9.43 billion, $9.61 billion and $8.43 billion and the number of ordinary shares outstanding was 315.7 million, 316.5 million and 342.1 million at December 2011, 2010 and 2009, respectively. Ordinary shares outstanding include all ordinary shares legally issued and outstanding (as disclosed on the face of the balance sheet) as well as all director share units outstanding.

(3) Fully diluted book value per ordinary share, a non-GAAP financial measure, represents book value per ordinary share combined with the dilutive impact of potential future share issuances at period end. The Company believes that fully diluted book value per ordinary share is a financial measure important to investors and other interested parties. However, this measure may not be comparable to similarly titled measures used by companies either outside or inside of the insurance industry.

(4) Return on average ordinary shareholders equity (ROE) is a non-GAAP financial measure and is calculated by dividing the net income (loss) for the year by the average of the opening and closing ordinary shareholders equity. See Return on Ordinary Shareholders Equity Calculation herein for a reconciliation of ROE to average ordinary shareholders equity.

Underwriting profit property and casualty operations

One way that the Company evaluates the performance of its insurance and reinsurance operations is by underwriting profit or loss. The Company does not measure performance based on the amount of gross premiums written. Underwriting profit or loss is calculated from premiums earned less net losses incurred and expenses related to underwriting activities. The Company s underwriting profit (loss) in the year ended December 31, 2011 was consistent with the combined ratio discussed below.

Combined ratio property and casualty operations

The combined ratio for P&C operations is used by the Company and many other insurance and reinsurance companies as another measure of underwriting profitability. The combined ratio is calculated from the net losses incurred and underwriting expenses as a ratio of the net premiums earned for the Company s insurance and reinsurance operations. A combined ratio of less than 100% indicates an underwriting profit and greater than 100% reflects an underwriting loss. The Company s combined ratio for the year ended December 31, 2011 reflects an underwriting loss and is higher than the same period in the previous year, primarily as a result of an increase in the loss and loss expense ratio, partially offset by a marginal decrease in the underwriting expense ratio. The loss and loss expense ratio has increased as a result of higher levels of catastrophe losses, higher large loss activity in the energy, property and marine businesses of the Insurance segment and other large loss events in U.S. property including a deterioration in the performance of a large U.S. agricultural program in the Reinsurance segment.

The Company s combined ratio for the year ended December 31, 2010 is higher than for the same period in the previous year, primarily as a result of an increase in the loss and loss expense ratio, partially offset by a marginal decrease in the underwriting expense ratio. The loss and loss expense ratio has increased as a result of higher levels of catastrophe losses and other large loss events in both the insurance and reinsurance segments. For further information on the combined ratio, see Income Statement Analysis below.

Net investment income property and casualty (P&C) operations

Net investment income related to P&C operations is an important measure that affects the Company s overall profitability. The largest liability of the Company relates to its unpaid loss reserves, and the Company s investment portfolio provides liquidity for claims settlements of these reserves as they become due. As a result, a significant part of the investment portfolio is invested in fixed income securities. Net investment income is influenced by a number of factors, including the amounts and timing of inward and outward cash flows, the level of interest rates and credit spreads and changes in overall asset allocation. See the segment results at Investment Activities below for a discussion of the Company s net investment income for the year ended December 31, 2011.

Book value per ordinary share

Management also views the change in the Company s book value per ordinary share as an additional measure of the Company s performance. Book value per ordinary share is a non-GAAP financial measure and is calculated by dividing ordinary shareholders equity (total shareholders equity less preference shareholders equity and non-controlling interest in equity of consolidated subsidiaries) by the number of outstanding ordinary shares at any period end. Ordinary shares outstanding include all ordinary shares legally issued and outstanding (as disclosed on the face of the balance sheet) as well as all director share units outstanding. Book value per ordinary share is affected by the Company s net income (loss), any changes in the net unrealized gains and losses on its investment portfolio and currency translation adjustments and also the positive impact of any share buyback or issuance activity.

Book value per ordinary share decreased by $0.52 in the year ended December 31, 2011 as compared to an increase of $5.73 during 2010. The decrease in 2011 was primarily due to the net loss attributable to ordinary shareholders of $474.8 million and the impact of settlement of the forward purchase contracts associated with the 10.75% equity security units (the 10.75% Units), which resulted in the issuance of an aggregate of 30,456,600 ordinary shares, partially offset by an increase in net unrealized gains on available for sale investments and the benefit of share buyback activity.

The increase in 2010 was a result of improved investment portfolio fair values, higher net income and the impact of share buyback activity. During 2010, there was a decrease in net unrealized losses on available for sale investments of $1.1 billion, net of tax, as compared to December 31, 2009. The improved investment portfolio fair values were due in large part to declining interest rates during 2010 but also tightening spreads.

Fully diluted book value per ordinary share is a non-GAAP financial measure and represents book value per ordinary share combined with the impact from dilution of share based compensation and certain conversion features where dilutive. Fully diluted book value per ordinary share decreased by $0.14 and increased by $5.18 during the years ended December 31, 2011 and 2010, respectively, as a result of the factors noted above.

Return on average ordinary shareholders equity

ROE is another non-GAAP financial measure that management considers important in evaluating the Company s operating performance. ROE is calculated by dividing the net income attributable to ordinary shareholders for any period by the average of the opening and closing ordinary shareholders equity. The Company establishes minimum target ROEs for its total operations, segments and lines of business. If the Company s minimum ROE targets over the longer term are not met with respect to any line of business, the Company seeks to modify and/or exit this line. In addition, among other factors, the Company s compensation of its senior officers is dependent on the achievement of the Company s performance goals to enhance ordinary shareholder value as measured by ROE (adjusted for certain items considered to be non-operating in nature).

In 2011, ROE was negative due to the net loss from the significant catastrophe losses and the impairment of goodwill, both discussed under Significant Items Affecting the Results of Operations. and other large loss events. See Return on Ordinary Shareholders Equity Calculation herein for a reconciliation of ROE to average ordinary shareholders equity.

In 2010, ROE was 6.5%, 3.4 percentage points higher than for the same period in the prior year when it was 3.1%. This was the result of increased net income which was largely offset by significantly higher equity levels during 2010 following the increase in the fair value of the Company s investment portfolio.

SIGNIFICANT ITEMS AFFECTING THE RESULTS OF OPERATIONS

The Company s net income and other financial measures as shown above for the year ended December 31, 2011 have been affected by, among other things, the following significant items:

1) The impact of significant large natural catastrophe activity;

2) Continuing competitive factors impacting the underwriting environment;

3) Net favorable prior year loss development;

4) Market movement impacts on the Company s investment portfolio; and

5) Goodwill impairment charge recorded in the fourth quarter of 2011.

1. The impact of significant large natural catastrophe activity

The following table outlines the underwriting losses and loss ratio impact for the Insurance and Reinsurance segments from natural catastrophes for the years ended December 31:

	Natural Catastrophe Underwriting Losses			Natural Catastrophe Loss Ratio Impact		
(U.S. dollars in thousands, except ratios)	2011	2010	2009	2011	2010	2009
Insurance	$ 355,256	$ 135,771	$ 10,744	9.6%	3.8%	0.3%
Reinsurance	405,870	158,574	41,604	25.2%	10.6%	2.7%
Total P&C	$ 761,126	$ 294,345	$ 52,348	14.4%	5.8%	1.0%

Notable natural catastrophes during the year ended December 31, 2011 included the Australia floods, the New Zealand earthquake, the Japan earthquake and tsunami, the U.S. Storms, the Atlantic Hurricanes and the Thailand floods.

Notable natural catastrophes during 2010 included the Chilean Earthquake, European Windstorm Xynthia, U.S. tornadoes and hailstorm activity, the New Zealand Earthquake and floods in Central Europe, China, Poland and Queensland, Australia.

In 2009, natural catastrophes included Hailstorm Wolfgang, Japanese earthquake, Windstorm Klaus, Typhoon Ketsana, Asian earthquake and tsunami and Australian wildfires.

The Company s loss estimates are based on combinations of its review of individual treaties and policies expected to be impacted, commercial model outputs, client data received to the date the estimates are made, and consideration of expectations of total insured market loss estimates if available, both from published sources and the Company s internal analysis. The Company s loss estimates involve the exercise of considerable judgment due to the complexity and scale of the insured events, and are, accordingly, subject to revision as additional information becomes available. Actual losses may differ materially from these preliminary estimates.

The following are analyses of the financial impact on the Company s results of operations for the three months and year ended December 31, 2011 from natural catastrophes:

(U.S. dollars in thousands, except ratios)	Three Months Ended December 31, 2011			Year Ended December 31, 2011		
	Insurance	**Reinsurance**	**Total**	**Insurance**	**Reinsurance**	**Total**
Operating data:						
Catastrophe reinstatement premium earned:						
Australia floods	$	$ (475)	$ (475)	$	$ 475	$ 475
New Zealand earthquake		1,960	1,960		602	602
Japan earthquake and tsunami		518	518		17,148	17,148
U.S. Storms		91	91		1,160	1,160
Atlantic Hurricanes (1)	258		258	(7,242)	929	(6,313)
Thailand floods	(3,403)	6,044	2,641	(3,403)	6,044	2,641
Other natural catastrophes (2) (3)		504	504		2,880	2,880
Total net premiums earned	$ (3,145)	$ 8,642	$ 5,497	$ (10,645)	$ 29,238	$ 18,593
Gross losses and loss expenses:						
Australia floods	$ (630)	$ 3	$ (627)	$ (80,855)	$ (15,623)	$ (96,478)
New Zealand earthquake		(2,204)	(2,204)	(5,000)	(99,198)	(104,198)
Japan earthquake and tsunami	(4,585)	7,549	2,964	(93,185)	(179,085)	(272,270)
U.S. Storms	(56)	(16,625)	(16,681)	(5,660)	(79,278)	(84,938)
Atlantic Hurricanes (1)	(60,902)	3,869	(57,033)	(192,893)	(15,335)	(208,228)
Thailand floods	(123,237)	(61,643)	(184,880)	(123,237)	(61,643)	(184,880)
Other natural catastrophes (2) (3)	(7,833)	(141)	(7,974)	(21,243)	(23,823)	(45,066)
Total gross losses and loss expenses	$ (197,243)	$ (69,192)	$ (266,435)	$ (522,073)	$ (473,985)	$ (996,058)
Losses and loss expenses recoverable:						
Australia floods	$	$	$	$ 27,525	$	$ 27,525
New Zealand earthquake		(2,082)	(2,082)		32,017	32,017
Japan earthquake and tsunami	472	(200)	272	14,072		14,072
U.S. Storms		1,128	1,128	315	5,952	6,267
Atlantic Hurricanes (1)	39,709	(79)	39,630	105,359	508	105,867
Thailand floods	24,483		24,483	24,483		24,483
Other natural catastrophes (2) (3)	2,642		2,642	5,708	400	6,108
Total losses and loss expenses recoverable	$ 67,306	$ (1,233)	$ 66,073	$ 177,462	$ 38,877	$ 216,339
Underwriting loss - P&C Operations:						
Australia floods	$ (630)	$ (472)	$ (1,102)	$ (53,330)	$ (15,148)	$ (68,478)
New Zealand earthquake		(2,326)	(2,326)	(5,000)	(66,579)	(71,579)
Japan earthquake and tsunami	(4,113)	7,867	3,754	(79,113)	(161,937)	(241,050)
U.S. Storms	(56)	(15,406)	(15,462)	(5,345)	(72,166)	(77,511)
Atlantic Hurricanes (1)	(20,935)	3,790	(17,145)	(94,776)	(13,898)	(108,674)
Thailand floods	(102,157)	(55,599)	(157,756)	(102,157)	(55,599)	(157,756)
Other natural catastrophes (2) (3)	(5,191)	363	(4,828)	(15,535)	(20,543)	(36,078)

Total underwriting loss	$ (133,082)	$ (61,783)	$ (194,865)	$ (355,256)	$ (405,870)	$ (761,126)
Loss ratio impact for the three months and year ended December 31, 2011	13.9%	15.0%	14.2%	9.6%	25.2%	14.4%

(1) Atlantic Hurricanes refers to Hurricane Irene and Tropical Storm Lee.
(2) For the Insurance segment, for the year ended December 31, 2011, Other natural catastrophes include U.S. windstorms, Missouri River flooding, Mississippi floods and Storm Rolf.
(3) For the Reinsurance segment for the year ended December 31, 2011, Other natural catastrophes include Cyclone Yasi in Australia, the Slave Lake fire in Canada, Texas wildfires and the Danish floods.

