BUILDING OUR FUTURE

Financial Condition Report 2020
Lancashire Holdings Limited
Lancashire Insurance Company Limited

Contents

Executive summary

Lancashire Holdings Limited ("LHL") is the parent company of the Lancashire Group ("Lancashire" or "the Group") and Lancashire Insurance Company Limited ("the Company" or "LICL") is the Group's Bermuda domiciled insurance subsidiary. Both the Group and LICL are providers of global specialty insurance and reinsurance products.

This Group Financial Condition Report ("FCR") has been prepared in accordance with the Bermuda Insurance (Public Disclosure) Rules 2015 and the Insurance (Group Supervision) Rules 2011. It includes quantitative and qualitative information about the business performance, system of governance, risk profile, valuation for solvency purposes and capital management of both LHL and LICL.

LICL has been granted an exemption by the Bermuda Monetary Authority ("BMA") from the requirement to prepare and file a separate FCR on the condition that disclosures that are specific to LICL are disclosed separately within this Group FCR. Disclosures relating to Group practices that are the same across the Group are mentioned only once in this report.

The executive summary outlines material changes over the reporting period. Due to differences between the IFRS and EBS bases the numbers presented in this report are not all comparable to those published in the financial statements as at 31 December 2020.

BUSINESS AND PERFORMANCE

The Group is a provider of global specialty insurance and reinsurance focusing on short-tail business in four main categories: Property, Energy, Marine and Aviation.

Gross premiums written increased by 15.2% in 2020 compared to 2019. The increase is primarily due to new business flows and positive rating trends resulting in a renewal price index of 112% for 2020. The Group has also grown and evolved its product offering as market conditions improve.

During 2020, Lancashire experienced an active loss environment across both its specialty and catastrophe lines, with exposure to COVID-19 related losses and to a number of natural catastrophe events, including hurricanes Laura and Sally, the Midwest derecho storm and the wildfires in California. The Group's net loss ratio for 2020 was 59.6% compared to 30.8% in 2019 (56.5% compared to 12.5% for LICL). Prior year favourable development for 2020 was $52.0 million, compared to $88.0 million of favourable development in 2019.

In response to the COVID-19 pandemic, the Group initiated its Post Loss Response process. The process reviewed and assessed the potential implications for each class of business that the Group underwrites, across all its platforms, with involvement from underwriting, exposure management, actuarial, claims, treasury and finance teams. The output of this review formed the basis of our loss reserving. The current best estimate financial impact of COVID-19 is $42.2 million, net of reinsurance and including the impact of reinstatement premiums. This constitutes 6.9% of our total net loss reserves and 2.7% of our net assets and relates primarily to our property segment.

The Group's investment portfolio generated a strong total return of 3.9% in 2020 with positive returns from all asset classes, driven primarily by the fixed maturity portfolios, given the decline in treasury yields and the tightening of credit spreads during the year. The tighter spreads and stronger equity markets also drove significant returns in the hedge fund and private debt portfolios. This was in contrast to 2019 which generated a strong total return of 4.9% with positive returns from all asset classes, driven primarily by the three 25 basis point rate cuts by the Federal Reserve. LICL's total investment returns were 4.0% in 2020 and 5.1% in 2019.

Other operating expenses were $114.4 million in 2020 compared to $106.0 million in the same period last year. The increase was driven primarily by higher employment costs due to an increase in the number of employees from 218 in the prior year to 255 in the current year. Non-employment costs increased slightly due to a number of project initiatives during the year which drove an increase in legal and external consulting fees. These increases were partly offset by reduced expenditure on travel and entertainment.

Overall, the Group generated comprehensive income of $24.3 million with a combined ratio of 107.8% in 2020 compared to comprehensive income of $145.7 million and a combined ratio 80.9% in 2019. LICL's comparable results were $49.0 million and 102.6% in 2020 compared to $162.2 million and 55.4% in 2019.

GOVERNANCE STRUCTURE

The Group strives to implement simple yet effective systems of governance in a way that helps shape strategy, monitors its implementation, balances support and challenge for management and the business and embeds a positive and open corporate culture throughout the Group. The LICL Board aligns its systems of corporate governance with that of the Group where applicable.

Good strategic debate and decision making remain central to the work of any board. We are fortunate in having a nimble strategy and a simple "flat" structure with a total employee headcount at 31 December 2020 of 255 at LHL and 49 at LICL. This means that all our Directors have regular opportunities to meet with both the members of our management team and other employees within the business. That helps inform the Board's active understanding of the business, its needs and challenges.

Bermuda regulated insurers are required to prepare an ORSA report (referred to by the BMA as GSSA for Group reporting, and CISSA for LICL reporting). Both the management team and the Board have engaged fully with the ORSA processes, and use it as a tool to help deepen our understanding of the business, better understand the risks and opportunities facing it and to refine and focus Lancashire's strategic thinking and priorities.

Details of the LHL and LICL Board of Directors, Board Committees and key functions are provided in Section B. There have been no material changes to the Group's governance structure during the year. The LHL Board Committees' terms of reference were reviewed by the LHL Board during 2020 and were considered to be in line with current best practice.

RISK PROFILE

The Group is exposed to risks from several sources. These include insurance risk, market risk, liquidity risk, credit risk, operational risk and strategic risk. The primary risk to the Group is insurance risk. There have been no significant changes to the Group's material risks or the measures used to assess these risks over the 2020 reporting period. Each of these risk areas is described in more detail in Section C. This includes the impacts of the COVID-19 pandemic on the risk profile.

SOLVENCY VALUATION

Detailed explanations and reconciliations from the assets and liabilities presented in the Group's and LICL's financial statements as at 31 December 2020 to those presented on an EBS basis in this report are included in Section D.

The valuation of technical provisions for the EBS moves from an IFRS 'best estimate' basis to a discounted cashflow approach. There have been no material changes to the valuation process or methodology since 2019 year-end.

CAPITAL MANAGEMENT

The key aim of the Group's capital management processes are unchanged and remain focused on maintaining a strong balance sheet, whilst:

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

On 10 June 2020, LHL issued 39,568,089 new common shares, raising a total of $340.3 million, $19.8 million of which is included in share capital and $320.5 million of which is included in contributed surplus, net of offering expenses. The capital augments our already robust capital base and remains at our disposal to fund new underwriting opportunities in 2021.

LICL, as a wholly owned subsidiary of LHL falls within the scope of the Group's capital management processes. The Group and LICL's regulatory capital position is detailed in Section E and reflects the BMA's BSCR arrangements. Both LHL and LICL have held capital in excess of their regulatory requirements throughout 2020 and 2019.

- the Group's 2020 year-end BSCR was $667.9 million with an ECR ratio of 220%.
- LICL's 2020 year-end BSCR was $633.9 million with an ECR ratio of 206%.

SUBSEQUENT EVENTS

DEBT ISSUANCE

LHL issued $450 million of junior subordinated notes in March 2021. The notes have been approved by the BMA as Tier 2 Ancillary capital. The proceeds of the notes will be used to repay the Group's existing senior and junior debt, which totals approximately $327.5 million, with the surplus available to support new underwriting opportunities. The Group's existing debt instruments were not approved for regulatory capital purposes so the impact of the issuance on the Group's and LICL's regulatory capital position will be favourable. Including the $450 million of junior subordinated notes as Tier 2 Ancillary capital would increase the 31 December 2020 total eligible capital to $1,920.4 million and materially increase the ECR ratio.

OTHER EVENTS

There have been no other significant events that are material to the Group or the Company that have taken place since the end of the 2020 financial year to the date of filing this Financial Condition Report.

However, on 9 February 2021, the Board of Directors declared the payment of an ordinary dividend of $0.10 per common share, which will result in an aggregate payment of approximately $24.4 million. The dividend will be paid on 4 June 2021 to shareholders of record on 7 May 2021.

Further details on subsequent events are provided in Section F1.

Directors' statement

We confirm that to the best of our knowledge and belief, this Financial Condition Report fairly represents the financial condition of the Group and the Company in all material respects.

Alex Maloney
Group CEO

Natalie Kershaw
Group CFO

20 May 2021

A. Business and performance

A1: BUSINESS

Name and Legal Form
The Lancashire Group and LICL are providers of global specialty insurance and reinsurance products.

LHL was incorporated under the laws of Bermuda on 12 October 2005.

LICL was incorporated under the laws of Bermuda on 28 October 2005 and is authorised by the BMA as a Class 4 general insurer under The Insurance Act 1978 and related Regulations ("the Act").

The registered office of the Group and Company is Power House, 7 Par-La-Ville Road, Hamilton HM 11, Bermuda.

Supervisory Authority and Group Supervisor
The Group and LICL are supervised by the Bermuda Monetary Authority, BMA House, 43 Victoria Street, Hamilton, HM 12, Bermuda.

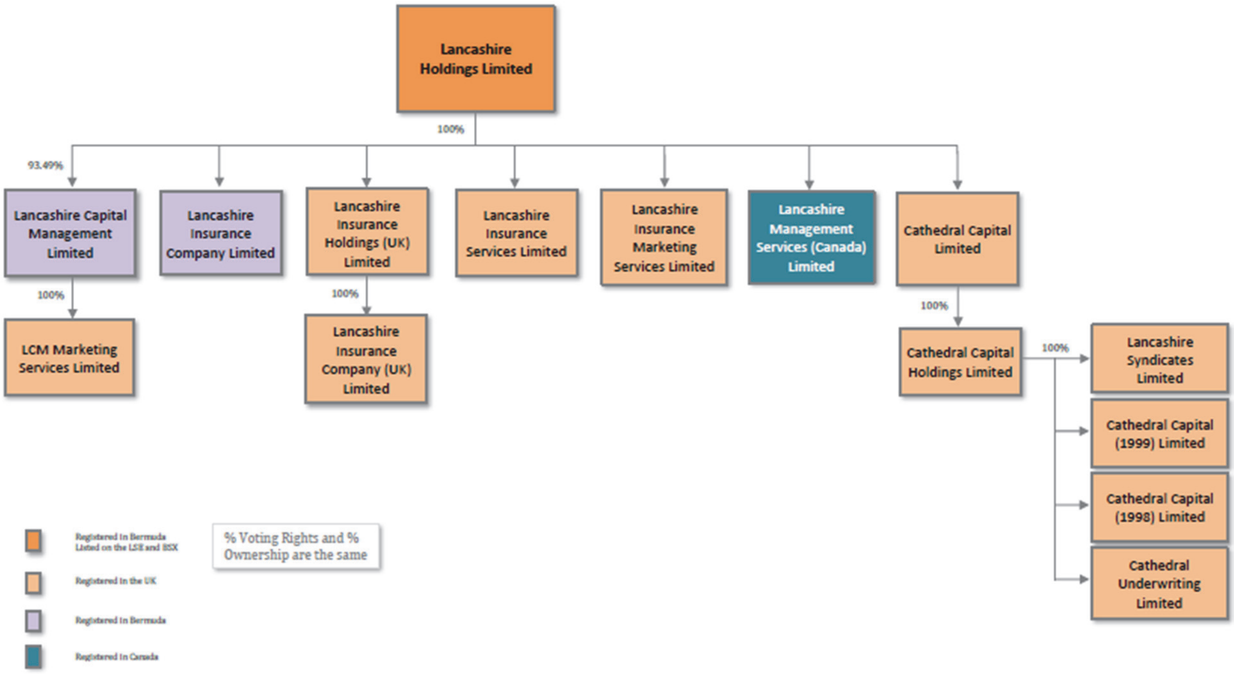
External Auditor
LHL's external auditor is KPMG LLP, 15 Canada Square, London, E14 5GL.