For further details see the segment results in the Income Statement Analysis below.

2. Continuing competitive factors impacting the underwriting environment

Soft market conditions were experienced across most lines of business throughout 2009, 2010 and 2011. This resulted in an overall decrease in gross and net premiums written in 2010 and 2009 but these amounts increased in 2011 due to new strategic initiatives. For further information in relation to the underwriting environment, including details relating to rates and retention, see Executive Overview Underwriting Environment, above.

3. Net favorable prior year loss development

Net favorable prior year loss development occurs when there is a decrease to loss reserves recorded at the beginning of the year, resulting from actual or reported loss development for prior years that is less than expected loss development. Net prior year adverse loss development occurs when there is an increase to loss reserves recorded at the beginning of the year, resulting from actual or reported loss development for prior years exceeding expected loss development.

The following table presents the net (favorable) adverse prior year loss development of the Company s loss and loss expense reserves for its property and casualty operations which include the Insurance and Reinsurance segments for each of the years indicated:

(U.S. dollars in millions)	2011	2010	2009
Insurance segment	$ (76.5)	$ (127.4)	$ (62.9)
Reinsurance segment	(208.4)	(245.5)	(221.8)
Total	$ (284.9)	$ (372.9)	$ (284.7)

The Company is a major writer of large, complex energy-related (re)insurance coverages and manages its exposure through, among other items, the purchase of reinsurance. Recent developments have reduced some of the uncertainty surrounding the Company s third party liability exposure to losses arising from the Deepwater Horizon oil rig explosion, including settlements by companies subject to lawsuits and judicial rulings in respect of the applicability and extent of contractual indemnities. In 2011, the Company strengthened its overall net incurred position relating to Deepwater Horizon across insurance and reinsurance segments by $72.7 million for a total net incurred to date of $165.7 million as at year end including both property damage and liability exposures. Very recent judicial decisions upholding indemnities owing from BP p.l.c. to other companies subject to lawsuits may be favorable to the Company s overall position. Despite the level of strengthening incurred resulting from this unusual event, the Company s total net reserves developed favorably by $285 million during 2011 as shown in the above table.

See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Note 10 to the Consolidated Financial Statements, Losses and Loss Expenses, for further information regarding the developments in prior year loss reserve estimates for each of the years indicated within each of the Company s operating segments.

4. Market movement impacts on the Company s investment portfolio

During the year ended December 31, 2011, credit spreads widened, particularly in Euro-zone, offset by decreasing interest rates. The net impact of the market conditions on the Company s investment portfolio for the year ended December 31, 2011 was favorable and resulted in an increase in the net unrealized position of on available for sale investments as compared to December 31, 2010 of $558.1 million. This represents approximately a 2.0% appreciation on average available for sale assets for the year ended December 31, 2011.

The following table provides further detail regarding the movements in the global credit markets, as well as in government interest rates using some sample market indices:

	Interest Rate Movement for the year ended December 31, 2011 (1) (+ / - represents increases / decreases in interest rates)	Credit Spread Movement for the year ended December 31, 2011 (2) (+ / - represents widening / tightening of credit spreads)
United States	-118 basis points (5 year Treasury)	+94 basis points (US Corporate A rated) +6 basis points (US Mortgage Master Index) +23 basis points (US CMBS, AAA rated)
United Kingdom	-142 basis points (10 year Gilt)	+72 basis points (UK Corporate, AA rated)
Euro-zone	-108 basis points (5 year Bund)	+122 basis points (Europe Corporate, A rated)

(1) Source: Bloomberg Finance L.P.
(2) Source: Merrill Lynch Global Indices.

Net realized losses on investments in the year ended December 31, 2011 totaled $188.4 million, including net realized losses of approximately $160.2 million related to the impairment of certain of the Company s fixed income investments, where the Company determined that there was an other-than-temporary decline in the value of those investments related to credit. For further analysis of this, see Results of Operations below.

5. Goodwill impairment charge recorded in the fourth quarter of 2011

The Company performs periodic impairment testing related to goodwill as circumstances require, in addition to its annual testing as of June 30 each year. The interim impairment test completed during the fourth quarter of 2011 resulted in a non-cash goodwill impairment charge of $429.0 million. The charge relates to the Insurance segment. The impairment was determined using the methodologies as described within Critical Accounting Policies and Estimates below, which includes discounted cash flow analyses and comparison with similar companies using their publicly traded price multiples as the basis for valuation. Continued low valuations in the insurance industry as a whole combined with several years of poor underwriting performance in the segment have impacted the technical valuations; however, management continues to see significant value in the Company s global insurance platform. For further information, see Item 8, Note 8 to the Consolidated Financial Statements, Goodwill and Other Intangible Assets and see further discussion under Critical Accounting Policies and Estimates.

OTHER KEY FOCUSES OF MANAGEMENT

Throughout 2011 and into 2012, the Company remained focused on, among other things, managing its capital, tailoring the Company s business model to focus on core P&C business, optimizing the P&C investment portfolio, and enhancing its enterprise risk management capabilities. The Company continues to focus on those lines of business within its Insurance and Reinsurance segments that provide the best return on capital. Details of these and other initiatives are outlined below.

Capital Management

Fundamental to supporting the Company s business model is its ability to underwrite business, which is largely dependent upon the quality of its claims paying and financial strength ratings as evaluated by independent rating agencies. As a result, in the event that the Company is downgraded, its ability to write business, as well as its financial condition and/or results of operations, could be adversely affected.

Buybacks of Ordinary Shares

On September 24, 2007, the Company s Board of Directors approved a share buyback program, authorizing the Company to purchase up to $500.0 million of its ordinary shares. As of January 1, 2010, $375.4 million ordinary shares remained available for purchase under that program. During 2010, the Company purchased and canceled 18.8 million ordinary shares under the program for $375.4 million, the full amount that had remained under that buyback program.

On November 2, 2010, the Company announced that its Board of Directors approved a share buyback program, authorizing the Company to purchase up to $1.0 billion of its ordinary shares. During 2010, the Company purchased and canceled 6.9 million ordinary shares under this program for $144.0 million. During 2011, the Company purchased and canceled 31.7 million ordinary shares under this program for $665.5 million. All share buybacks were carried out by way of redemption in accordance with Irish law and the Company s constitutional documents. All shares so redeemed were canceled upon redemption. At December 31, 2011, $190.5 million remained available to be used for purchases under this program. No further buybacks have been made as of February 24, 2012.

Sale of 5.75% Senior Notes

On September 30, 2011, XL-Cayman completed the public sale of $400 million aggregate principal amount of 5.75% Senior Notes (the 5.75% Senior Notes) due 2021 at the issue price of 100% of the principal amount. The 5.75% Senior Notes are fully and unconditionally guaranteed by XL-Ireland. The 5.75% Senior Notes bear interest at a rate of 5.75% per annum, payable semiannually, beginning on April 1, 2012, and mature on October 1, 2021. XL-Cayman may redeem the 5.75% Senior Notes, in whole or part, from time to time in accordance with the terms of the indenture pursuant to which the 5.75% Senior Notes were issued. XL-Cayman received net proceeds of approximately $395.9 million from the offering, which were used to partially repay the $600 million principal amount outstanding of the 6.5% Guaranteed Senior Notes due January 2012 (the XLCFE Notes), which were issued by XL Capital Finance (Europe) plc (XLCFE).

Repayment of the XLCFE Notes

On January 15, 2012, the $600 million principal amount outstanding of the XLCFE Notes was repaid at maturity.

Equity Security Units

In August 2011, in accordance with the terms of the 10.75% Units, XL-Cayman purchased and retired all of the 8.25% senior notes due August 2021 (the 8.25% Senior Notes) for $575 million in a remarketing. These notes comprised a part of the 10.75% Units. The proceeds from the remarketing were used to satisfy the purchase price for XL-Ireland s ordinary shares issued to holders of the 10.75% Units pursuant to the forward purchase contracts comprising a part of the 10.75% Units. Each forward purchase contract provided for the issuance of 1.3242 ordinary shares of XL-Ireland at a price of $25 per share. The settlement of the forward purchase

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contracts resulted in XL-Ireland s issuance of an aggregate of 30,456,600 ordinary shares for an aggregate purchase price of $575 million. As a result of the settlement of the forward purchase contracts, the 10.75% Units ceased to exist and are no longer traded on the NYSE.

Series C Preference Ordinary Shares

On March 26, 2009, the Company completed a cash tender offer for a portion its outstanding Redeemable Series C preference ordinary shares that resulted in approximately 12.7 million Redeemable Series C preference ordinary shares with a liquidation value of $317.3 million being purchased by the Company for approximately $104.7 million plus accrued and unpaid dividends, combined with professional fees totaling $0.8 million. As a result, a book value gain to ordinary shareholders of approximately $211.8 million was recorded in the first quarter of 2009.

On February 12, 2010, the Company repurchased a portion of its outstanding Redeemable Series C preference ordinary shares, which resulted in approximately 4.4 million Redeemable Series C preference ordinary shares with a liquidation value of $110.8 million being purchased by the Company for approximately $94.2 million. As a result, a book value gain of approximately $16.6 million was recorded in the first quarter of 2010 to ordinary shareholders.

On February 16, 2011, the Company repurchased 30,000 of the outstanding Redeemable Series C preference ordinary shares with a liquidation preference value of $0.75 million for $0.65 million.

On August 15, 2011, XL-Cayman completed a cash tender offer for its outstanding Redeemable Series C preference ordinary shares that resulted in 2,811,000 Redeemable Series C preference ordinary shares with a liquidation value of $25 per share being repurchased and canceled by XL-Cayman for approximately $71.0 million including accrued and unpaid dividends and professional fees. Subsequent to the expiration of the tender offer, and on the same terms as the offer, XL-Cayman repurchased and canceled the remaining outstanding Redeemable Series C preference ordinary shares for approximately $0.9 million plus accrued and unpaid dividends. As of December 31, 2011, no Redeemable Series C preference ordinary shares were outstanding.

Series D Preference Ordinary Shares

On October 15, 2011, XL-Cayman issued 350,000 non-cumulative Series D Preference Ordinary Shares for $350 million of cash and liquid investments that were held in a trust account that was part of the Stoneheath Re (Stoneheath) facility. Holders of the non-cumulative perpetual preferred securities (Stoneheath Securities) issued by Stoneheath in December 2006 received one Series D Preference Ordinary Share in exchange for each Stoneheath Security. Dividends on the non-cumulative Series D Preference Ordinary Shares are declared and paid quarterly at a floating rate of three-month LIBOR plus 3.120% on the liquidation preference. The Series D Preference Ordinary Shares are perpetual securities with no fixed maturity dates and are not convertible into any of the Company s other securities.

On December 5, 2011, the Company repurchased 5,000 of the outstanding Series D Preference Ordinary Shares with a liquidation preference value of $5.0 million for $3.7 million, including accrued dividends. As a result of these repurchases, the Company recorded a gain of approximately $1.3 million through Non-controlling interests in the Consolidated Statement of Income in the fourth quarter of 2011.

Series E Preference Ordinary Shares

On March 15, 2007, the Company issued 1.0 million Fixed/Floating Series E Perpetual Non-Cumulative preference ordinary shares, par value $0.01 each, with liquidation preference $1,000 per share (the Series E preference ordinary shares). The Company received net proceeds of approximately $983.8 million from the offering. The Series E preference ordinary shares are perpetual securities with no fixed maturity date and are not convertible into any of the Company s other securities.

On February 16, 2011, the Company repurchased 500 of the outstanding Series E preference ordinary shares with a liquidation preference value of $0.50 million for $0.47 million. As a result of these repurchases, the Company recorded a reduction in Non-controlling interests of approximately $0.13 million in the first quarter of 2011.

Risk Management

The Company s risk management and risk appetite framework is detailed at Item 1, Business - Enterprise Risk Management. The table below shows the Company s estimated per event net 1% and 0.4% exceedance probability exposures for certain peak natural catastrophe peril regions. These estimates assume that amounts due from reinsurance and retrocession purchases are 100% collectible. There may be credit or other disputes associated with these potential receivables. Finally, the probable maximum losses in the table below were derived by application of a new vendor model that was released during the first quarter of 2011 and, accordingly, could be more unreliable than the model that was used historically.

			1-in-100 Event		1-in-250 Event	
Geographical Zone *(U.S. dollars in millions)*	**Peril**	**Measurement Date of In-Force Exposures (1)**	**Probable Maximum Loss (2)**	**Percentage of Tangible Shareholders Equity at December 31, 2011**	**Probable Maximum Loss (2)**	**Percentage of Tangible Shareholders Equity at December 31, 2011**
North America	Earthquake	October 1, 2011	$ 785	7.6%	$ 1,263	12.2%
North Atlantic	Windstorm	October 1, 2011	1,338	12.9%	1,710	16.5%
U.S.	Windstorm	October 1, 2011	1,319	12.7%	1,695	16.4%
Europe	Windstorm	October 1, 2011	474	4.6%	636	6.1%
Japan	Earthquake	October 1, 2011	240	2.3%	323	3.1%
Japan	Windstorm	October 1, 2011	131	1.3%	193	1.9%

(1) Detailed analyses of aggregated in-force exposures and maximum loss levels are done periodically. The measurement dates represent the date of the last completed detailed analysis by geographical zone.

(2) Probable maximum losses include secondary uncertainty which incorporates variability around the expected probable maximum loss for each event, does not represent the Company s maximum potential exposures and are pre-tax.

See Significant Items Affecting the Results of Operations - 1) The impact of significant large natural catastrophe activity above.

Regulatory Change

Management continues to actively monitor the various regulatory bodies and initiatives that impact the Company globally and assess the potential for significant impact on results or operations. The European Commission is in the process of implementing changes to the prudential regulation of European insurers, known as Solvency II, with a timeline to achieve full compliance by January 1, 2014. Solvency II is designed to impose economic risk-based solvency requirements across all EU Member States. Advice and implementation consists of three pillars: (1) Pillar I quantitative capital requirements, based on a valuation of the entire balance sheet; (2) Pillar II qualitative regulatory review, which includes governance, internal controls, enterprise risk management and supervisory review process, and (3) Pillar III market discipline, which is accomplished through reporting of the insurer s financial condition to regulators and the public. Other jurisdictions such as Bermuda and Canada are in the process of implementing consistent changes to strengthen their capital and risk management requirements in order to be considered equivalent for purposes of group regulatory considerations. The Company has significant resources supporting the regulatory process, such as the Solvency II Quantitative Impact Studies and Bermuda Monetary Authority regulatory data calls, and these resources are also actively engaged in the implementation of Solvency II related measures across the Company.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The following are considered to be the Company s critical accounting policies and estimates due to the judgments and uncertainties affecting the application of these policies and/or the likelihood that materially different amounts would be reported under different conditions or using different assumptions. If actual events differ significantly from the underlying assumptions or estimates applied for any or all of the accounting policies (either individually or in the aggregate), there could be a material adverse effect on the Company s results of operations, financial condition and liquidity. These critical accounting policies have been discussed by management with the Audit Committee of the Company s Board of Directors.

Other significant accounting policies are nevertheless important to an understanding of the Company s Consolidated Financial Statements. Policies such as those related to revenue recognition, financial instruments and consolidation require difficult judgments on complex matters that are often subject to multiple sources of authoritative guidance. See Item 8, Note 2 to the Consolidated Financial Statements, Significant Accounting Policies.

1) Unpaid Loss and Loss Expenses and Unpaid Loss and Loss Expenses Recoverable

As the Company earns premiums for the underwriting risks it assumes, it also establishes an estimate of the expected ultimate losses related to the premium. Loss reserves for unpaid loss and loss expenses are established due to the significant periods of time that may elapse between the occurrence, reporting and settlement of a loss. The process of establishing reserves for unpaid property and casualty claims can be complex and is subject to considerable variability, as it requires the use of informed estimates and judgments. These estimates and judgments are based on numerous factors, and may be revised as additional experience and other data become available and are reviewed, as new or improved methodologies are developed or as current laws change. Loss reserves include:

a) Case reserves reserves for reported losses and loss expenses that have not yet been settled; and

b) IBNR reserves reserves for incurred but not reported losses or for reported losses over and above the amount of case reserves.

Case Reserves

Case reserves for the Company s property and casualty operations are established by management based on amounts reported from insureds or ceding companies and consultation with legal counsel, and represent the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company. The method of establishing case reserves for reported claims differs among the Company s operations.

With respect to the Company s insurance operations, the Company is notified of insured losses and records a case reserve for the estimated amount of the settlement, if any. The estimate reflects the judgment of claims personnel based on general reserving practices, the experience and knowledge of such personnel regarding the nature of the specific claim and, where appropriate, advice of legal counsel. Reserves are also established to provide for the estimated expense of settling claims, including legal and other fees and the general expenses of administering the claims adjustment process. With respect to the Company s reinsurance operations, case reserves for reported claims are generally established based on reports received from ceding companies. Additional case reserves may be established by the Company to reflect the estimated ultimate cost of a loss. The uncertainty in the reserving process for reinsurers is due, in part, to the time lags inherent in reporting from the original claimant to the primary insurer to the reinsurer. As a predominantly broker market reinsurer for both excess-of-loss and proportional contracts, the Company is subject to a potential additional time lag in the receipt of information as the primary insurer reports to the broker who in turn reports to the Company. As of December 31, 2011, the Company did not have any significant backlog related to its processing of assumed reinsurance information.

Since the Company relies on information regarding paid losses, case reserves and IBNR provided by ceding companies in order to assist it in estimating its liability for unpaid losses and LAE, the Company maintains certain procedures in order to help determine the completeness and accuracy of such information. Periodically, management assesses the reporting activities of its ceding companies on the basis of qualitative and quantitative criteria. In addition to conferring with ceding companies or brokers on claims matters, the Company s claims personnel conduct periodic audits of specific claims and the overall claims procedures of its ceding companies at their offices. The Company relies on its ability to effectively monitor the claims handling and claims reserving practices of ceding companies in order to help establish the proper reinsurance premium for reinsurance agreements and to establish proper loss reserves. Disputes with ceding companies have been rare and generally have been resolved through negotiation.

In addition to information received from ceding companies on reported claims, the Company also utilizes information on the pattern of ceding company loss reporting and loss settlements from previous catastrophic events in order to estimate the Company s ultimate liability related to catastrophic events such as hurricanes. Commercial catastrophe model analyses and zonal aggregate exposures are utilized to assess potential client loss before and after an event. Initial cedant loss reports are generally obtained shortly after a catastrophic event, with subsequent updates received as new information becomes available. The Company actively requests

loss updates from cedants periodically whilst there is still considerable uncertainty for an event, often for the first year following an event. The Company s claim settlement processes also incorporate an update to the total loss reserve at the time a claim payment is made to a ceding company.

While the reliance on loss reports from ceding companies may increase the level of uncertainty associated with the estimation of total loss reserves for property catastrophe reinsurance relative to direct property insurance, there are several factors which serve to reduce the uncertainty in loss reserve estimates for property catastrophe reinsurance. First, for large natural catastrophe events, aggregate limits in property catastrophe reinsurance contracts are generally fully exhausted by the loss reserve estimates. Second, as a reinsurer, the Company has access to information from a broad cross section of the insurance industry. The Company utilizes such information in order to perform consistency checks on the data provided by ceding companies and is able to identify trends in loss reporting and settlement activity and incorporate such information in its estimate of IBNR reserves. Finally, the Company also supplements the loss information received from cedants with loss estimates developed by market share techniques and/or from third party catastrophe models applied to exposure data supplied by cedants.

IBNR Reserves

IBNR reserves represent management s best estimate, at a given point in time, of the amount in excess of case reserves that is needed for the future settlement and loss adjustment costs associated with claims incurred. It is possible that the ultimate liability may differ materially from these estimates. Because the ultimate amount of unpaid losses and LAE is uncertain, the Company believes that quantitative techniques to estimate these amounts are enhanced by professional and managerial judgment. Management reviews the IBNR estimates produced by the Company s actuaries who determine the best estimate of the liabilities to record in the Company s financial statements. The Company considers this single point estimate to be the mean expected outcome.

IBNR reserves are estimated by the Company s actuaries using several standard actuarial methodologies including the loss ratio method, the loss development or chain ladder method, the Bornhuetter-Ferguson (BF) method and frequency and severity approaches. IBNR related to a specific event may be based on the Company s estimated exposure to an industry loss and may include the use of catastrophe modeling software. On a quarterly basis, IBNR reserves are reviewed by the Company s actuaries, and are adjusted as new information becomes available. Any such adjustments are accounted for as changes in estimates and are reflected in the results of operations in the period in which they are made.

The Company s actuaries use one set of assumptions in calculating the single point estimate, which includes actual loss data, loss development factors, loss ratios, reported claim frequency and severity. The actuarial reviews and documentation are completed in accordance with professional actuarial standards with reserves established on a basis consistent with GAAP. The selected assumptions reflect the actuary s judgment based on historical data and experience combined with information concerning current underwriting, economic, judicial, regulatory and other influences on ultimate claim settlements.