LICL's external auditor is KPMG Audit Limited, Crown House, 4 Par-la-Ville Road, Hamilton, HM 08, Bermuda.

Ownership
LHL's common shares are traded on the main market of the London Stock Exchange ("LSE"), with a secondary listing on the Bermuda Stock Exchange ("BSX"). Voting rights are equivalent to share ownership.

LICL is a wholly owned subsidiary of LHL.

Group Structure
The Group's structure is summarised in the chart below, including country of incorporation:



A. BUSINESS AND PERFORMANCE CONTINUED

A2: UNDERWRITING PERFORMANCE

The Group and LICL are providers of global specialty insurance and reinsurance focusing on short-tail business in four main categories: Property, Energy, Marine and Aviation.

The operating segments for the purpose of segmental reporting have been revised in the current year. The revenue and expenses previously reported in the Lancashire Syndicates segment are now reported across the four principal operating segments. Comparative figures for the year ended 31 December 2019 have been represented in conformity with the current year view.

The Group and Company's underwriting performance on an IFRS basis for the years ended 31 December 2020 and 2019 is summarised in the tables below.

LHL:

For the year ended 31 December 2020	Property $m	Aviation $m	Energy $m	Marine $m	Total $m
– U.S. and Canada	250.4	10.9	33.2	6.3	300.8
– Worldwide – multi territory	50.7	80.0	81.0	72.8	284.5
– Europe	46.3	19.4	9.1	6.1	80.9
– Rest of World	79.5	40.7	21.4	6.3	147.9
Total	426.9	151.0	144.7	91.5	814.1
Outwards reinsurance premiums	(157.9)	(71.3)	(47.7)	(17.8)	(294.7)
Change in unearned premiums	(15.7)	(18.1)	(6.7)	(11.0)	(51.5)
Change in unearned premiums on premiums ceded	(1.7)	8.8	1.0	(0.2)	7.9
Net premiums earned	251.6	70.4	91.3	62.5	475.8
Insurance losses and loss adjustment expenses	(159.4)	(79.6)	(85.1)	(39.5)	(363.6)
Insurance losses and loss adjustment expenses recoverable	14.6	47.5	18.3	(0.6)	79.8
Insurance acquisition expenses	(62.3)	(25.8)	(28.0)	(22.9)	(139.0)
Insurance acquisition expenses ceded	10.1	12.4	1.2	0.3	24.0
Net underwriting profit (loss)	**54.6**	**24.9**	**(2.3)**	**(0.2)**	**77.0**

For the year ended 31 December 2019	Property $m	Aviation $m	Energy $m	Marine $m	Total $m
– U.S and Canada	194.6	5.2	20.0	6.4	226.2
– Worldwide – multi territory	59.1	68.1	89.4	60.1	276.7
– Europe	44.7	18.9	4.8	4.3	72.7
– Rest of World	83.7	27.4	13.9	6.1	131.1
Total	382.1	119.6	128.1	76.9	706.7
Outwards reinsurance premiums	(167.0)	(56.7)	(43.6)	(14.7)	(282.0)
Change in unearned premiums	(3.0)	(28.2)	(0.3)	(4.3)	(35.8)
Change in unearned premiums on premiums ceded	14.4	16.5	1.3	0.6	32.8
Net premiums earned	226.5	51.2	85.5	58.5	421.7
Insurance losses and loss adjustment expenses	(185.3)	(36.2)	(27.5)	(15.5)	(264.5)
Insurance losses and loss adjustment expenses recoverable	111.5	17.6	8.5	(2.9)	134.7
Insurance acquisition expenses	(60.4)	(17.5)	(27.0)	(19.5)	(124.4)
Insurance acquisition expenses ceded	9.5	7.9	1.4	0.2	19.0
Net underwriting profit	**101.8**	**23.0**	**40.9**	**20.8**	**186.5**

A. BUSINESS AND PERFORMANCE CONTINUED

LICL:

For the year ended 31 December 2020	Property $m	Aviation $m	Energy $m	Marine $m	Total $m
– U.S. and Canada	138.0	—	8.6	—	146.6
– Worldwide – multi territory	25.2	24.2	37.5	29.2	116.1
– Europe	24.7	—	4.2	—	28.9
– Rest of World	38.6	—	7.1	—	45.7
Gross premiums written	226.5	24.2	57.4	29.2	337.3
Outwards reinsurance premiums	(82.7)	(0.1)	—	(2.9)	(85.7)
Change in unearned premiums	(7.5)	0.2	(1.6)	(4.3)	(13.2)
Change in unearned premiums on premiums ceded	(0.9)	(0.1)	(0.8)	—	(1.8)
Net premiums earned	135.4	24.2	55.0	22.0	236.6
Insurance losses and loss adjustment expenses	(47.9)	(10.8)	(39.1)	(24.6)	(122.4)
Insurance losses and loss adjustment expenses recoverable	(11.7)	0.3	0.2	—	(11.2)
Insurance acquisition expenses	(37.4)	(11.1)	(30.2)	(10.8)	(89.5)
Insurance acquisition expenses ceded	6.3	0.1	—	0.1	6.5
Net underwriting profit (loss)	**44.7**	**2.7**	**(14.1)**	**(13.3)**	**20.0**

For the year ended 31 December 2019	Property $m	Aviation $m	Energy $m	Marine $m	Total $m
– U.S. and Canada	100.6	—	2.3	—	102.9
– Worldwide – multi territory	25.2	23.8	48.1	24.4	121.5
– Europe	23.9	—	1.2	—	25.1
– Rest of World	42.5	—	2.5	—	45.0
Gross premiums written	192.2	23.8	54.1	24.4	294.5
Outwards reinsurance premiums	(88.0)	(0.2)	(1.4)	(2.3)	(91.9)
Change in unearned premiums	(2.8)	(4.6)	1.4	0.4	(5.6)
Change in unearned premiums on premiums ceded	11.3	0.2	0.8	—	12.3
Net premiums earned	112.7	19.2	54.9	22.5	209.3
Insurance losses and loss adjustment expenses	(67.2)	(6.9)	(7.4)	(3.0)	(84.5)
Insurance losses and loss adjustment expenses recoverable	58.3	—	—	—	58.3
Insurance acquisition expenses	(30.8)	(7.3)	(24.2)	(9.1)	(71.4)
Insurance acquisition expenses ceded	5.3	—	—	0.1	5.4
Net underwriting profit	**78.3**	**5.0**	**23.3**	**10.5**	**117.1**

Property

Our property segment includes our property reinsurance lines, such as property catastrophe and retrocession, as well as property insurance and terrorism and political risks. Our property (re)insurance lines all contain high degrees of catastrophe risk and as such have seen pricing dislocation during 2020 leading to the property segment RPI of 108%. Catastrophe exposed products are the most capital intensive within our portfolio. It is in these lines where we see strong pricing dynamics, where we will use our robust capital position to enable further growth in 2021. We underwrite these classes across all of our underwriting platforms and remain both product and platform agnostic as to where we grow. The building blocks for growth in the product lines have been cemented in place. The capital is available to support growth in an improving market and we expanded our underwriting teams and platform options when these positive signs first appeared. As always, the growth will be driven by the underwriting opportunity and we have the flexibility to adapt to the market conditions in each product line.

In the catastrophe exposed classes, we remain very aware of the changing climate and the elevated risks this brings. Our strong risk management is supplemented with the use of vendor models that collate the latest available data on the frequency and severity of the principal catastrophe events such as windstorm, flood and earthquake. This information forms part of our underwriting process which helps us assess and price natural catastrophe risk. With heightened awareness of climate change, demand for the products we sell increases and as the underwriting of climate change improves so does our assessment of such risk. Natural catastrophe events are damaging to businesses and economies. The products our industry sells help people, businesses and economies to rebuild.

A. BUSINESS AND PERFORMANCE CONTINUED

The terrorism and political risk products we sell do not currently benefit from the same market dynamics as our other products. Market conditions are stable but not improving. These classes have not experienced many loss events and appetite for these classes remains strong across the market. Consequently, the demand and supply dynamics are not pushing the rating environment forward. The terrorism risks we underwrite range from hotels in city centres to offshore windfarms, and our political and sovereign risk product supports investments in various industries and infrastructure projects across the globe. Given the link between the economy and our political and sovereign risk offering, demand for the product is impacted by the COVID-19 pandemic, but as the economy recovers so should this demand. Our appetite for these products remains stable in line with market conditions and this segment of our business continues to generate healthy underwriting returns.

Aviation
Our aviation segment has been building out steadily in the past few years, growing our product offering as market conditions improve. Much like the marine market, capacity has continued to tighten with numerous capacity providers retracting from multiple product lines. We had the platforms and people to seize this opportunity to grow just when market conditions improved. As can be seen from our aviation RPI of 121%, market conditions have been favourable for growth in 2020.

The aviation industry has had one of its most challenging years in history with COVID-19 unexpectedly impacting global demand for air travel. Our clients have been severely tested, and they will continue to be tested in years to come. We aim to adapt where possible and support clients, whilst finding a balance that allows for underwriting profitability. The products we sell are often mandatory purchase products, and therefore there is some insulation from demand headwinds. In addition, as other capacity providers retract, we have grown our market share in a profitable market, stepping in to provide needed capacity.

As we look to 2021, whilst we anticipate continued rate improvement, there will be demand headwinds in a sector so badly impacted by COVID-19. Whilst we anticipate some form of industry recovery, it is likely to be slow. Overall, despite these challenges, our aim will be to further grow our aviation segment where possible.

Energy
Our energy portfolio continues to evolve, building upon foundations laid in recent years to diversify our product offering. Only a few years ago our portfolio was principally upstream assets and now we underwrite all parts of the energy industry including upstream energy, downstream energy, power and utilities and renewable energy.

Market conditions within the energy segment vary considerably. The 2020 energy RPI of 113% masks the different levels of pricing movement within each segment. Within upstream energy (which includes renewable energy) capacity for these products remains plentiful so, whilst rate momentum is positive, the rate of increase is less pronounced than within both downstream energy and power. In these two segments of the energy market supply of capacity has continued to retract following a high frequency of loss incidents, which has fuelled price momentum and allowed us to develop our underwriting footprint. Given the current economic environment, the energy sector is experiencing a difficult period with demand directly linked to the health of the global economy. In parts of the energy sector, such as upstream energy and to a lesser degree the downstream sector, these difficulties could create demand headwinds for insurance products in 2021. Power and utilities see far less impact and this demonstrates the value of having a more diversified product offering. Despite these challenges our clients still require insurance; in fact the value of insurance products is even more important at times of financial stress as they provide balance sheet protection and encourage active risk management.

Our portfolio will continue to evolve as our clients do. The energy industry itself is changing and will continue to do so in the future. As the world moves to a more sustainable future the assets our clients invest in will change to meet this goal and the products we sell will continue to adapt to support this changing client demand.

Marine
Our marine segment encompasses all aspects of the marine industry from cargo to cruise liners; we underwrite the marine class from both our Lloyd's and Company platforms. The marine market has seen capacity withdrawals across all sub-segments for the past number of years. As a result, market pricing has been rising, demonstrated by our marine RPI of 116% in 2020. The year saw some high-profile marine incidents that generated losses to the sector, from which we were not immune. These losses further strengthen the marine market's resolve to improve the profitability of the product.

Whilst everyone would prefer for these incidents not to occur, they demonstrate the value of our insurance products. Our insurance helps companies protect their balance sheets in difficult times and helps fund valuable clean-up operations protecting the environment and local economies.

Like many industries, discrete parts of the marine industry have been directly impacted by COVID-19. Demand from certain clients, for example cruise liner operators, has reduced significantly. The insurance industry has reacted and adapted insurance products as best it can to assist clients in these difficult times. Despite these demand headwinds, we have been able to grow our marine footprint during 2020 ahead of rate increases, which is extremely pleasing. We anticipate market conditions to continue to strengthen into 2021 and will be looking to grow and strengthen our marine segment further.

A. BUSINESS AND PERFORMANCE CONTINUED

COVID-19 pandemic

On 12 March 2020, the World Health Organisation classified the COVID-19 outbreak as a pandemic. The COVID-19 pandemic is an ongoing situation making it exceptionally difficult to predict what the ultimate impact for the Group or the insurance industry will be.

In response to the COVID-19 pandemic, the Group initiated its Post Loss Response process. The process reviewed and assessed the potential implications for each class of business that the Group underwrites, across all its platforms, with involvement from underwriting, exposure management, actuarial, claims, treasury and finance teams. The output of this review formed the basis of our loss reserving. The current best estimate financial impact of COVID-19 is $42.2 million ($38.6 million for LICL), net of reinsurance and including the impact of reinstatement premiums. This constitutes 6.9% of our total net loss reserves and 2.7% of our net assets and relates primarily to our property segment.

The Group does not write the following lines of business: travel insurance; trade credit; and long-term life and prior to the COVID-19 pandemic did not write Directors and Officers or medical malpractice. The Group underwrites a small number of event cancellation contracts and has minimal exposure through mortgage, accident and health business.

On 15 January 2021, the UK Supreme Court delivered its judgement on the FCA's business interruption test case. The aim of the test case was to obtain clarity on insurance contract wording and determine whether certain business interruption clauses were triggered by the COVID-19 pandemic. For the insurance industry, this means that in certain instances, policyholders will now have their COVID-19 related business interruption claims paid where previously these claims may have been denied. It may also impact the reinsurance industry as insurers will seek to recover from the reinsurance protection they have in place. In light of the UK Supreme Court ruling, the Group has performed a detailed review of the business interruption clauses in its insurance and reinsurance contracts and concluded that there is no material impact on the COVID-19 best estimate loss booked for the year ended 31 December 2020.

The Group's long-term strategy is to deploy more capital into a hardening market, in which pricing strengthens due to market capital constraints, and to lower the amount of capital deployed in a softer market, where pricing is weaker due to over-supply of risk capital. The COVID-19 pandemic has generated (re)insurance market losses both in terms of the claims environment and the impact on financial markets. In the face of these challenges there has been a retrenchment in (re)insurance markets risk capital and capacity. This in turn has led to continued rate increases in many of the Group's core insurance segments and accelerated rating dislocation in the catastrophe exposed reinsurance lines. The Group expects the momentum of rising rates to continue in this and other classes of business across its portfolio throughout 2021 and beyond. The Group expects to take advantage of this rating improvement by writing increased levels of business at higher pricing levels.

On 10 June 2020, the Group raised an additional $340.3 million of equity capital which will be used to fund organic growth and take advantage of the much improved market opportunities.

The maintenance of financial strength ratings are a key factor impacting on the ability of the Group to continue as a going concern. A ratings downgrade to lower than A- could adversely impact on the ability of the Group to source and write new business, retain existing business or enter into new financing arrangements. A.M. Best has assigned LICL and LUK a financial strength rating of A (Excellent). This was reaffirmed on 22 September 2020 and the outlook for all entities is stable. Lancashire syndicates 3010 and 2010 also benefit from an A.M. Best rating of A (Excellent) assigned to all Lloyd's of London syndicates. This was reaffirmed on 15 July 2020 and the outlook is stable.

As at 31 December 2020, the Group considers that it has more than adequate liquidity to pay its obligations as they fall due. The Group held cash and cash equivalents of $432.4 million and fixed maturity investments with maturity dates of less than one year of $276.0 million. In addition to the cash and investment portfolio, the Group also has access to a number of LOC and revolving credit facilities.

As at 31 December 2020, the average credit quality of the fixed maturity portfolio was A+ (31 December 2019: A+) and there has not been a change in our counterparty credit exposure as a result of the COVID-19 pandemic. However, it is an area we continue to monitor.

During the year-ended 31 December 2020, there has been no restructuring of the Group's long-term debt as a result of the COVID-19 pandemic and the Group was in compliance with its financial covenants under each of its financing arrangements. In addition, no uncertainties have been identified around the ability to meet the interest payments of the Group's long-term debt.

Whilst considering guidance from both regulatory and shareholder bodies in relation to the use of capital, including payments of dividends, the Group's dividend policy has remained unchanged from prior years. The Board considers that the business is well capitalised to meet all of its obligations to our policyholders and to afford appropriate headroom for growth opportunities. In view of this, the Group paid its final ordinary dividend of $0.10 per common share in relation to the 2019 financial year and declared an interim dividend of $0.05 per common share during the year. There is currently no expectation to amend the Group's dividend policy for the foreseeable future.

The Group has not entered into any rent concessions or other lease modifications during the year ended 31 December 2020 as a result of the COVID-19 pandemic and is not expected to enter into any rent concessions or modifications in the foreseeable future.

The Group has not applied for, or received, any grants offered by the UK government to support businesses during the ongoing COVID-19 pandemic and is not expected to in the foreseeable future. None of our employees have been furloughed and we are not expected to furlough any employees in the foreseeable future.

A3: INVESTMENT RETURN

Since inception, the primary objectives for our investment portfolio have been capital preservation and liquidity. Those objectives remain unchanged, and are more important than ever in today's volatile and reactive markets. As market volatility continues, we position our portfolio to limit downside risk in the event of market shocks. 2020 has been an extremely volatile year, but the Group's investment portfolio has rebounded from the stress of the first quarter. In this environment of very low rates and a flat yield curve, it does not pay to increase duration. While any expectations of higher rates is at least a few years out, the Group's focus will be on maintaining a defensive portfolio with short duration and high credit quality. We will use our risk budget to add to our portfolio some additional yield, however we will endeavour to add low volatility products. We continue to maintain a short duration fixed maturity portfolio and have been using our risk budget to add products to our portfolio to help diversify from interest rate volatility.

Our portfolio mix illustrates our conservative philosophy. With the composition regulated by the Group's investment guidelines, we have three investment portfolio categories: 'core', 'core plus' and 'surplus'. The core and core plus portfolios contain at least enough funds required to meet near-term obligations and cash flow needs following an extreme event. Assets in excess of those required to be held in the core and core plus portfolios may be held in any of the three portfolio categories.

The composition, duration and asset allocation of the investment portfolio are reviewed on a regular basis in order to respond to changes in interest rates and other market conditions. If certain asset classes are anticipated to produce a higher return within management's risk tolerance, an adjustment in asset allocation may be made. Conversely, if the risk profile is expected to move outside of tolerance levels, adjustments may be made to reduce the risk in the portfolio. We try to be nimble in our investment strategy while putting our objective of capital preservation first and foremost.

We believe in the application of common sense, and do not place much reliance on 'black box' approaches to investment selection.

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

Group net investment income excluding realised and unrealised gains and losses was $29.0 million for the year ended 31 December 2020, a decrease of 23.1% compared to 2019. Total investment return, including net investment income, net realised gains and losses, impairments and net change in unrealised gains and losses, was $69.1 million for the year ended 31 December 2020 compared to $83.2 million for 2019 ($55.0 million and $64.6 million respectively for LICL).

In a year of significant volatility, the investment portfolio generated a strong total return of 3.9% (4.0% for LICL) with positive returns generated from all asset classes. The returns were driven primarily by the fixed maturity portfolios, given the decline in treasury yields and the tightening of credit spreads during the year. The tighter spreads and stronger equity markets also drove significant returns in the hedge fund and private debt portfolios. All other asset classes also had positive returns on a year to date basis. The Group's investment portfolio generated a strong total return of 4.9% (5.1% for LICL) in 2019 with positive returns from all asset classes driven primarily by the three 25 basis point rate cuts by the Federal Reserve. Credit spreads also tightened during 2019.

The Group's total investment return (excluding foreign exchange) for the years ended 31 December 2020 and 2019 is summarised below:

LHL	2020 $m	2020 %	2019 $m	2019 %
Fixed maturity securities – AFS	49.6	72%	64.4	77%
Fixed maturity securities – at FVTPL	2.9	4%	5.3	6%
Equity securities – AFS	—	—%	3.8	5%
Hedge funds – at FVTPL	4.7	7%	3.0	4%
Private investment funds – at FVTPL	7.3	11%	—	—%
Other investments	2.4	3%	2.4	3%
Cash and cash equivalents	2.2	3%	4.3	5%
Total	**69.1**	**100%**	**83.2**	**100%**

LICL	2020 $m	2020 %	2019 $m	2019 %
Fixed maturity securities – AFS	36.6	67%	49.1	76%
Fixed maturity securities – at FVTPL	2.9	5%	5.3	8%
Equity securities – AFS	—	—%	3.8	6%
Hedge funds – at FVTPL	4.7	9%	3.0	5%
Private investment funds – at FVTPL	7.3	13%	—	—%
Other investments	2.2	4%	1.9	3%
Cash and cash equivalents	1.3	2%	1.5	2%
Total	**55.0**	**100%**	**64.6**	**100%**

A4: OTHER MATERIAL INFORMATION

Combined operating expenses for the years ended 31 December 2020 and 2019:

	LHL		LICL	
	2020 $m	2019 $m	**2020 $m**	2019 $m
Other Operating Expenses	114.4	106.0	26.1	23.9
Equity-based Compensation	12.3	9.6	2.3	1.9
Total	**126.7**	**115.6**	**28.4**	**25.8**

Other operating expenses were $114.4 million in 2020 compared to $106.0 million in the same period last year ($26.1 million and $23.9 million for LICL). The increase was primarily driven by higher employment costs due to an increase in the number of employees from 218 in the prior year to 255 in the current year. Non-employment costs increased slightly due to a number of project initiatives during the year which drove an increase in legal and external consulting fees. These increases were partly offset by reduced expenditure on travel and entertainment and promotional events.