When estimating IBNR reserves, each of the Company s insurance and reinsurance business units segregate business into exposure classes. Within each class, the business is further segregated by either the year in which the contract incepted (underwriting year), the year in which the claim occurred (accident year), or the year in which the claim is reported (report year). The majority of the Insurance segment is reviewed on an accident year basis. Professional lines insurance business is reviewed on a report year basis due to the claims made nature of the underlying policies. The majority of the Reinsurance segment is reviewed on an underwriting year basis.

Generally, initial actuarial estimates of IBNR reserves not related to a specific event are based on the loss ratio method applied to each class of business. Actual paid losses and case reserves (reported losses) are subtracted from expected ultimate losses to determine IBNR reserves. The initial expected ultimate losses involve management judgment and are based on historical information for that class of business; which includes loss ratios, market conditions, changes in pricing and conditions, underwriting changes, changes in claims emergence, and other factors that may influence expected ultimate losses.

Over time, as a greater number of claims are reported, actuarial estimates of IBNR are based on the BF method and loss development techniques. The BF method utilizes actual loss data and the expected patterns of loss emergence, combined with an initial expectation of ultimate losses to determine an estimate of ultimate losses. This method may be appropriate when there is limited actual loss data and a relatively less stable pattern of loss emergence. The chain ladder method utilizes actual loss and expected patterns of loss emergence to determine an estimate of ultimate losses that is independent of the initial expectation of ultimate losses. This method may be appropriate when there is a relatively stable pattern of loss emergence and a relatively larger number of reported claims. Multiple estimates of ultimate losses using a variety of actuarial methods are calculated for each of the Company s classes of business for each year of loss experience. The Company s actuaries look at each class and determine the most appropriate point estimate based on the characteristics of the particular class and other relevant factors, such as historical ultimate loss ratios, the presence of individual large losses, and known occurrences that have not yet resulted in reported losses. Once the Company s actuaries make their determination of the most appropriate point estimate for each class, this information is aggregated and presented to management for review and approval.

The pattern of loss emergence is determined using actuarial analysis, including judgment, and is based on the historical patterns of the recording of paid and reported losses by the Company, as well as industry information. Information that may cause historical patterns to differ from future patterns is considered and reflected in expected patterns as appropriate. For property, marine and aviation insurance, losses are generally reported within 2 to 3 years from the beginning of the accident year. For casualty insurance, loss emergence patterns can vary from 3 years to over 20 years depending on the type of business. For other insurance, loss emergence patterns fall between the property and casualty insurance. For reinsurance business, loss reporting lags the corresponding insurance classes often by at least one quarter due to the need for loss information to flow from the ceding companies to the Company generally via reinsurance intermediaries. Such lags in loss reporting are reflected in the actuary s selections of loss reporting patterns used in establishing the Company s reserves.

Such estimates are not precise because, among other things, they are based on predictions of future developments and estimates of future trends in claim severity, claim frequency, and other issues. In the process of estimating IBNR reserves, provisions for economic inflation and changes in the social and legal environment are considered, but involve considerable judgment. When estimating IBNR reserves, more judgment is typically required for lines of business with longer loss emergence patterns.

Due to the low frequency and high severity nature of some of the business underwritten by the Company, the Company s reserve estimates are highly dependent on actuarial and management judgment and are therefore uncertain. In property classes, there can be additional uncertainty in loss estimation related to large catastrophe events. With wind events, such as hurricanes, the damage assessment process may take more than a year. The cost of claims is subject to volatility due to supply shortages for construction materials and labor. In the case of earthquakes, the damage assessment process may take several years as buildings are discovered to have structural weaknesses not initially detected. The uncertainty inherent in IBNR reserve estimates is particularly pronounced for casualty coverages, such as excess liability, professional liability coverages, and workers compensation, where information emerges relatively slowly over time.

The Company s three types of property and casualty reserve exposure with the longest tails are:

(1) high layer excess casualty insurance;

(2) casualty reinsurance; and

(3) discontinued asbestos and long-tail environmental business.

Certain aspects of the Company s casualty operations complicate the actuarial process for establishing reserves. Certain casualty business written by the Company s insurance operations is high layer excess casualty business, meaning that the Company s liability attaches after large deductibles including self insurance or insurance from sources other than the Company. The Company commenced writing this type of business in 1986 and issued policies in forms that were different from traditional policies used by the industry at that time. Initially, there was a lack of industry data available for this type of business. Consequently, the basis for establishing loss reserves by the Company for this type of business was largely judgmental and based upon the Company s own reported loss experience which was used as a basis for determining ultimate losses, and therefore IBNR reserves. Over time, the amount of available historical loss experience data has increased. As a result, the Company has obtained a larger statistical base to assist in establishing reserves for these excess casualty insurance claims.

High layer excess casualty insurance claims typically involve claims relating to (i) a shock loss such as an explosion or transportation accident causing severe damage to persons and/or property over a short period of time, (ii) a non-shock loss where a large number of claimants are exposed to injurious conditions over a longer period of time, such as exposure to chemicals or pharmaceuticals or (iii) a professional liability loss such as a medical malpractice claim. In each case, these claims are ultimately settled following extensive negotiations and legal proceedings. This process typically takes 5 to 15 years following the date of loss.

Reinsurance operations by their nature add further complications to the reserving process, particularly for casualty business written, in that there is an inherent lag in the timing and reporting of a loss event from an insured or ceding company to the reinsurer. This reporting lag creates an even longer period of time between the policy inception and when a claim is finally settled. As a result, more judgment is required to establish reserves for ultimate claims in the Company s reinsurance operations.

In the Company s reinsurance operations, case reserves for reported claims are generally established based on reports received from ceding companies. Additional case reserves may be established by the Company to reflect the Company s estimated ultimate cost of a loss.

Casualty reinsurance business involves reserving methods that generally include historical aggregated claim information as reported by ceding companies, combined with the results of claims and underwriting reviews of a sample of the ceding company s claims and underwriting files. Therefore, the Company does not always receive detailed claim information for this line of business.

Discontinued asbestos and long-tail environmental business were contained within certain policies previously written by NAC Re Corp. (now known as XL Reinsurance America Inc.), prior to its acquisition by the Company. At December 31, 2011, total gross unpaid losses and loss expenses in respect of this business represented less than 1% of unpaid losses and loss expenses.

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Except for certain workers compensation (including long-term disability) and certain U.K. motor liabilities, the Company does not discount its unpaid losses and loss expenses. The Company utilizes tabular reserving for workers compensation unpaid losses that are considered fixed and determinable. For further discussion see the Consolidated Financial Statements.

Loss and loss expenses are charged to income as they are incurred. These charges include loss and loss expense payments and any changes in case and IBNR reserves. During the loss settlement period, additional facts regarding claims are reported. As these additional facts are reported, it may be necessary to increase or decrease the unpaid losses and loss expense reserves. The actual final liability may be significantly different than prior estimates.

The amount of the Company s net unpaid losses and loss expenses relating to the Company s operating segments at December 31, 2011 and 2010 was as follows:

(U.S. dollars in millions)	2011	2010
Insurance	$ 11,374	$ 11,240
Reinsurance	5,610	5,642
Net unpaid loss and loss expense reserves	$ 16,984	$ 16,882

	Net Unpaid Losses and Loss Expenses as at December 31, 2011			Net Unpaid Losses and Loss Expenses as at December 31, 2010		
(U.S. dollars in thousands)	Case Reserves	IBNR Reserves	Total Reserves	Case Reserves	IBNR Reserves	Total Reserves
Insurance						
Casualty professional lines	$ 1,244	$ 3,175	$ 4,419	$ 1,280	$ 3,093	$ 4,373
Casualty other lines	1,180	2,628	3,808	1,392	2,454	3,846
Property	475	308	783	414	96	510
Marine, energy, aviation, and satellite	534	439	973	514	447	961
Other specialty lines (1)	413	675	1,088	375	630	1,005
Other (2)	196	66	262	341	144	485
Structured indemnity		41	41		60	60
Total	**$ 4,042**	**$ 7,332**	**$ 11,374**	**$ 4,316**	**$ 6,924**	**$ 11,240**
Reinsurance						
Casualty (3)	$ 1,501	$ 1,999	$ 3,500	$ 1,606	$ 2,122	$ 3,728
Property catastrophe (4)	180	197	377	146	192	338
Other property	410	467	877	322	397	719
Marine, energy, aviation, and satellite	399	71	470	367	30	397
Other (2)	163	174	337	201	202	403
Structured indemnity		49	49		57	57
Total	2,653	2,957	5,610	**$ 2,642**	3,000	5,642
TOTAL	**$ 6,695**	**$ 10,289**	**$ 16,984**	**$ 6,958**	**$ 9,924**	**$ 16,882**

(1) Other specialty lines within the Insurance segment includes: environmental, programs, equine, warranty, specie, middle markets and excess and surplus lines.
(2) Other includes credit and surety, whole account contracts and other lines.
(3) Within the Reinsurance segment, casualty-other and casualty-professional lines of business are shown in the aggregate.
(4) Property catastrophe IBNR includes event specific reserves for losses that the Company s insureds and cedants have informed the Company they expect to incur but have not yet had reported known claims.

As noted above, management reviews the IBNR estimates produced by the Company s actuaries who determine the best estimate of the liabilities to record in the Company s financial statements. The Company considers this single point estimate to be the mean expected outcome. Management believes that the actuarial methods utilized adequately provide for loss development.

Management does not build in a provision for uncertainty outside of the estimates prepared by the Company s actuaries.

While the proportion of unpaid losses and loss expenses represented by IBNR is sensitive to a number of factors, the most significant ones have historically been accelerated business growth and changes in business mix. Other factors that have affected the ratio in the past include additions to prior period reserves, catastrophic occurrences, settlement of large claims and changes in claims settlement patterns.

The ratio of IBNR to total reserves has increased in recent years, with the increase attributable to professional lines of business where we continue to hold IBNR for subprime and related credit crisis claims and other potential clash exposures in recent years while these claims develop at a relatively slow pace. Additionally, the ratio of IBNR to total reserves has increased this year for the property lines due to late 2011 catastrophe activity. Typically, the ratio of IBNR to total reserves is greater for casualty (including professional) lines (which are longer-tail in nature) than for property lines due to the policy forms utilized and timing of loss reporting and settlement.

IBNR reserves are calculated by the Company s actuaries using standard actuarial methodologies as discussed above. Since the year ended December 31, 2003, the Company adopted a methodology that provides a single point reserve estimate separately for each line of business and also a range of possible outcomes across each single point reserve estimate. This is discussed further below.