The equity based compensation expense was $12.3 million in 2020 compared to $9.6 million in the same period last year. The equity-based compensation charge was driven by anticipated vesting levels of active awards based on current performance expectations. Increased equity-based compensation charges were recorded in 2020 as higher performance targets were met.

The total contribution from third-party capital activities consists of the following items:

LHL	**2020 $m**	2019 $m
LCM underwriting fees	10.0	7.9
LCM profit commission	1.8	1.0
LSL fees and profit commission	3.5	2.5
Share of profit of associate	10.7	5.9
Total	**26.0**	**17.3**

The higher LCM underwriting fees in 2020 reflect the increased level of premiums under management compared to 2019. The amount of LCM profit commission recognised is driven by the timing of loss experience, settlement of claims and collateral release and therefore varies year on year. The share of profit of associate reflects Lancashire's equity interest in the LCM managed vehicle.

LICL's other income is made up as follows:

LICL	**2020 $m**	2019 $m
LSL Quota Share income	2.4	6.4
Net service fee income	1.3	1.6
Total	**3.7**	**8.0**

The Company enters into a quota share treaty ("QST") agreement with CCL 1998. Under this agreement CCL 1998 cedes 85.0% of its financial result, which includes both insurance and non-insurance balances, to the Company. Net other income (losses) in the Company's statement of comprehensive income includes an income of $2.4 million (2019: $6.4 million) relating to the QST agreement.

The Company conducts business with its parent company and other Group subsidiaries. This includes providing services, including professional and administrative support services, to related entities within the Group. Service agreements are in place to allow corresponding expenses to be re-allocated to the relevant entity with a mark-up to reflect commercial terms. For the year ended 31 December 2020 the Company recorded net service fee income of $1.3million (2019: $1.6 million) relating to such transactions with LHL and its subsidiaries.

A. BUSINESS AND PERFORMANCE CONTINUED

Excerpts from the CCL 1998 statement of comprehensive income are shown below. LICL's share of the CCL 1998's financial results is shown in the statement of comprehensive income within net other income:

LICL	2020 $m	2019 $m
Gross premiums written	356.5	299.8
Outwards reinsurance premiums	(115.2)	(105.6)
Net premium written	241.3	194.2
Net premium earned	214.8	175.0
Net insurance losses and loss adjustment expenses	131.5	97.4
Other expenses	80.5	70.1
Net result	2.8	7.5
LICL 85% share of net result from CCL 1998	**2.4**	**6.4**

LICL holds $268.2 million (31 December 2019 – $265.4 million) of cash and cash equivalents and fixed maturity securities in FAL in relation to the CCL 1998 QST agreement, with the remaining FAL requirement covered by an LOC facility. An uncollateralised facility has been in place since 30 July 2019, for an original amount of $31.0 million. The facility was increased from $31.0 million to $44.0 million on 28 October 2019 and further increased from $44.0 million to $95.0 million on 2 November 2020 and will expire on 31 December 2024. It is available for utilisation by LICL and guaranteed by LHL for FAL purposes. As at 31 December 2020, $90.5 million of LOCs were issued under this facility.

B. Governance structure

B1: SYSTEM OF GOVERNANCE

The Group strives to implement simple yet effective systems of corporate governance in a way which helps shape strategy, monitors its implementation, balances support and challenge for management and the business and embeds a positive and open corporate culture throughout the Group. The LICL Board aligns its systems of corporate governance with that of the Group where applicable.

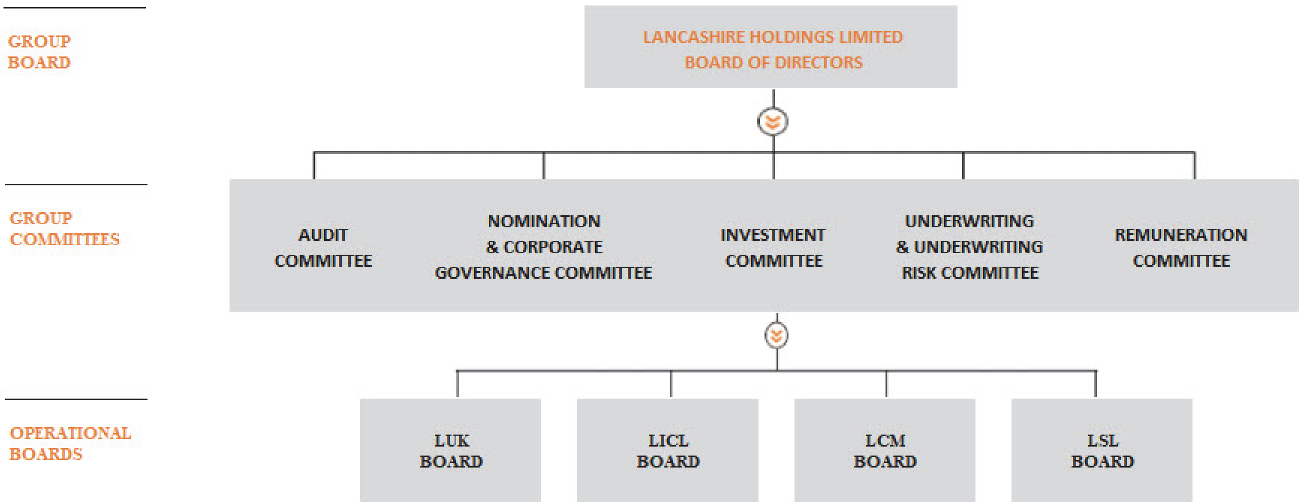
Good strategic debate and decision making remain central to the work of any board. At LHL and LICL we are fortunate in having a nimble strategy and a simple "flat" structure with a total employee headcount at 31 December 2020 of 255 at LHL and 49 at LICL. This means that all our Directors have regular opportunities to meet with both the members of our management team and other employees within the business. That helps inform the Board's active understanding of the business, its needs and challenges.

Bermuda regulated insurers are required to prepare an ORSA report (GSSA for Group reporting, and CISSA for LICL reporting). Both the management team and the Board have engaged fully with the ORSA process, and use it as a tool to help deepen their understanding of the business, better understand the risks and opportunities facing it and to refine and focus Lancashire's strategic thinking and priorities.

As a premium-listed company on the LSE, LHL measures its corporate governance compliance against the requirements of the UK Corporate Governance Code published by the UK FRC. The UK's Financial Conduct Authority ("FCA") requires each company with a premium listing to 'comply or explain' against the Code (i.e. to disclose how it has complied with Code provisions or, if the Code provisions have not been complied with, provide an explanation for the non-compliance). The Group monitors its compliance with the Code on at least a quarterly basis. The LICL Board seeks to align its general approach, in relation to the matters that they regularly consider, with that of the LHL Board and committees and their terms of reference as adopted from time to time.

As a wholly owned subsidiary, the Company benefits from the guidance provided by the Group's Board of Directors ("Board") and Committees.

The Group's Board has established Audit, Investment, Nomination Corporate Governance & Sustainability, Underwriting and Underwriting Risk and Remuneration Committees. Each of the Committees has written terms of reference, which are reviewed regularly and are available on the Group's website. The Committees' terms of reference were reviewed by the LHL Board during 2020 and were considered to be in line with current best practice. The LHL Board and its Committees are generally scheduled to meet quarterly, although additional meetings and information updates are arranged as business requirements dictate. LICL's Board also generally meets quarterly.



Please refer to the Corporate Governance section of the Group's 2020 Annual Report and Accounts for additional details on the Group's system of governance, supplementary to that disclosed below: Investors – Lancashire Group.

B2: BOARD MEMBERS AND SENIOR EXECUTIVES

The Board of Directors is responsible for the leadership, strategy and control and the long-term success of Lancashire's business. The Board has reserved a number of matters for its decision, including responsibility for setting the Group's values and standards, and approval of the Group's strategic aims and objectives. The Board is responsible for the approval of the Group's risk appetites, defining its risk tolerances, and setting and monitoring the risk management and internal control systems including compliance with risk tolerances.

During 2020 the Board carried out a robust assessment of the principal risks affecting the Group's business model, future performance, solvency and liquidity and the operation of internal control systems.

The Board has delegated certain matters to Committees of the Board. There are a number of matters which the Board considers not suitable for delegation including: approval of dividends and dividend policy; receiving reports from the Group CRO and legal and compliance department; approval of the Annual Report and Accounts and any qualification thereon; approval of significant changes in accounting policy or practice; approval of annual regulatory submissions; appointments and removal of directors and the Company Secretary; selection of the Chairman and CEO; committee membership and chairmanship; appointment and removal of external auditors; division of responsibilities between the Group Chairman and CEO; approval of committee Terms of Reference; receiving committee reports; and determining the independence of directors. Further details pertaining to the Board's schedule of reserved matters are available on the Group's website here: Our Board – Lancashire Group.

Further information relating to the Group Board committees can be found on pages 62 to 81 of LHL's 2020 Annual Report and Accounts, available on the Group's website here: Investors – Lancashire Group.

At the regular quarterly Board meetings, the Directors review all areas of the Group's business, strategy and risk management and receive reports from management on underwriting, reserving, finance, investments, capital management, internal audit, risk, legal and regulatory developments, compliance, climate change risk and sustainability and other matters affecting the Group. Management provides the Board with the information necessary for it to fulfil its responsibilities. In addition, presentations are made by external advisers such as the independent actuary, the investment managers, the external auditors, the remuneration consultants and the corporate brokers. The Board Committees are authorised to seek independent professional advice at the Company's expense.

The Board also meets to discuss strategic planning matters in addition to the customary schedule of quarterly meetings. The Board dedicated additional time to strategic opportunity and capital planning discussions in the period prior to its decision to raise additional risk capital by way of an equity placing, which took place in June 2020.

The Board has approved and adopted a formal division of responsibilities between the Chairman and the CEO. The Chairman is responsible for the leadership and management of the Board and for providing appropriate support and advice to the CEO. The CEO is responsible for the management of the Group's business and for the development of the Group's strategy and commercial objectives. The CEO is responsible, along with the executive team, for implementing the Board's decisions.