The following table shows the recorded estimate and the high and low ends of the range of the Company s net unpaid losses and loss expenses for each of the lines of business noted above at December 31, 2011:

(U.S. dollars in millions)	Net Unpaid Losses and Loss Expenses Recorded as at December 31, 2011	Range of Net Unpaid Losses & Loss Expenses Estimated as at December 31, 2011 High	Range of Net Unpaid Losses & Loss Expenses Estimated as at December 31, 2011 Low
Insurance			
Casualty professional lines	$ 4,419	$ 4,977	$ 3,893
Casualty other lines	3,808	4,288	3,353
Property	783	856	711
Marine, energy, aviation, and satellite	973	1,079	872
Other specialty lines (1)	1,088	1,205	977
Other (2)	262	296	231
Total (3)	$ 11,333	$ 12,372	$ 10,337
Reinsurance			
Casualty (4)	$ 3,500	$ 3,866	$ 3,152
Property catastrophe	377	467	295
Other property	877	1,027	738
Marine, energy, aviation, and satellite	470	549	394
Other (2)	337	389	288
Total (3)	$ 5,561	$ 6,068	$ 5,073
Structured Indemnity (3)	$ 90		
Total	$ 16,984		

(1) Other specialty lines within the Insurance segment includes: environmental, programs, equine, warranty, and excess and surplus lines.
(2) Other includes credit and surety, whole account contracts and other lines.
(3) The range for the total Insurance and Reinsurance segment reserves is narrower than the sum of the ranges for the lines of business shown in the table due to diversification benefits across the lines of business. In addition, the total for each of the Insurance and Reinsurance segments does not include reserves relating to structured indemnity business as the Company does not develop reserve ranges for this line of business.
(4) Within the Reinsurance segment, casualty-other and casualty-professional lines of business are shown in the aggregate.

There are factors that would cause reserves to increase or decrease within the context of the range provided. The magnitude of any change in ultimate losses would be determined by the magnitude of any changes to the Company s assumptions or combined impact of changes in assumptions. Factors that would increase reserves include, but are not limited to, increases in claim severity, increases in expected level of reported claims, changes to the regulatory environment which expand the exposure insured by the Company, changes in the litigation environment that increase claim awards, filings or verdicts, unexpected increases in loss inflation, and/or new types of claims being pursued against the Company. Factors that would decrease reserves include, but are not limited to, decreases in claim severity, reductions in the expected level of reported claims, changes to the regulatory environment which contract the exposure insured by the Company, changes in the litigation environment that decrease claim awards, filings or verdicts, and/or unexpected decreases in loss inflation.

The Company s methodology in 2011 for calculating reserve ranges around its single point reserve estimate is consistent with that used in 2010. The Company modeled a statistical distribution of potential reserve outcomes over a one year run-off period for each of the approximately 35 lines of business. In doing so the Company evaluated a number of alternative models, and for each line of business the Company s actuaries selected the distribution parameters deemed to be most appropriate. Factors affecting this decision included an assessment of the model fit, availability and relevance of data and the impact of changes in business mix. The Company used the modeled statistical distribution to calculate an 80% confidence interval for the potential reserve outcomes over this one year run-off period. The high and low end points of the ranges set forth in the above table are such that there is a 10% modeled probability that the reserve will develop higher than the high point and a 10% modeled probability that the reserve will develop lower than the low point.

The development of a reserve range models the uncertainty of the claim environment as well as the limited predictive power of past loss data. These uncertainties and limitations are not specific to the Company. The ranges represent an estimate of the range of possible outcomes over a one year development period. A range of possible outcomes should not be confused with a range of best estimates. The range of best estimates will generally be much narrower than the range of possible outcomes as it will reflect reasonable actuarial best estimates of the expected reserve.

Reserve volatility was analyzed for each line of business (excluding structured indemnity) within both the Reinsurance and Insurance segments using the Company s historical data, supplemented by industry data. These ranges were then aggregated to the lines of business shown above taking into account correlation between lines of business. The practical result of the correlation approach to aggregation is that the ranges by line of business disclosed above are narrower than the sum of the ranges of the individual lines of business. Similarly, the range for the Company s total reserves in the aggregate, is narrower than the sum of the ranges for the lines of business disclosed above.

On an annual basis, the Company reviews the correlation assumptions between its various lines of business. Since 2006, the Company has utilized a simplified approach of assigning ratings of low, medium or high to its correlation assumptions for each line of business pairing based on the judgment of the reserving actuaries. This simplified approach has been utilized due to the limited amount of historical experience within the Company s portfolio as well as limited applicable industry data. However, the Company s actual historical experience and industry data were used to judgmentally select a range of values for the low, medium and high correlations, respectively, of 15%, 30% and 50%. It should be noted that both the Company s own experience and the industry data exhibit negative correlations in reserve developments between certain lines of business. However, as a measure of prudence in evaluating the reserve ranges, the Company has used a minimum of 15% correlation between any two lines of business. The analysis of correlations and the reflection of potential diversification benefits across lines of business represent another area of uncertainty in the development of estimated reserve ranges.

The Company is not aware of any generally accepted model to perform the reserve range analysis described above. However, other models may be employed to develop these ranges.

See Segments, below for further discussion on prior year development of loss reserves.

Unpaid losses and loss expenses recoverable

The recognition of unpaid losses and loss expenses recoverable requires two key judgments. The first judgment involves the Company s estimation of the amount of gross IBNR to be ceded to reinsurers. Ceded IBNR is generally developed as part of the Company s loss reserving process and, consequently, its estimation is subject to similar risks and uncertainties as the estimation of gross IBNR (see Critical Accounting Policies and Estimates Unpaid losses and loss expenses and unpaid loss and loss expense recoverable). The second judgment involves the Company s estimate of the amount of the reinsurance recoverable balance that the Company will ultimately be unable to recover from related reinsurers due to insolvency, contractual dispute, or for other reasons. Amounts estimated to be uncollectible are reflected in a bad debt provision that reduces the reinsurance recoverable balance. Changes in the bad debt provision are reflected in net income. See Item 8, Note 9 to the Consolidated Financial Statements, Reinsurance, for further information.

The Company uses a default analysis to estimate uncollectible reinsurance. The primary components of the default analysis are reinsurance recoverable balances by reinsurer, net of collateral, estimated recovery rates and default factors used to determine the portion of a reinsurer s balance deemed uncollectible. The definition of collateral for this purpose requires some judgment and is generally limited to assets held in trust, letters of credit, and liabilities held by the Company with the same legal entity for which the Company believes there is a right of offset. Default factors require considerable judgment and are determined using the current rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions.

2) Future Policy Benefit Reserves

Future policy benefit reserves relate to the Company s Life operations and are estimated using assumptions for investment yields, mortality, expenses and provisions for adverse loss deviation. Uncertainties related to interest rate volatility and mortality experience make it difficult to project and value the ultimate benefit payments.

Most of the Company s future policy benefit reserves relate to annuity portfolio reinsurance contracts under which the Company makes annuity payments throughout the term of the contract for a specified portfolio of policies.

For certain of these contracts, a single premium is paid at inception of the contract by way of a transfer of cash and investments to the Company.

The reserving methodology for these annuity portfolio reinsurance contracts is described in the authoritative guidance issued by the FASB for accounting and reporting by insurance for certain long-duration contracts as well as authoritative guidance over realized gains and losses from the sale of investments. These contracts subject the Company to risks arising from policyholder mortality over a period that extends beyond the periods in which premiums are collected. Liabilities for future policy benefit reserves are established in accordance with the provisions of this guidance.

Claims and expenses for individual policies within these annuity reinsurance contracts are projected over the lifetime of the contract to calculate a net present value of future cash flows. Assumptions for each element of the basis (mortality, expenses and interest) are determined at the issue of the contract and these assumptions are locked-in throughout the term of the contract unless a premium deficiency exists. The assumptions are best estimate assumptions plus provisions for adverse deviations on the key risk elements (i.e., mortality and interest). Provisions for adverse deviation are designed to cover reasonable deviations from the best estimate outcome of the contract. As the experience on the contracts emerges, the assumptions are reviewed. This occurs at least annually and includes both an analysis of experience and review of likely future experience. If such review would produce reserves in excess of those currently held then lock-in assumptions will be revised and a loss recognized. During the years ended December 31, 2011, 2010 and 2009, there were no adjustments to the locked-in assumptions for these annuity reinsurance contracts.

The future policy benefit reserves for these annuity portfolio reinsurance contracts amounted to $4.0 billion and $4.3 billion at December 31, 2011 and 2010 respectively. The Company holds the investment assets backing these liabilities. These investments are primarily fixed income securities with maturities that closely match the expected claims settlement profile. A 0.1% decrease in the investment yield assumption would result in approximately a $31 million increase in the value of future claims related to annuity portfolio reinsurance.

As stated above, the future policy benefit reserves include provisions for adverse deviation in excess of best estimate assumptions consistent with the underlying pricing that amounted to approximately $36 million and $193 million at December 31, 2011 and 2010, respectively. The reduction in 2011 has arisen as the Company has taken a more conservative view of future mortality improvements in its best estimate assumptions. The future policy benefit reserves would only be increased if these provisions for adverse deviation became insufficient in the light of emerging claims experience. The present value of future claims would increase by approximately $19 million if mortality rates were to decrease by 1% in all future years, relative to the reserving assumptions.

The Company also provides reinsurance of disability income protection, for an in-force block of business. The future policy benefit reserves for these contracts amounted to approximately $99 million and $96 million at December 31, 2011 and 2010, respectively. Future policy benefit reserves include the lock-in of assumptions at inception with periodic review against experience. The liabilities relate to in-force blocks of business, comprising underlying insurance policies that provide an income if the policyholder becomes sick or disabled. The liabilities are therefore driven mainly by the rates at which policyholders become sick (where sickness is defined by the policy conditions) and by the rates at which these policyholders recover or die. A 1% increase in the incidence rate would increase the value of future claims by approximately $2.3 million, while a 1% decrease in the termination rate would increase the value of future claims by approximately $4.1 million. While no changes to the locked-in assumptions were made in 2011 or in 2009, a review of lapse experience in 2010 led to an increase in the reserve of $2.2 million.

The Company also provides reinsurance of term assurance and critical illness policies written in the U.K., Ireland and the U.S. The future policy benefit reserves for these contracts amounted to approximately $241 million and $220 million at December 31, 2011 and 2010, respectively. This increase was caused by ageing of the portfolio, which was marginally offset by movements of the U.K. Pound sterling and Euro against the U.S. dollar over 2011. Future policy benefit reserves include the lock-in of assumptions at inception with periodic review against experience. The provisions for adverse deviation in these reserves amounted to approximately $22 million and $20 million at December 31, 2011 and 2010, respectively.

The liabilities relate to in-force blocks of business and to treaties accepting new business up until the end of 2009, comprising underlying insurance policies that provide mainly lump sum benefits if the policyholder dies or becomes sick. For term assurance, the liabilities are therefore driven by the rates of mortality and for critical illness cover, the liabilities are driven predominantly by the rates at which policyholders become sick, where sickness is defined by the treaty conditions (i.e., the morbidity rates). A 1% increase in the mortality rate relative to the reserving assumption would increase the value of future claims by approximately $2.4 million, and a 1% increase in the morbidity rate would increase the value of future claims by approximately $0.9 million.

The term assurance and critical illness treaties have been written using a variety of structures, some of which incur acquisition costs during an initial period. For such treaties, a deferred acquisition cost (DAC) asset has been established and an increase in future lapse rates could impact the recoverability of such costs from future premiums. The recoverability will also be influenced by the impact of lapses on future claims. An increase in the annual lapse rates by 1% could lead to a 5%-10% reduction in future margins available for amortizing the DAC asset.