(I) DIRECTORS AND ROLES AND RESPONSIBILITIES OF KEY FUNCTIONS

LHL Directors

Peter Clarke	Non-Executive Chairman
Michael Dawson	Non-Executive Director
Simon Fraser	Senior Independent Non-Executive Director
Samantha Hoe-Richardson	Non-Executive Director
Robert Lusardi	Non-Executive Director
Sally Williams	Non-Executive Director
Alex Maloney	Chief Executive Officer
Natalie Kershaw	Chief Financial Officer (appointed 1 March 2020)
Elaine Whelan	Chief Financial Officer (retired 28 February 2020)

LICL Directors

Beverley Todd	Non-Executive Chairman
Hayley Johnston	Chief Executive Officer (appointed 1 April 2020)
Elaine Whelan	Chief Executive Officer / President (retired 28 February 2020)
Jennifer Wilson	Chief Financial Officer
Benjamin Readdy	Group Chief Actuary
James Irvine	Chief Underwriting Officer

See section B3(ii) below for details of the skills and experience of the LHL and LICL Directors.

B. GOVERNANCE STRUCTURE CONTINUED

Risk Management Function
The risk management function oversees all the Group and entity level risk management duties. The function is led by Louise Wells, Group CRO, who is a Fellow of the Institute of Chartered Accountants of England and Wales. The Group CRO reports directly to the LHL and LICL Boards. The Group CRO is supported by a number of additional individuals who are deemed to be sufficiently skilled to perform risk management function duties. The risk management function therefore has the required skills, knowledge and expertise to fulfil its duties.

Whilst risk is considered at Board level, committees of the Board have responsibility for various aspects of risk. The Group CRO reports directly to the Group and subsidiary boards and facilitates and aids the identification, evaluation, quantification, mitigation and control of risks at a Group and subsidiary level. The Group CRO provides regular reports to the Group and subsidiary boards covering, amongst other things, actual risk levels against tolerances, emerging risks and any lessons learned. The Board considers that a supportive Enterprise Risk Management ("ERM") culture, established at the Board and embedded throughout the business, is of key importance. Facilitating and embedding ERM, and helping the Group to improve its ERM practices, is a major responsibility assigned to the Group CRO.

The risk management function is deemed sufficiently independent and has performed its duties in an objective and fair manner. The function has direct access to the Board to report on any matters that may impact its ability to perform its duties effectively.

Internal Audit Function
The internal audit function oversees all the Group and subsidiary internal audits. The function is led by Samantha Churchill, Head of Internal Audit, who is a Fellow of the Institute of Chartered Accountants of England and Wales. The Head of Internal Audit reports to the Audit Committees and the LICL Board and is supported by a number of additional individuals who are deemed to be sufficiently skilled to perform internal audit function duties. The internal audit function has the required skills, knowledge and expertise to fulfill its duties. Internal audit plays a key role in the Group's ERM by providing an independent opinion regarding the accuracy and completeness of risks in the risk register, in addition to verification of the effectiveness of controls and the consistency of their operation.

The internal audit function is deemed sufficiently independent and has performed its duties in an objective and fair manner. The function has direct access to the Audit Committee to report on any matters that may impact its ability to perform its duties effectively.

The internal audit function is described more fully in Section B.6 below.

Compliance Function
The Group compliance function oversees all the Group and subsidiary compliance matters. The function is led by John Cadman, Group General Counsel, who has direct access to the LHL Board. Its key responsibilities are to identify, assess, monitor and report on the compliance risks which the Group faces as well as the establishment of a robust compliance framework and assessing the appropriateness of the Group's compliance procedures.

We maintain separate compliance functions across our operating entities to ensure that we maintain our focus on the specific legal and regulatory issues in each of our operating jurisdictions. Within Bermuda, the function is led by Nick Nebard the Head of LICL Compliance, who has direct access to the LICL Board. The compliance function at both the Group and legal entity level is supported by a number of additional individuals who are deemed to be sufficiently skilled to perform compliance function duties. The compliance function has the required skills, knowledge and expertise to fulfil its duties.

The compliance function is deemed sufficiently independent and has performed its duties in an objective and fair manner. The function has direct access to the LHL Board, via the Group General Counsel, and to the subsidiary Boards via other team members, to report on any matters that may impact its ability to perform its duties effectively.

The compliance function is described more fully in Section B.5 below.

Actuarial Function
The actuarial function oversees all the Group and entity level actuarial duties. Ben Readdy is the Group Chief Actuary and is a Fellow of the Institute and Faculty of Actuaries (IFoA). Further, as required by the IFoA, Ben also holds a UK Practising Certificate and complies with the additional requirements from the IFoA to maintain this certificate. The Chief Actuary is supported by a number of additional individuals who are deemed to be sufficiently skilled to perform actuarial function duties. The actuarial function has the required skills, knowledge and expertise to fulfill its duties.

The actuarial function is deemed sufficiently independent and has performed its duties in an objective and fair manner. The function has direct access to the Lancashire Board to report on any matters that may impact its ability to perform its duties effectively.

(II) REMUNERATION POLICY AND PRACTICES

Detailed information concerning the Group's remuneration policies and practices can be found on pages 82 to 104 of LHL's Annual Report and Accounts for 31 December 2020: Investors – Lancashire Group.

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

B. GOVERNANCE STRUCTURE CONTINUED

There is a strong link between the Remuneration Policy and the business strategy. The Group's strategy focuses on the effective operation of the business necessary to deliver superior total shareholder returns on a risk-adjusted basis over the course of the insurance cycle. Our Remuneration Policy and the way it is implemented are closely aligned to this strategy. The Remuneration Committee of the Board of Directors sets the Remuneration Policy for the Group's Chairman, the Executive Directors, Company Secretary and other designated senior executives to deliver long-term benefits to the Group. The full terms of reference for the Remuneration Committee are available on the Group's website here: Board Committees – Lancashire Group.

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

The Remuneration Policy for all staff is, in principle, broadly the same as that for Executive Directors in that any of the Group's employees may be offered similarly structured packages, with participation in annual bonus and long-term incentive plans, although award types (restricted cash, restricted stock or performance shares) and size may vary between different categories of staff. For Executive Directors, with higher remuneration levels, a higher proportion of the compensation package is subject to performance pay, share based remuneration and deferral. This ensures that there is a strong link between remuneration, Group performance and the interests of shareholders.

The non-executive directors are paid a single fee for all responsibilities, although supplemental fees may be payable where additional responsibilities are undertaken, including a non-executive director role on a subsidiary board.

Bonus Plan
The annual bonus is based on financial and personal performance. The precise weightings may differ each year and also differ dependent on the employee's level of seniority and roles and responsibilities within the organisation, with more senior employees having a higher weighting to financial performance metrics. Not all roles have a financial performance element to their bonus structure.

The financial component is based on the Group's key financial measures of performance. For any year, these may include change in FCBVS, growth in BVS, profit, comprehensive income, combined ratio, investment return or any other financial KPI.

Typically, a sliding scale of targets applies for financial performance targets. Bonus is earned on an incremental basis once a predetermined threshold level is achieved. The degree of stretch in targets may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year.

The personal performance component is based upon achievement of clearly articulated objectives. A performance rating is attributed to participating employees, which determines the pay-out for this part of the bonus. The weightings applying to the bonus measures and the degree of stretch in objectives may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year. For Executive Directors, the financial component of the bonus plan will have a higher weighting than the personal element.

The Remuneration Committee will have the ability to override the bonus outcome by either increasing or decreasing the amount payable, subject to the bonus cap of 200% of target bonus, to ensure a robust link between reward and performance. At least 25 % of each Executive Director's bonus is automatically deferred into shares as nil-cost options or conditional awards over three years, with one third vesting each subsequent year. The bonus for the Executive Directors is subject to claw back if the financial statements of the Group were materially misstated or an error occurred in assessing the performance conditions on bonuses and/or if the Executive ceased to be a Director or employee due to gross misconduct.

Further details of the performance criteria for the 2020 annual bonus award for the Group's CEO and CFO are disclosed on pages 95 to 97 of LHL's Annual Report and Accounts for 31 December 2020: Investors – Lancashire Group.

Long Term Incentives
RSS awards are normally made annually in the form of nil-cost options. For Executive Directors and some members of senior management, vesting is dependent on the achievement of performance conditions over at least three financial years, commencing with the year of grant. For all other members of staff, vesting is over three financial years with no performance conditions. The three-year period is longer than the typical pattern of loss reserve development on the Group's insurance business, which is approximately two years. The number of awards will normally be determined by reference to the share price around the time of grant unless the Committee, at its discretion determines otherwise. The Remuneration Committee considers carefully the quantum of awards each year to ensure that they are competitive in light of peer practice and the targets set. Awards are subject to claw back if there is a material misstatement in the Group's financial statements, an error in the calculation of any performance conditions or if the Executive Director ceases to be a Director or employee due to gross misconduct. A dividend equivalent provision operates enabling dividends to be accrued (in cash or shares) on RSS awards up to the point of exercise. Award levels are determined primarily by seniority. A maximum individual grant limit of 350% of salary applies.

Performance metric based awards vest at the end of a three-year performance period based on performance measures reflecting the long-term strategy of the business at the time of grant. These may include measures such as TSR, change in FCBVS, growth in BVS, Group profitability or any other relevant financial measures. If more than one measure is used, the Remuneration Committee will review the weightings between the measures chosen and the target ranges prior to each LTI grant to ensure that the overall balance and level of stretch remains appropriate. A sliding scale of targets applies for financial metrics with no more than 25% vesting for threshold performance.

(III) PENSION OR EARLY RETIREMENT SCHEMES

The Group operates a defined contribution pension scheme (via outsourced pension providers) or cash-in-lieu of pension. There is a salary sacrifice structure in the UK and the opportunity for additional voluntary contributions to be made by individuals, if elected. The pension scheme operates on the same basis for all employees in the Group; there are no supplementary retirement schemes for executive directors or key function holders. Non-Executive Directors do not receive any retirement benefits.

(IV) MATERIAL TRANSACTIONS WITH SHAREHOLDERS, PERSONS WHO EXERCISE SIGNIFICANT INFLUENCE, BOARD MEMBERS OR SENIOR EXECUTIVES

For the year ended 31 December 2020, the following dividends were declared:

LHL:

- An Interim dividend of $0.05 per common share was declared on 29 July 2020 and paid on 11 Sep 2020; and
- A Final dividend relating to 2019 of $0.10 per common share was declared on 13 Feb 2020 and paid on 5 June 2020.

LICL:

- No dividend was declared in 2020.