The Company also provided reinsurance of a block of U.S. based term assurance, which was novated to the Company from an insurance affiliate in December 2002. The future policy benefit reserves for these contracts amounted to approximately $258 million and $261 million at December 31, 2011 and 2010, respectively. Future policy benefit reserves are established in accordance

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with the provisions of general authoritative guidance on accounting for insurance enterprises, including the lock-in of assumptions at inception with periodic review against experience.

The liabilities relate to in-force blocks of business, which are comprised of underlying insurance policies that provide mainly lump sum benefits if the policyholder dies. The liabilities are therefore driven by the rates of mortality, and a 1% increase in the mortality rate relative to the reserving assumption would increase the value of future claims by approximately $7 million. The liabilities are also affected by lapse experience, and a 1% decrease in lapse rates relative to the reserving assumption would increase the reserve by approximately $0.8 million. No changes to the locked-in assumptions were made in 2011, 2010 or 2009.

For further information see Item 8, Note 12 to the Consolidated Financial Statements, Future Policy Benefit Reserves.

3) Other-Than-Temporary Declines in Investments (OTTI)

The Company s process for identifying declines in the fair value of investments that are other-than-temporary involves consideration of several factors. These primary factors include (i) an analysis of the liquidity, business prospects and financial condition of the issuer including consideration of credit ratings, (ii) the significance of the decline, (iii) an analysis of the collateral structure and other credit support, as applicable, of the securities in question, and (iv) for debt securities, whether the Company intends to sell such securities. In addition, the authoritative guidance requires that OTTI for certain asset backed and mortgage backed securities are recognized if the fair value of the security is less than its discounted cash flow value and there has been a decrease in the present value of the expected cash flows since the last reporting period. Where the Company s analysis of the above factors results in the Company s conclusion that declines in fair values are other-than-temporary, the cost of the security is written down to discounted cash flow and a portion of the previously unrealized loss is therefore realized in the period such determination is made.

If the Company intends to sell an impaired debt security, or it is more likely than not that it will be required to sell the security before recovery of its amortized cost basis, the impairment is other-than-temporary and is recognized in earnings in an amount equal to the entire difference between fair value and amortized cost.

There are risks and uncertainties associated with determining whether declines in the fair value of investments are other-than-temporary. These include subsequent significant changes in general economic conditions as well as specific business conditions affecting particular issuers, the Company s liability profile, subjective assessment of issue-specific factors (seniority of claims, collateral value, etc.), future financial market effects, stability of foreign governments and economies, future rating agency actions and significant disclosure of accounting, fraud or corporate governance issues that may adversely affect certain investments. In addition, significant assumptions and management judgment are involved in determining if the decline is other-than-temporary. If management determines that a decline in fair value is temporary, then a security s value is not written down at that time. However, there are potential effects upon the Company s future earnings and financial position should management later conclude that some of the current declines in the fair value of the investments are other-than-temporary declines. See Investment Activities herein for further information on other-than-temporary declines in the value of investments and unrealized loss on investments.

Key Assumptions used in determination of credit losses related to fixed maturities

The Company reviews, on a quarterly basis, the entirety of the securities in its investment portfolio that are in a gross unrealized loss position to assess whether it believes a credit loss, relative to the current amortized cost of the security, exists. The Company utilizes specific screening criteria to identify securities at risk for a credit loss, and if any of these conditions exists, subject the individual security to a detailed review to determine if a credit loss exists. The screening criteria used by the Company include the absolute degree of impairment of the security as a percentage of amortized cost, the credit rating of the security and the market yield-to-maturity of the security. Any securities that have previously been identified as impaired due to credit losses are at elevated risk of further impairments. In addition, on a quarterly basis, the Company reviews any current market developments and identifies any new issues that may adversely impact the Company s investment portfolio, and reviews any impacted holdings.

Credit loss methodology structured credit

Credit loss on structured credit securities is determined through a comparison of the security s discounted cash flow to the amortized cost of the security. To the extent that the discounted cash flow is estimated to be lower than the amortized cost of the security, the security is impaired to the discounted cash flow value of all security cash flows, including both coupon and principal repayment, discounted using the forward curve.

The Company, in conjunction with its third-party investment management service providers, makes significant assumptions in its impairment analysis and these assumptions are subject to changes in both economic fundamentals and management s estimates in future periods.

(1) Non-Agency RMBS

The Company utilizes assumptions specific to its individual holdings and, accordingly, individual assumptions will differ on a security by security basis depending on the quality of the collateral and the performance of the underlying pools. In general, the

Company projects that future defaults will develop based on the performance of the underlying collateral, measured by the number of loans currently in arrears.

Loans < 30 days in arrears	50% will ultimately default
Loans 30-60 days in arrears	60% will ultimately default
Loans 60-90 days in arrears	75% will ultimately default
Bank held	100% default rate
Loans in foreclosure	100% default rate

The Company estimates that the cumulative losses on the mortgage structures it owns will vary depending on the vintage and collateral of the underlying loans in the holdings. Cumulative deal loss expectations are projected based on the number of loans expected to take a loss and the severity of loss upon default. Loan loss severities depend on the borrower, geographic location and loan to value characteristics of the underlying collateral. The Company estimates that loss severities will range from 35-75% for sub-prime and Alt-A loans and 20-40% for Prime loans. These cumulative losses results are then compared to the level of subordination within the Company s holdings to measure if impairment exists.

	Average Cumulative Losses by Vintage			
	2007	**2006**	**2005**	**2004**
Alt-A non option ARM	33%	27%	16%	7%
Alt-A Option ARM	43%	36%	20%	11%
Prime	12%	12%	6%	3%
Subprime	50%	44%	26%	14%

(2) Core CDOs

The Company utilizes a scenario based approach to reviewing the majority of its CDO portfolio, which consists primarily of collateralized loan obligations. The five significant scenarios utilized in the model consist of:

2 base cases assuming asset defaults are equivalent to either the expected corporate default probabilities, or the cumulative default rates for similar time frames from the period of 1983 to 2010.

Optimistic/pessimistic cases assuming assets have a default rate equivalent to 1 rating notch higher/ lower than their current rating and if on positive/negative watch then 2 notches higher/lower than their current rating.

A market implied scenario based on the current asset market price, assuming that lower priced loans have a higher default rate.

The weighted scenario of the five scenarios above is used for the determination of a potential impairment. If losses are forecast to be below the subordination level for the tranche held by the Company, the security is determined not to be impaired. The weighting between these scenarios varies over time depending on market conditions, but the weighting used for the year end 2011 evaluation consisted of 45% to the base cases noted above, 5% to the optimistic case, 10% to the pessimistic case, and 40% to the market implied case. For the non-CLO portion of the core CDO portfolio, the Company utilizes specific default scenarios related to the particular underlying assets.

(3) Other structured credit assets classes

The remainder of the gross unrealized losses related to the Company s structured credit portfolio are concentrated in the following significant asset classes:

Other ABS, which is a mix of mostly investment grade credit card, auto and non-U.S. ABS structures that have risk and performance characteristics unrelated to the U.S. housing market. In cases where these sectors have met Company screens, the individual securities are evaluated based on fundamental credit analysis of the underlying structure.

CMBS, which are dominated by AAA rated holdings which generally have high levels of credit subordination, are highly diversified and priced reasonably close to par. The gross unrealized losses on CMBS are spread evenly across the credit rating buckets. The Company reviews these holdings on an individual security basis to the extent they meet the screens noted above, but generally does not believe these securities to have a high risk of credit loss given their high subordination levels.

Credit loss analysis corporate sector securities

Credit losses on corporate securities are determined on an individual security basis. The Company reviews the circumstances and conditions associated with its credit issuers, including considering credit rating and forecast operating and financing activities of the issuer, and will make a determination as to whether it believes the issuer is likely to fully meet its contractual principal and interest obligations. To the extent the Company does not believe the issuers will meet these obligations, it recognizes a credit loss as the difference between amortized cost and the estimated present value of cash flows expected to be received. The Company reviews the ability to pay at the lowest tier (i.e., most subordinated) of the capital structure at which it holds securities, and, to the extent it is satisfied in the performance of the lower tier, concludes that any more senior tiers are also likely to meet obligations.

The Company evaluates the credit losses associated with its medium term notes, which generally represent notes backed primarily by investment grade European credit. The Company evaluates the cash flows expected from the notes over their remaining expected life, including an evaluation of the likelihood of current holdings to meet their principal and interest obligations, and incorporates current reinvestment assumptions on any security maturities or reinvestment of cash flows. These cash flows are discounted at the current yield, adjusted for changes in interest rates for floating rate securities expected from these securities, and, to the extent the discounted cash flow value is below the amortized cost, recognizes an impairment charge.

4) Income Taxes

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company had net operating tax loss carry forward balances of $263.6 million and $282.2 million against which a valuation allowance of $239.1 million and $240.0 million at December 31, 2011 and 2010, respectively, was established. The Company had realized capital loss carry forward balances of approximately $237.2 million and $261.0 million against which a valuation allowance of approximately $237.2 million and $261.0 million at December 31, 2011 and 2010, respectively, was established. Included within these realized capital losses are $117.9 million and $142.3 million of losses arising from the intercompany sale of investments, against which a valuation allowance of $117.9 million and $142.3 million has been established. The deferral of benefits from tax losses is evaluated based upon management s estimates of the future profitability of the Company s taxable entities based on current forecasts, the character of income and the period for which losses may be carried forward. A valuation allowance may have to be established for any portion of a deferred tax asset that management believes will not be realized. Should the future income of these entities fall below expectations, a further valuation allowance would have to be established, which could be significant. In addition, if any further losses are generated by these entities, these losses may not be tax affected.

For further information see Other Revenues and Expenses and Item 8, Note 22 to the Consolidated Financial Statements, Taxation.

5) Goodwill and Other Intangible Assets

The Company has recorded goodwill in connection with various acquisitions in prior years. Goodwill represents the excess of the purchase price over the fair value of net assets acquired. In accordance with FASB issued final authoritative guidance on goodwill and other intangible assets, the Company tests goodwill for potential impairment annually as of June 30 and between annual tests if an event occurs or circumstances change that may indicate that potential exists for the fair value of a reporting unit to be reduced to a level below its carrying amount. The Company tests for impairment at the reporting unit level in accordance with the authoritative guidance on intangibles and goodwill. For the reinsurance segment, a reporting unit is one level below the business segment, while for insurance, the segment is also the reporting unit. The first step is to identify potential impairment by comparing the estimated fair value of a reporting unit to the estimated book value, including goodwill. The fair value of each reporting unit is derived based upon valuation techniques and assumptions the Company believes market participants would use to value the business and this is then compared to the book value of the business. The Company derives the net book value of its reporting units by estimating the amount of shareholders equity required to support the activities of each reporting unit. The estimated fair values of the reporting units are generally determined utilizing methodologies that incorporate price-to-net-tangible-book and price-to-earnings multiples of certain comparable companies, from an operational and economic standpoint. If such estimated fair value, combined with an estimate of an appropriate control premium, indicates a close call or potential impairment, further analysis using discounted cash flows is performed and the results of the various valuation methodologies are weighted to arrive at the estimated fair value for each reporting unit. A control premium represents the value an investor would pay above minority interest transaction prices in order to obtain a controlling interest in the respective company. If the estimated fair value exceeds the book value, goodwill at the reporting unit level is not deemed to be impaired. If the book value exceeds the estimated fair value, the second step of the process is performed to measure the amount of impairment.

The Company completed an interim impairment test during the fourth quarter of 2011 which resulted in a non-cash goodwill impairment charge of $429.0 million. The charge relates to the insurance segment. The impairment was determined using the methodologies as described above, which included discounted cash flow analyses and comparison with similar companies using their publicly traded price multiples as the basis for valuation. Continued low valuations in the insurance industry as a whole combined with several years of poor underwriting performance in the segment have impacted the technical valuations; however, management continues to see significant value in the Company s global insurance platform.

For further detailed information, see Item 8, Note 8 to the Consolidated Financial Statements, Goodwill and Other Intangible Assets.

6) Reinsurance Premium Estimates

The Company writes business on both an excess of loss and proportional basis. In the case of excess of loss contracts, the subject written premium is generally outlined within the treaty and the Company receives a minimum and/or deposit premium on a quarterly basis which is normally followed by an adjustment premium based on the ultimate subject premium for the contract. The Company estimates the premium written on the basis of the expected subject premium and regularly reviews this against actual quarterly statements to revise the estimate based on the information provided by the cedant. An estimate of premium is recorded at the inception of the contract.

On proportional contracts, written premiums are estimated based on expected ultimate premiums using information provided by the ceding companies. The ceding company s premium estimate may be adjusted based on its history of providing accurate premium estimates. When the actual premium is reported by the ceding company, normally on a quarterly basis, it may be materially higher or lower than the estimate. Adjustments arising from the reporting of actual premium by the ceding companies are recorded at the earliest point in time that the supporting information indicates an adjustment is appropriate.

Written premiums on excess of loss contracts are earned in accordance with the loss occurring period defined within the treaty, normally 12 months following inception of the contract. Written premiums on proportional contracts are earned over the risk periods of the underlying policies issued and renewed, normally 24 months. For both excess of loss and proportional contracts, the earned premium is recognized ratably over the earning period, namely 12-24 months. The portion of the premium related to the unexpired portion of the policy at the end of any reporting period is reflected in unearned premiums.

Reinstatement premiums are recognized at the time a loss event occurs where coverage limits for the remaining life of the contract are reinstated under pre-defined contract terms and are fully earned when recognized. Recognition of reinstatement premiums is based on the Company s estimate of loss and loss adjustment expense reserves, which involves management judgment.

Reinsurance business by its nature can add further complications since, generally, the ultimate premium due under a specific contract will not be known at the time the contract is entered into. As a result, more judgment and ongoing monitoring is required to establish premiums written and earned in the Company s reinsurance operations.

At December 31, 2011 and 2010, the amount of premiums receivable related to the Company s reinsurance operations amounted to $1.1 billion and $1.2 billion, respectively.

A significant portion of amounts included as premiums receivable, which represent estimated premiums written, net of commissions, are not currently due based on the terms of the underlying contracts. Management reviews the premiums receivable balance at least quarterly and provides a provision for amounts deemed to be uncollectible. The Company recorded a provision for uncollectible premiums receivable related to its reinsurance operations at December 31, 2011 and 2010 of $1.9 million and $4.4 million, respectively.

The amount of proportional and excess of loss reinsurance gross premiums written and gross acquisition expenses recognized by the Company s reinsurance operations for each line of business for the years ended December 31, 2011, 2010 and 2009 was as follows:

	2011		2010		2009	
(U.S. dollars in thousands)	Gross Premiums Written	Gross Acquisition Expenses	Gross Premiums Written	Gross Acquisition Expenses	Gross Premiums Written	Gross Acquisition Expenses
Proportional Contracts:						
Casualty other lines	$ 115,835	$ 30,657	$ 38,671	$ 9,945	$ 44,924	$ 12,075
Casualty professional lines	65,492	19,422	51,922	14,604	41,195	12,652
Other property	693,825	145,367	651,733	168,981	703,219	164,094
Marine, energy, aviation and satellite	50,438	12,556	49,105	14,106	34,636	8,116
Other (1)	90,845	25,796	86,303	22,745	144,116	40,628
Total Proportional contracts	$ 1,016,436	$ 233,798	$ 877,734	$ 230,381	$ 968,090	$ 237,565

	2011		2010		2009	
(U.S. dollars in thousands)	Gross Premiums Written	Gross Acquisition Expenses	Gross Premiums Written	Gross Acquisition Expenses	Gross Premiums Written	Gross Acquisition Expenses
Excess of Loss Contracts:						
Property catastrophe	$ 461,742	$ 43,705	$ 370,266	$ 37,720	$ 357,267	$ 33,074
Casualty other lines	176,673	26,602	190,864	30,764	173,853	34,383
Casualty professional lines	151,897	28,055	166,379	30,969	129,733	26,241
Other property	153,991	17,659	150,762	16,363	159,091	12,892
Marine, energy, aviation and satellite	105,724	9,267	68,333	6,066	54,463	5,429
Other (1)	11,338	3,399	17,655	6,361	11,978	2,642
Structured Indemnity	(4,182)	1,257	957	2,380	4,948	2,566
Total Excess of loss contracts	$ 1,057,183	$ 129,944	$ 965,216	$ 130,623	$ 891,333	$ 117,227

(1) Other includes credit and surety, whole account contracts and other lines.

Segments

Following a streamlining of the Company s operating segments in the first quarter of 2009, the Company is organized into three operating segments: Insurance, Reinsurance and Life operations. The Company s general investment and financing operations are reflected in Corporate.

The Company evaluates the performance of both the Insurance and Reinsurance segments based on underwriting profit and the performance of the Life operations segment based on its contribution to net income. Other items of revenue and expenditure of the Company are not evaluated at the segment level for reporting purposes. In addition, the Company does not allocate investment assets by segment for its P&C operations. Investment assets related to the Company s Life operations and certain structured products included in the Insurance and Reinsurance segments and in Corporate are held in separately identified portfolios. As such, net investment income from these assets is included in the contribution from each of these segments. See Item 8, Note 4 to the Consolidated Financial Statements, Segment Information, for a reconciliation of segment data to the Company s consolidated financial statements.

Income Statement Analysis

Insurance

The following table summarizes the underwriting profit (loss) for the Insurance segment:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009
Gross premiums written	$ 4,824,665	9.2%	$ 4,418,380	3.9%	$ 4,251,888
Net premiums written	3,707,664	7.1%	3,461,150	5.7%	3,273,380
Net premiums earned	3,663,727	3.8%	3,529,138	(0.9)%	3,559,793
Net losses and loss expenses	(2,951,413)	17.8%	(2,505,502)	4.4%	(2,399,747)
Acquisition costs	(461,965)	10.5%	(418,146)	(2.6)%	(429,170)
Operating expenses	(683,814)	6.5%	(642,103)	(6.8)%	(689,131)
Underwriting profit (loss)	$ (433,465)	NM*	$ (36,613)	NM*	$ 41,745
Net results structured products	$ 10,976	(25.3)%	$ 14,696	(11.8)%	$ 16,660
Net fee income and other	(16,370)	5.2%	(15,564)	9.3%	(14,241)

* NM Not Meaningful

Gross premiums written increased by 9.2% during the year ended December 31, 2011 compared to the same period of 2010 and, when evaluated in local currency, increased by 6.8%. The IPC, NAPC and Specialty business groups all experienced increased gross premiums written which were partially offset by declines from the Professional business group. The growth in premium is driven by new business growth across (i) all lines in NAPC; (ii) property and middle market lines in IPC; and (iii) general aviation and specie lines in Specialty. In addition to the new business growth outlined above, favorable foreign exchange and the renewal of long term agreements as annual policies in IPC Primary Casualty, partially offset by a large multi-year program written in the fourth quarter of 2010 (discussed below), contributed to increased premiums for the segment. For the Professional business group, a reduction in gross premiums written was attributable to lower multi-year deals and lower new business in U.S. Professional partially offset by new business in professional lines in international markets.

Gross premiums written increased by 3.9% during the year ended December 31, 2010 compared to the same period of 2009 and, when evaluated in local currency, increased by 4.2%. A large proportion of the gross and net premiums written increase related to a multi-year agreement with gross written premium of $126.5 million written in primary casualty during the fourth quarter of 2010. Excluding this multi-year program, across most lines of business, premium levels were flat, having been maintained despite continued challenging market conditions and strong competition, which continue to negatively impact new business and pricing. In addition, there have been improved retention rates across most lines of business as a result of the Company s stronger financial condition and market position since the end of 2009. New business growth in upper middle market, marine and offshore energy, active programs, U.S. general aviation, and select professional businesses has been offset by decreases in North America environmental and excess and surplus lines, the run-off of a large U.S. automobile warranty program, the termination of a specialty lines aviation program in 2009 and decreases in U.S.-based professional lines due to continued market pressures and pricing.

Net premiums written increased by 7.1% during the year ended December 31, 2011 as compared to the same period of 2010. The increase resulted from the gross premiums written increases outlined above partially offset by an increase in ceded premiums written of 16.7%. The increase in ceded premiums written relates to increased utilization of facultative reinsurance, primarily in IPC property, the unfavorable impact of foreign exchange rates, higher reinsurance premiums on certain excess of loss treaties and reinstatement premiums related to catastrophe, property and marine losses.

Net premiums written increased by 5.7% during the year ended December 31, 2010 as compared to the same period of 2009. The increase resulted from a reduction in ceded written premiums partially offset by the increase in gross premiums written noted above. The decrease in ceded written premiums is largely related to Specialty due to cost savings from a restructuring of the marine and specie global, and property excess of loss reinsurance treaties, as well as certain adjustments to premium estimates in aviation and property which gave rise to a positive variance over 2009.

Net premiums earned increased by 3.8% during the year ended December 31, 2011 as compared to the same period of 2010. The increase primarily resulted from higher net written premiums earned through primary casualty, property, programs and middle markets and favorable foreign exchange impacts offset by the ceded catastrophe, property and marine reinstatement premiums noted above and the earn-out of lower net premiums written in U.S. Professional and certain discontinued and environmental lines. Net premiums earned decreased by 0.9% in 2010 as compared to 2009 which was primarily a reflection of the overall reduction of net premiums written over the previous 12 to 24 months.

The following table presents the ratios for the Insurance segment for the last three years ended December 31:

	2011	2010	2009
Loss and loss expense ratio	80.6%	71.0%	67.4%
Underwriting expense ratio	31.2%	30.0%	31.4%
Combined ratio	111.8%	101.0%	98.8%

The loss and loss expense ratio noted above includes net losses incurred for both the reported year and any favorable or adverse prior year development of loss and loss expense reserves held at the beginning of the year.