B3: FITNESS AND PROPRIETY REQUIREMENTS

(I) PROCESS FOR ASSESSING BOARD MEMBERS AND SENIOR EXECUTIVES

The Group has implemented a 'fit and proper' policy and process for persons who effectively run the Group or hold other key functions. The fit and proper policy explicitly covers the Chairman, CEO, Chairman of the Audit Committee, Chairman of the Remuneration Committee, Company Secretary, CFO, CRO, Compliance Oversight Officer and the Heads of Internal Audit and Actuarial functions. The Group defines key functions as those prescribed by the relevant regulators as well as those functions which the Group considers to be important within the system of governance. This policy has been applied to LICL employees that hold these key functions.

The fitness for a role is based on the assessment of the individual's management competence as well as their technical competence. The assessment of propriety of an individual is based on their reputation, which will reflect on their past conduct, criminal record, financial record and their supervisory experience.

The Group has the following principal requirements for key function holders:

- integrity;
- soundness of judgement;
- financial soundness; and
- sufficient knowledge, experience and professional qualifications.

Sufficient diversity between key functions holders is required so that they are able to govern and operate the Group effectively. Key function holders, as a collective, are required to have sufficient knowledge, experience and qualifications to ensure that they run the Group professionally and in accordance with the applicable regulations.

The collective knowledge and expertise of the individuals holding a key function is such that the Group can demonstrate:

- there is a professional management team which ensures that the Group is run in accordance with all relevant legal and regulatory requirements;
- there is an understanding of the insurance products and processes and the market in which it operates;
- there is an understanding of the finance and actuarial functions including the financing, investments and financial markets, actuarial principles and reinsurance;
- there is an understanding of administrative structures and processes within the organisation including internal controls, information technology and risk management;
- there is an understanding of financial accounting and reporting;
- there is an understanding of any outsourcing arrangements and their control; and
- overall, the collective knowledge should be of an adequate level and consist substantially of individuals each with several years of experience in management of an insurer.

The fitness and propriety of individuals is an ongoing requirement, therefore the relevant regulator(s) are notified of any changes regarding the individuals who effectively run the Companies within the Group or are responsible for a key function. If there are changes made to personnel then their fitness and propriety will need to be assessed. If during an assessment of fitness and propriety it is found that an individual no longer fulfils the requirement set out then the relevant regulator(s) will be advised.

The Group has a number of processes in place to ensure ongoing fitness and propriety. All individuals who effectively run the organisation or are key functions holders complete a tailored induction process, aligned to their particular skill set and responsibilities, and, as with all staff, are subject to an annual performance assessment. An ongoing assessment of the Board and its Committees is completed annually and includes an overall review of the fitness and propriety of the composition of the Board and Committees, both collectively and individually.

(II) SKILLS, KNOWLEDGE AND EXPERTISE OF THE BOARD AND PERSONS IN KEY FUNCTIONS

The skills, knowledge and expertise of the Board and persons in key functions are included in Appendix II.

B4: RISK MANAGEMENT AND SOLVENCY SELF ASSESSMENT

The risk management system comprises of its governance structures, risk strategy, policies and procedures, which together encapsulate the way it identifies, analyses, controls, manages and monitors its risk profile and exposures on a continuous basis. LICL's risk management system and risk strategy is aligned with those of the Group.

(I) PROCESSES AND PROCEDURES

Risk Strategy

The primary objective of the Group's ERM framework is to ensure that the capital resources held are matched to the risk profile of the Group and that the balance between risk and reward is considered as part of all key business decisions.

Our overall Group strategic goal remains to maximize risk-adjusted return for our shareholders across the cycle. The Group aims to target a maximum modelled exposure of 25% of its capital to a peak zone loss, be this to a 1 in 100 wind event or a 1 in 250 quake event. In order to achieve these objectives, we employ an effective risk management framework. All of the Group's strategic ERM objectives have a common aim of supporting its business and capital strategy.

Within this context, the primary strategic ERM objectives are to:

- ensure that all key decisions and risk taking will be undertaken within boundaries that are defined clearly and aligned to the strategic objectives and risk profile of the Group and the Company; and
- promote informed risk taking that considers the risk reward equation in all major decisions with a view to optimising risk adjusted change in FCBVS.

Other key objectives are to:

- encourage a culture of risk challenge, questioning and understanding including the use of stress, reverse stress and scenario testing to verify assumptions and loss scenarios;
- quantify and assign risk values to the key risks (within each risk category) to which it is exposed and maintain a risk register to track and manage such risks; and
- ensure that the Group's capital resources are aligned with risk levels and comply with relevant regulatory capital requirements.

Risk Appetite

The Group Board and sub-committees set the annual rolling three year strategy, from which the risk appetite and risk profile are determined. The risk appetites correspond to the level of exposure the Group and its subsidiary undertakings are willing to accept within each risk category. These risk appetites are expressed through detailed risk tolerances at both a Group and Company level. Risk tolerances represent the maximum amount of capital, generally on a modelled basis, that the Group and its subsidiary undertakings are prepared to expose to certain risks.

All risk appetites and tolerances are subject to at least an annual review and consideration by the respective Boards of Directors. The LHL and individual Boards of Directors review actual risk levels versus tolerances, emerging risks and any lessons learned from risk events at least quarterly. In addition, on at least a monthly basis for PMLs and a quarterly basis for RDSs, management reviews modelled potential losses against risk tolerance and ensure that risk levels are managed in accordance with them.

Risk Universe

The risk universe is the starting point for the identification and categorisation of all risk exposures within the Group and its subsidiary undertakings. The Group's risk universe articulates the range of risks to which it could potentially be exposed, setting the context for the risk management policy framework and the monitoring, quantification and management of risk.

The risk universe categorises risks into three broad classes: intrinsic risk, operational risk and other risk. These risks for the Group and the Company are described in more detail on pages 30 to 41 of the LHL Annual Report and Accounts for 31 December 2020, available on the Group's website here: Investors – Lancashire Group.

The categorisation in the risk universe is supported by a more granular risk taxonomy demonstrating the linkage between the risk universe, the capital models, the detailed risk register, and key monitoring and reporting processes. The risk universe and taxonomy are key to enabling the risk profile across different entities to be aggregated and reported coherently both internally and externally.

Risk Policy Framework

The Group's risk policy framework formalises its approach to the management of its more material risk categories in a way that can easily be communicated to both internal and external stakeholders.

The policies build upon the high level detail in the risk universe and the detailed controls documented in the risk register. For each category, the policies set out the key underlying sources of risk, the processes in place across the first and second line of defence to prevent and/or detect the risk and the approach to risk transfer or mitigation.

The framework documentation is designed to be proportionate to the scale and complexity of the Group's business and organisational structure and is published on the Group's SharePoint platform.

B. GOVERNANCE STRUCTURE CONTINUED

ERM Processes and Reporting Procedures
The ERM processes are effected by the Group's and subsidiary companies' Boards of Directors, management and other personnel, applied in strategy setting and across the Group. They are designed to identify potential events that may affect the Group and subsidiary companies, and manage risks within their risk appetite, to provide reasonable assurance regarding the achievement of the Group's objectives. The processes are centred on the Group's risk policies and integrated in the ERM and ORSA procedure documents which explain the day-to-day activities employed in the Group to manage risks. The Group's overall system of risk governance relies on a number of key committees and management processes to bring together effective reports on the management of risk for each management team and board within the Group.

The following annual, quarterly and management processes are in place:

Annual Processes
Group Strategy – The annual strategy is approved by the Group Board of Directors and encompasses a three year forward view, updated and refreshed each year initially at the Group level in the context of the anticipated competitive environment and other considerations. The strategic plan is implemented formally through business plans at the Group and subsidiary levels which explicitly refer to it, and informally through regular interactions of management. LICL prepares an annual strategy, which closely mirrors the Group strategy but reflects any specific local strategic drivers.

Business Planning Process – The Group business plan approved by the Group Board of Directors is underpinned by specific entity plans and projections to allow appropriate consideration and approval by the subsidiary boards. The plan establishes the risk return objectives, risk and capital appetite and capital management plan for the coming year, considering a range of potential business scenarios supported by the use of stress testing to test forecast financial stability and capital adequacy and inform capital and liquidity management strategies and associated contingency plans.

The process involves extensive input from the underwriting, finance, risk management and actuarial functions with the review of the capital requirements and the risk profile of the proposed plan being undertaken by the RRC.

Regulatory Capital Submissions – The process is initiated by the regulatory reporting and finance teams in line with regulatory requirements as applying to the Group and subsidiary undertakings. A BSCR is calculated annually for the Group and Company (and more frequently in the event of a material change in the business's risk profile) in accordance with regulatory reporting requirements. The BSCR is prepared on an EBS basis.

Annual ORSA/CISSA Process and Report – On an annual basis the Group CRO performs an assessment of the Group's and LICL's overall solvency needs and produces a report detailing their risk profiles and the capital and other means needed to address these risks (the ORSA report). In addition the ORSA provides a forward looking analysis of risk and the associated capital requirement. Stress and scenario tests are performed on both the Group required regulatory capital and business plan and the results included within the ORSA. The Group ORSA is reviewed, challenged and approved by the LHL Board of Directors and the LICL Board reviews, challenges and approves the LICL CISSA report.

Quarterly Processes
Quarterly ORSA report – A quarterly ORSA report is prepared for the LHL Board and subsidiary boards by the Group CRO. This draws upon the bi-weekly RRC reviews and exposure modelling updates and covers the following:

- capital resource adequacy;
- risk levels versus risk tolerances;
- summary of risk groups and their impact upon capital requirements;
- volatility and overall risk levels compared to strategy;
- risk register updates;
- rating agency update (applicable for the Group only); and
- emerging risk issues.

The quarterly ORSA report is reviewed and challenged, as appropriate by the Board; formal approval is only requested when decision items are included in the paper, for example, annual review and approval of risk appetite statements.

Group CFO Capital Management Review – A quarterly capital management paper is prepared for the Group Board of Directors by the Group CFO who reports its conclusion and recommendations to the Board. It draws upon the rating agency and capital management procedure and on-going regulatory capital monitoring process and covers the following:

- capital position, review and projections;
- capital management recommendations;
- analysis of capital measures;
- analysis of capital tolerances;
- rating agency and shareholder views;
- projections and impact on change in FCBVS; and
- headroom strategy.

B. GOVERNANCE STRUCTURE CONTINUED

The LICL CFO prepares a quarterly capital adequacy report for the Board which highlights LICL's capital position as compared to the BSCR.

Group Board Underwriting & Underwriting Risk Committee Review – The Underwriting and Underwriting Risk Committee considers insurance risk levels and strategy in detail on a quarterly basis. The Committee:

- formulates the Group underwriting strategy;
- oversees the development of and adherence to underwriting guidelines by operating company CUOs;
- reviews underwriting performance and significant changes in underwriting rules and policy;
- establishes, reviews and maintains strict underwriting criteria and limits; and
- monitors underwriting risk and its consistency with the Group's risk profile and risk appetite.