The following table summarizes the net (favorable) adverse prior year development by line of business relating to the Insurance segment for the last three years ended December 31:

(U.S. dollars in millions)	2011	2010	2009
Property	$ (8.9)	$ (23.5)	$ (50.7)
Casualty and Professional	(47.1)	(105.2)	(41.0)
Specialty and Other	(20.5)	2.1	28.8
Structured Indemnity		(0.8)	
Total	$ (76.5)	$ (127.4)	$ (62.9)
Loss and loss expense ratio excluding prior year development	82.6%	74.6%	69.2%

In addition, the following tables present the prior year (favorable) adverse development of the Company s gross and net loss and loss expense reserves within the Insurance segment for the last three years ended December 31:

Gross:

(U.S. dollars in millions)	2011	2010	2009
Unpaid losses and loss expense reserves at the beginning of the year	$ 14,325	$ 14,157	$ 14,373
Gross (favorable) adverse development of those reserves during the year	23	(31)	(45)
Unpaid losses and loss expense reserves re-estimated one year later	$ 14,348	$ 14,126	$ 14,328

Net:

(U.S. dollars in millions)	2011	2010	2009

Unpaid losses and loss expense reserves at the beginning of the year	$ 11,240	$ 11,129	$ 11,126
Net (favorable) adverse development of those reserves during the year	(77)	(127)	(63)
Unpaid losses and loss expense reserves re-estimated one year later	$ 11,163	$ 11,002	$ 11,063

Excluding prior year development, the loss ratio for the year ended December 31, 2011 increased by 8.0 loss percentage points as compared to the same period in 2010 due to higher levels of catastrophe losses occurring in the year ended December 31, 2011. Catastrophe losses net of reinsurance recoveries and including reinstatement premiums were $219.5 million higher for year ended December 31, 2011 compared to the same period of 2010. For further details on these catastrophe losses in 2011 see Significant Items affecting the Results of Operations 1) The impact of significant large natural catastrophe activity above. Excluding favorable prior year development and net catastrophe losses in both periods, the current accident year loss ratio increased by 2.2 points from 2010 to 2011 due to higher large loss activity in energy, property and marine businesses.

Excluding prior year development, the loss ratio for the year ended December 31, 2010 increased by 5.4 loss percentage points as compared to the same period in 2009 due primarily to higher levels of natural catastrophe losses occurring in 2010. Excluding favorable prior year development, natural catastrophe losses and reinstatement premiums in both periods, the loss ratio increased by 1.9 points year over year largely due to several individual large loss events in property and excess casualty, adverse experience in exited lines of business and the impact of flat to slightly negative rate changes partially offset by changes in business mix and improved loss experience in aerospace.

For further information on the net favorable prior year reserve development for the years ended December 31, 2011, 2010 and 2009, see Item 8, Note 10 to the Consolidated Financial Statements, Losses and Loss Expenses.

The increase in the underwriting expense ratio for the year ended December 31, 2011 as compared to the same period of 2010 was due to an increase in the acquisition expense ratio of 0.8 points (12.6% as compared to 11.8%) and an increase in the operating expense ratio of 0.4 points (18.6% as compared to 18.2%). The increase in the acquisition expense ratio was primarily from favorable adjustment to guaranty fund assessments in 2010, higher commissions and lower amounts of fee based business in excess casualty and aerospace, as well as the impact of the catastrophe, property and marine reinstatement premiums on the ratio. The increase in the operating expense ratio was mainly as a result of increased compensation costs from certain severance costs, higher number of employees, and unfavorable foreign exchange impacts.

The decrease in the underwriting expense ratio for the year ended December 31, 2010 compared to the same period in 2009 was due to a decrease in the operating expense ratio of 1.1 points (18.2% as compared to 19.3%), and a decrease in the acquisition expense ratio of 0.3 points (11.8% as compared to 12.1%). The decrease in the operating expense ratio was as a result of costs savings associated with the Company s expense reduction initiatives announced in the third quarter of 2008 and first quarter of 2009, including changes to the Company s previously communicated operational transformation program. The decrease in the acquisition expense ratio is attributable to changes in business mix partially offset by the impact of higher commission rates in certain professional, casualty and middle market lines.

Net results from structured insurance products include certain structured indemnity contracts that are accounted for as deposit contracts. Net results from these contracts decreased 25.3% during the year ended December 31, 2011 as compared to the same period of 2010. The decrease reflects the overall run-off nature of this line of business combined with a change in the interest rate hedging strategy on one of the larger transactions during 2010. Net results from these contracts for the year ended December 31, 2010 decreased compared to the same period in 2009, again reflecting the overall run-off nature of this line of business.

Net fee income and other improved during the year ended December 31, 2011 as compared to the same period of 2010 mainly as a result of higher fee income in Specialty partially offset by higher expenses related to the Company s loss prevention consulting services. Net fee income and other decreased in the year ended December 31, 2010 compared to the same period in 2009 mainly as a result of lower engineering fee income associated with the Company s loss prevention consulting services business coupled with other expenses in professional lines related to the cost of an endorsement facility with National Indemnity Company, under which National Indemnity Company issued endorsements to certain Side A directors and officers liability insurance policies underwritten by XL Specialty Insurance Company. For further information, see Item 8, Note 7 to the Consolidated Financial Statements, Other Investments. During the first quarter of 2010, management concluded that it did not require the $100 million extension to this endorsement facility and did not purchase the related payment obligation.

Reinsurance

The following table summarizes the underwriting profit (loss) for this segment:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009
Gross premiums written	$ 2,073,619	12.5%	$ 1,842,951	(0.9)%	$ 1,859,423
Net premiums written	1,725,724	12.2%	1,538,438	4.6%	1,470,332
Net premiums earned	1,663,385	10.7%	1,501,999	(5.7)%	1,591,946
Net losses and loss expenses	(1,126,978)	59.6%	(706,298)	(8.2)%	(769,090)
Acquisition costs	(324,128)	1.0%	(321,008)	(7.4)%	(346,699)
Operating expenses	(176,167)	0.3%	(175,586)	(7.9)%	(190,596)
Underwriting profit	$ 36,112	(87.9)%	$ 299,107	4.7%	$ 285,561
Net results structured products	12,053	NM*	3,075	NM*	26,374
Fee income and other	3,903	56.9%	2,488	NM*	6,209

* NM Not meaningful

Gross premiums written increased by 12.5% during the year ended December 31, 2011 compared to the same period of 2010 and, when evaluated in local currency, increased by 8.9%. Premium growth was most significant in the International unit and was due to new motor and marine business, as well as positive amendments to prior year premium estimates. In addition, there were increased premiums in North America property on a U.S. agricultural program due to rising commodity prices in 2011, partially offset by decreases in North America casualty due to current market conditions and the non-renewal of certain treaties. The growth in property catastrophe gross premiums written was through price and capacity increases, from new business in the year and from natural catastrophe reinstatement premiums partially offset by the non-renewal of certain property treaties.

Gross premiums written decreased by 0.9% while net premiums written increased by 4.6% during the year ended December 31, 2010 compared with the same period of 2009. Gross premiums written decreased by 2.2% when evaluated in the local currency. The gross premium written decrease was mainly from the North America property business where there have been lower premiums on a U.S. agricultural program due to a fall in commodity prices. In addition, the exit of certain casualty facultative markets, non renewed business, cancelations and certain reductions in price and capacity also contributed to the marginal reduction in gross premiums written. Offsetting the reduction was premium growth from the recapture of business lost during 2009 following ratings actions as well as new business in Europe, Bermuda and Asia and loss related premium adjustments in Europe. The increase in net premiums written was mainly due to the reduction in ceded written premiums as a result of a reduction in volume associated with the U.S. agricultural program already mentioned above, of which a significant portion was retroceded.

Net premiums earned increased by 10.7% during the year ended December 31, 2011 as compared to the same period of 2010. The increase is a reflection of the overall growth in net premiums written in 2011. In addition, reinstatement premiums on catastrophe losses, increased during the year ended December 31, 2011 compared to the same period of 2010. Net premiums earned decreased by 5.7% in 2010 as compared to 2009 which is primarily a reflection of the overall reduction of net premiums written over the previous three years.

The following table presents the ratios for the Reinsurance segment for the last three years ended December 31:

	2011	2010	2009
Loss and loss expense ratio	67.8%	47.0%	48.3%
Underwriting expense ratio	30.0%	33.1%	33.8%
Combined ratio	97.8%	80.1%	82.1%

The loss and loss expense ratio includes net losses incurred in the reported year and any favorable or adverse prior year development of loss reserves held at the beginning of the year.

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The following table summarizes the net (favorable) adverse prior year development by line of business relating to the Reinsurance segment for the last three years ended December 31:

(U.S. dollars in millions)	2011	2010	2009
Property and other short-tail lines	$ (64.3)	$ (145.8)	$ (142.5)
Casualty and other	(144.1)	(99.7)	(80.3)
Structured Indemnity			1.0
Total	$ (208.4)	$ (245.5)	$ (221.8)
Loss and loss expense ratio excluding prior year development	80.3%	63.4%	62.2%

In addition, the following tables present the prior year (favorable) adverse development of the Company s gross and net loss and loss expense reserves within the Reinsurance segment for the last three years ended December 31:

Gross:

(U.S. dollars in millions)	2011	2010	2009
Unpaid losses and loss expense reserves at the beginning of the year	$ 6,206	$ 6,667	$ 7,278
Gross (favorable) adverse development of those reserves during the year	(297)	(284)	(257)
Unpaid losses and loss expense reserves re-estimated one year later	$ 5,909	$ 6,383	$ 7,021

Net:

(U.S. dollars in millions)	2011	2010	2009
Unpaid losses and loss expense reserves at the beginning of the year	$ 5,642	$ 6,138	$ 6,559
Net (favorable) adverse development of those reserves during the year	(208)	(245)	(222)
Unpaid losses and loss expense reserves re-estimated one year later	$ 5,434	$ 5,893	$ 6,337

Excluding prior year development, the loss ratio for the year ended December 31, 2011 increased by 16.9 loss percentage points as compared to the same period in 2010 due to higher levels of catastrophe losses occurring in the year ended December 31, 2011. Catastrophe losses net of reinsurance recoveries and including reinstatement premiums were $247.3 million higher for the year ended December 31, 2011 compared to the same period of 2010. For further details on these catastrophe losses in 2011 see Significant Items affecting the Results of Operations 1) The impact of significant large natural catastrophe activity above. Excluding favorable prior year development, net catastrophe losses and reinstatement premiums in both periods, the loss ratio increased by 2.3 points from 2010 to 2011 mainly due to higher levels of large loss events in U.S. property including a deterioration in the performance of a large U.S. agricultural program, higher attritional losses and business mix changes.

Excluding prior year development, the loss ratio for the year ended December 31, 2010 increased by 1.2 loss percentage points as compared with the same period of 2009 attributable primarily to the impact of natural catastrophe losses and large loss events in 2010 compared to 2009. Excluding favorable prior year development, natural catastrophe losses and associated reinstatement premiums in both years ending December 31, the loss ratio decreased by 6.7 percentage points from 2009 to 2010. This improvement relates to changes in business mix as well as a lower level of loss activity in 2010 relative to 2009 in several lines including property, discontinued financial lines, and the professional and trade credit business related to the credit crisis.

For further information on the net favorable prior year reserve development of $208.4 million and $245.5 million for the years ended December 31, 2011 and 2010 see Item 8, Note 10 to the Consolidated Financial Statements, Losses and Loss Expenses.

The decrease in the underwriting expense ratio during the year ended December 31, 2011 as compared to the same period of 2010 was due to a decrease in the operating expense ratio of 1.2 points (10.5% as