Group Board Investment Committee Review – The Investment Committee reviews the investment portfolio and risk levels in detail on a quarterly basis. The Committee:

- recommends investment strategies, guidelines and policies for the Board to approve annually;
- recommends and sets risk asset definitions and risk tolerance levels;
- recommends to the relevant Boards the appointment of investment managers to manage the Group's investments;
- monitors the performance of investment strategies within the risk framework; and
- establishes and monitors compliance with investment operating guidelines relating to the custody of investments and the related internal controls.

Management Committee Reviews

RRC Review – The RRC is a Group committee that includes the Group CEO and members from the finance team, capital management, actuarial, underwriting and operations functions. The Group CRO attends the meetings and reports on the RRC's activities to the Group and subsidiary undertaking Boards of Directors. The RRC meets on approximately a bi-weekly basis covering a range of ORSA related topics set out in their terms of reference and annual timetable, both of which are reviewed on an annual basis to ensure that they best meet the Group's needs in a changing internal and external environment.

The RRC considers the core insurance risk profile against Group and subsidiary undertaking risk tolerances on a monthly basis for elemental PML modelling and quarterly non-elemental RDS analysis. The RRC has a key role in terms of oversight of the capital models, evaluating the appropriateness of and any proposed major changes to its design, implementation and operation and ensuring that it remains an effective tool to support decision making.

IRRC Review – The Group committee meets quarterly to ensure that the Group's strategies and tactical investment actions are consistent with the Group's investment risk preference, appetite and risk and return objectives. The committee also reviews new products and potential correlations with insurance risk. The committee further ensures the risk tolerances are incorporated into the overall risk appetite framework. On a quarterly basis, the committee's reports and conclusions are reviewed by the RRC.

Reserve Committee Review – The committee meets formally at least quarterly to review and approve all significant individual claim reserves and any large additional case reserves. Although a single meeting is held, the committee consists of LUK members and LICL members who can only make decisions in respect of their own companies.

Group Reinsurance Security Committee (RSC) Review – The committee is responsible for the monitoring and approving of individual reinsurers within the framework of overall limits and methodologies maintained by the RRC. Whilst the committee meets formally on a quarterly basis approvals may be made more frequently via email as business needs require.

On-going Management Processes

Aggregation, Monitoring and Reporting – Underwriting risk is by far the greatest driver of the Group's and LICL's overall risk profile and capital requirements and this is reflected in the scope, granularity and frequency of monitoring of both elemental and non-elemental catastrophe risk exposures.

Elemental exposures are considered on the basis of PMLs at a range of return periods, whereas, non-elemental exposures are considered in terms of deterministic RDSs representing hypothetical extreme, but nonetheless credible, potential loss scenarios.

The RRC reviews the PMLs on a monthly basis and RDSs on a quarterly basis. In addition, they are reported to the Group and LICL Boards through the quarterly Group CRO reporting. Any projected or actual breach of limits requires immediate action by management, the risk owner being required to immediately contact the Group CRO with an explanation and mitigating plan.

Actual breaches require a mitigating plan approved by the Group CRO and the CEO and are reported to Group management, the RRC and appropriate Board(s).

Group Rating Agency and Capital Management – The significance of this area is such that it is covered by a specific rating agency policy, associated procedure and supporting processes forming part of the overall system of governance. These processes explain how the Group and LICL monitor available capital headroom given the current book of business, the projected book of business and various stress test scenarios.

Regulatory Capital Monitoring – Both the Group and the Company are subject to regulatory requirements in respect to BMA regulation. The Company maintains and operates a series of processes to ensure and evidence continued compliance with its regulatory requirements and resultant changes in regulatory and supervisory arrangements.

Operational Risk Management – The Group maintains risk registers encompassing assessments of all material operational risks and the controls designed to prevent, mitigate or detect them at both Group and subsidiary undertaking levels.

On a quarterly basis, individual risk owners are required to formally reassess and reaffirm the full scope of their controls and semi-annually the gross and net risk scores for which they are responsible are reassessed. The self-assessment is recorded on the Group's Governance Portal and is subject to Group CRO review, challenge and approval. In the intervening quarters, the Group CRO meets with all risk owners to have a detailed discussion on their risks and reaffirm the gross and net risk scores. Detailed follow up is performed on a sample of controls each quarter to verify the affirmations made by the control operators.

A qualitative assessment of key risks and any material changes is reported quarterly by the Group CRO to Board(s) supported by an extract from the register showing key risks and their scores.

Emerging Risk Management – The Group identifies and monitors emerging risks through a range of channels including but not limited to semi-annual Group CRO reviews with risk owners, Group CRO attendance at key committees' meetings, a rolling review as part of the RRC annual timetable, output from the Group Emerging Risk Forum, the climate change working group and the review of external inputs.

An emerging risk register is maintained by the Group CRO and emerging risks are a standing item in the Group CRO's quarterly ORSA report to the Board(s) ensuring that they remain under consideration at Board level.

Stress and Scenario Testing – The Group conducts sensitivity, stress (standard and reverse) and scenario testing on both a scheduled and ad-hoc basis as part of a number of underlying components in the ERM and ORSA framework.

(II) ORGANISATIONAL STRUCTURE AND DECISION-MAKING PROCESSES

The governance and the implementation of an effective risk management system within the Group is facilitated by the Group Risk Management function whose role it is to deliver ERM across all aspects of the Group and its subsidiaries. The function is headed up by the Group CRO, who reports directly to the Chairmen of the Group and subsidiary boards, and facilitates and aids the identification, evaluation, quantification, mitigation and control of risks at a Group and subsidiary level with support from the Risk Management and Actuarial functions. Facilitating and embedding of ERM and helping the Group improve its ERM practices is a major responsibility assigned to the Group CRO. The Group CRO drives the risk assessment process including maintaining risk registers and ensuring the efficacy and appropriateness of the risk management procedures and processes.

The Group CRO provides regular reports to the Group and subsidiary Boards covering, amongst other things, actual risk levels against tolerances, emerging risks and any lessons learned from risk events. The Group Board considers that a supportive ERM culture, established at the Board and embedded throughout the business, is of key importance.

The RRC, under the chairmanship of the Group CEO, is the key management tool for monitoring and challenging the assessment of risk on a continual basis. The RRC agenda is reviewed each year to ensure its activities remain appropriate and aligned with the business cycle.

Chief Risk Officer

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

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

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

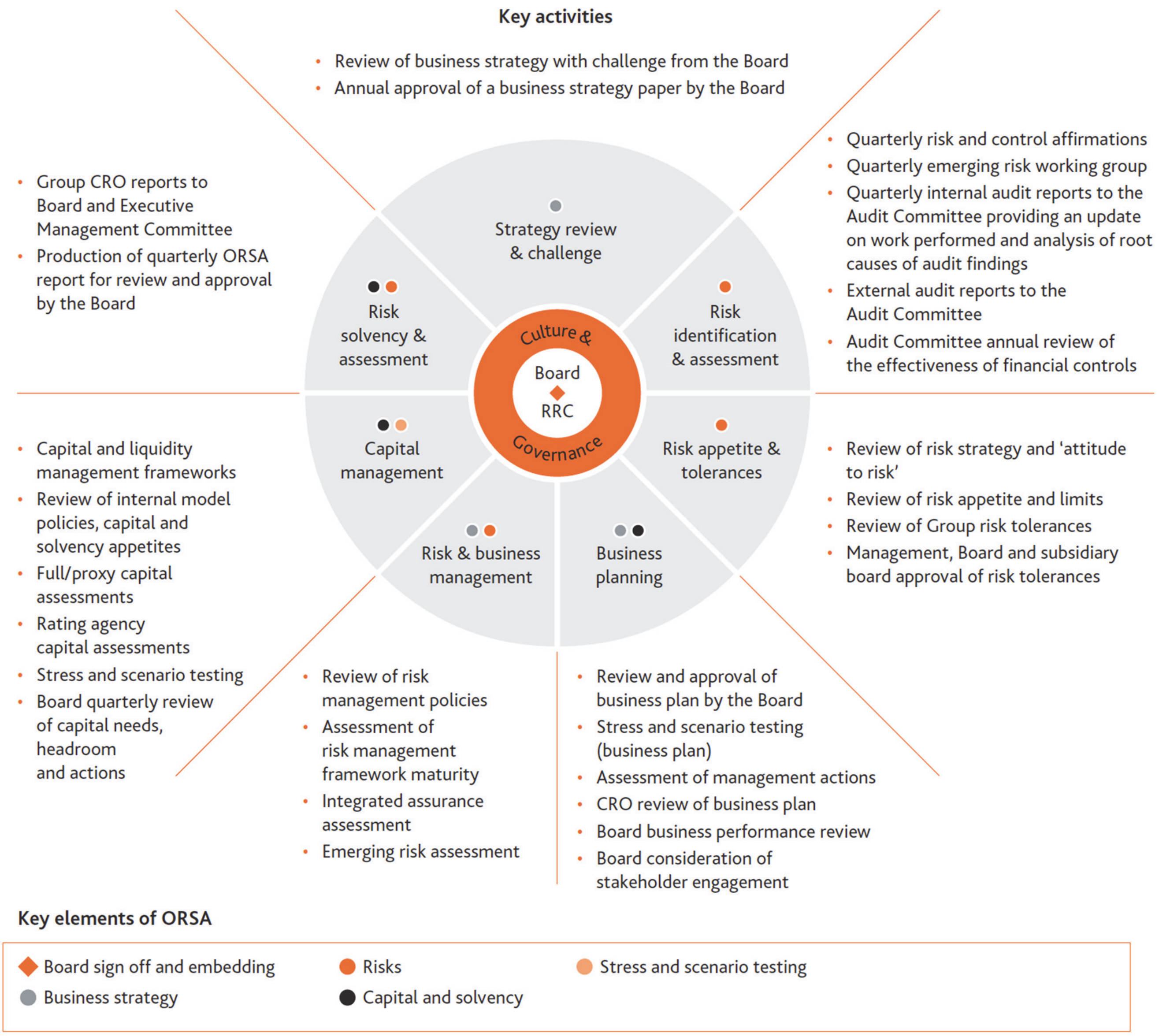
B. GOVERNANCE STRUCTURE CONTINUED

(III) ORSA PROCESS

The ORSA process is integrated into the overall ERM framework, and is embedded in the entirety of the Group's risk management processes and procedures outlined above, which seek to identify, assess, manage, monitor and report the risk exposures of the business and its strategy. It also encompasses activities used to determine the adequacy of the capital necessary to ensure that the overall solvency needs of the business are met at all times and involves a continuous current year risk profile monitoring and reporting as well as forward looking forecasting of risk profile.

The diagram below illustrates how the various parts of the ERM framework come together to form the ORSA process.

ERM & ORSA



B. GOVERNANCE STRUCTURE CONTINUED

ORSA Report
Bermuda regulated Groups and insurers are required to prepare an ORSA report (referred to by the BMA as the GSSA for Group reporting, and CISSA for LICL reporting). The Group ORSA report is a material output of the ongoing ORSA and ERM processes. It reports on the dynamic elements of the ORSA process, focussing on the moving components of the Group's solvency and risk profile to enable management to make informed decisions. A separate CISSA report is also completed for LICL.

In summary, current year monitoring processes feed into the Group CRO's quarterly ORSA report to the Board; whilst the forward looking forecasting process feeds into the annual ORSA report. In both instances the reports are used to support decision making and are standing agenda items for the Boards and other committees.

A full out-of-cycle ORSA report would also be produced on an ad-hoc basis as required following a planned or unplanned material change in the risk or solvency profile of the business. The Group and its subsidiaries will report the results of the ORSA process to its respective supervisors. In an out-of-cycle ORSA, the decision to conduct such an ORSA will be notified to the supervisor in a timely fashion upon the occurrence of the trigger event and a date agreed for reporting. Trigger events will include, but not necessarily be limited to, planned or unplanned risk or solvency profile changes such that:

- the Group or Company breaches or would expect to breach its capital and solvency tolerances; and
- the risk profile of the business changes or is expected to change in such a way that the methodologies used to calculate its capital requirements are no longer deemed reliable for the projected risk profile.

In the event of an out-of-cycle ORSA, the results will be reported to the supervisor without undue delay following review and approval by the Board and in conjunction with the compliance function.

Solvency needs and risk profile
The Group considers a wide range of measures when establishing the appropriate level of capital at Group and individual entity level including its internal measures of capital requirements, used for reviewing risk and solvency profile across entities, applicable regulatory minima and external rating agency capital requirements.

Risk tolerances are set at a level that aims to prevent the Group and subsidiaries incurring losses that would impair their ability to operate.

The Group's key capital measure is currently its A.M. Best rating. The Group's maintenance of an A.M. Best rating of a minimum of A- remains the key determinant of its ability to attract and retain business in the markets in which it operates. In 2020, the Group maintained its A rating.

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

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

(IV) BOARD OVERSIGHT, REVIEW AND APPROVAL
On an ongoing basis, the Board reviews the risk profile via the quarterly ORSA report produced by the Group CRO for the Board. The quarterly ORSA report covers all material risk exposures within each category of risk as well as commenting on the solvency capital profile. The annual ORSA report is also reviewed and approved by the Board prior to regulatory submission.

B5: INTERNAL CONTROLS

(I) INTERNAL CONTROL SYSTEM
The LHL Board is responsible for ensuring that an adequate and effective system of internal control is established and maintained throughout the Group. The subsidiary Boards are responsible for approving and periodically reviewing the overall business strategies and significant policies as well as the organisational structure and internal control strategy of the respective companies. The Boards provide direction, guidance and suitable prudential oversight, ensuring that the companies are appropriately and effectively managed, controlled and in compliance with laws and regulations. The Boards are supported in discharging these responsibilities by the relevant company secretarial department and with advice and guidance from the legal and compliance function, which is led by the Group General Counsel. The Boards are responsible for the supervision and evaluation of the respective company's performance, including management.

B. GOVERNANCE STRUCTURE CONTINUED

Internal control can be defined as a continuous set of processes carried out by the Board of Directors, management and all personnel, designed to provide reasonable assurance of:

- effectiveness and efficiency of operations;
- reliability of financial and non-financial information;
- adequate control of risks;
- prudent approach to business; and
- compliance with laws and regulation, and internal policies and procedures.

The key components of the Group's internal control system are:

- the affirmation process and associated detailed control testing;
- the internal audit function; and
- the Board and its committees (both on a Group and subsidiary level).

The Group maintains an effective internal control system comprising efficient control activities applied across all key areas of business operations.

The key control activities within the Group and its subsidiaries include:

- approval processes (including peer review);
- authorisations;
- verifications;
- reconciliations;
- management reviews;
- appropriate measurements applicable to each business area;
- monitoring compliance with agreed exposure limits and operating principles/instructions, and
- follow-up on any instances of non-compliance.

The control activities are proportionate to the risks coming from the processes and they ensure that any potential conflicts of interest are identified and managed appropriately.

Control Monitoring
Through its monitoring of the control framework the Group seeks to have a continual cycle of review and improvement to ensure that the control framework remains appropriate to the needs of the companies and provides management with assurance of the effectiveness of the controls framework and that procedures are in place to detect deficiencies.

Each control is allocated to an individual control owner. The risk register identifies the named control owners who are responsible for the effective performance of each of the identified controls. The actual operation of the control can be delegated by the control owner to a control operator, notwithstanding the control owner remains responsible for the suitability and operation of the control.

On a quarterly basis all control owners/operators affirm the effectiveness and appropriateness of their assigned controls. Results are recorded on the Lancashire Governance Portal in a process that is facilitated by the Group Risk Management function and the Group CRO. All control assessments are then reviewed and approved by the Group CRO who reports any material changes to the Boards on a quarterly basis.

(II) COMPLIANCE FUNCTION

The Group is committed to ensuring compliance with all applicable laws and regulations and has no tolerance for breaches or a failure to adhere to prudential regulatory standards as well as the standards of conduct expected of it in those markets and territories in which it operates.

The Group has implemented policies and procedures to document the control environment in place including how it mitigates regulatory risk. The Group recognises that compliance is the responsibility of all staff and directors, including non-executive directors. Ensuring the implementation of a compliance policy throughout the firm is the responsibility of the Group and subsidiary undertaking Boards. On a day-to-day basis executive management are responsible for ensuring that the policy remains appropriate and effective.

All members of the compliance function have the appropriate experience and expertise relevant to their individual roles, providing a mix and balance of skills, so that they collectively can fulfil their duties.

The Group's compliance function identifies, assesses, monitors and reports on ongoing compliance risk exposure, including the tracking of changes in the environment that could affect the compliance and regulatory risk and the monitoring of the appropriateness of the Group's and LICL's compliance.

B6: INTERNAL AUDIT FUNCTION

The Head of Internal Audit oversees internal audit and assists executive management and the Audit Committee of the Board of Directors in discharging their responsibilities by furnishing them with analyses, advice and recommendations concerning activities reviewed and by promoting effective and efficient controls and pursuing corrective action on significant issues.

Annually, Internal Audit submits to the Audit Committee a detailed audit plan outlining the proposed audit methodology, work schedule and budget for the following year. The audit work schedule is developed based on a prioritisation of the audit universe using a risk-based methodology. Any significant deviation from the formally approved work schedule is communicated to senior management and the Audit Committee through periodic activity reports. The Head of Internal Audit also provides reports to the LICL Board in respect to internal audit activities relevant to the Company.

A written report is prepared and issued by Internal Audit following the conclusion of each audit and is distributed as appropriate. A summary audit report is provided to the Audit Committee. The audit reports include the auditee's agreed actions to be taken in respect of each specific finding. Reports must outline clearly any instances where Internal Audit and the auditee are unable to formulate satisfactory agreed actions and the Audit Committee will then determine the appropriate actions.

Management's response should include a timetable for anticipated completion of action to be taken and an explanation for any recommendations not addressed.

Management will be responsible for appropriate follow-up on those audit findings and recommendations. All significant findings will remain open in Internal Audit's issue tracking software until cleared by Internal Audit or the Audit Committee.

Internal Audit's roles and responsibilities are clearly defined through the Internal Audit Charter, available on the Group's website here: Internal Audit Charter. This states that all internal audit activities shall remain free of influence by any element in the organisation, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of an independent and objective mental attitude necessary in rendering reports.

The Internal Audit function maintains its independence and objectivity from the activities it reviews by the Head of Internal Audit reporting directly to the Group Audit Committee and subsidiary Boards. In addition, the Group CRO has input to the scope of each audit and receives a copy of each internal audit report. This integration of internal audit and ERM into the business helps facilitate the Group's protection of its assets and reputation and maintain Internal Audit's objectivity.

The Internal Audit team govern themselves by adherence to The Institute of Internal Auditors' (IIA) International Professional Practice Framework ("IPPF").

B7: ACTUARIAL FUNCTION

The actuarial function consists of individuals with the appropriate skill sets and knowledge of financial and insurance mathematics commensurate with the nature, scale and complexity of the Group's business. All members of the actuarial function are either fully qualified actuaries or working towards qualification. As such, experience and skills are maintained through continued professional development and education and adherence to the relevant professional body's code of conduct, standards or practice.

In order to demonstrate independence between performing and reviewing work Lancashire engaged external actuaries during the year to:

- conduct independent reviews of the Group's and LICL's claims reserves on an IFRS basis on a six monthly basis;
- perform the duties of the Approved Actuary under the BMA's regime and are responsible for providing an opinion on the adequacy of the EBS technical provisions to the BMA; and
- provide an opinion on the adequacy of the reserves held in the Company's U.S. MBRT.

The Group considers that the above internal and external resource has sufficient knowledge, skills and experience to address the requirements of the actuarial function.

B8: OUTSOURCING

The key objectives of the Group's outsourcing policy are:

- to ensure that the Group and subsidiary undertakings receive optimal value for money whilst also understanding and controlling the risks involved in the engagement of third party providers or outsourcing services; and
- to ensure compliance with the relevant regulatory requirements in which the Group's entities operate in respect of any outsourcing undertaken.

The Group and LICL remains fully responsible for discharging all of its obligations under the rules and other laws, regulations and administrative provisions, and therefore cannot contract out its regulatory obligations and takes care to supervise the discharge of any outsourced functions and/or activities. None of the Group's or Company's key or important functions are outsourced; however external service providers are used in certain instances to provide expertise, skills or products that are not available internally. In all instances key and important functions are managed and supervised by employees, who retain oversight and responsibility for the functions. With the exception of the underwriting services agreement between LCM, KRL and KHL, there are no material intra-group outsourcing arrangements in place within the Group.

Areas in which external service providers are utilised by the Group's key and/or important functions are as follows:

Internal Audit
The Group's Internal Audit function uses various "co-source" service providers to provide assistance with audits that are particularly technical or specialist in nature, for example IT, actuarial or tax related matters. In all instances the co-source audit provision is managed by the Head of Internal Audit and the results of the audits are reported to management and the Group Audit Committee using reporting and scoring consistent with the internally sourced internal audits.

Actuarial Function
As noted above, during 2020 the Group's actuarial function has used external actuaries to provide independent support around aspects of the IFRS technical provision process. The independent actuary also acts as "Approved Actuary" for the Company and provides the required regulatory opinion on the Company's reserves. This support is not considered to constitute outsourcing of the role or tasks of the Actuarial Function; the responsibility for these is maintained internally.

Finance and Investment Management
The Group's principal expertise lies in underwriting so we use the services of internationally recognised investment managers, custodians and investment accountants who are experts in their respective fields to provide assistance with the day-to-day management of the Group's investment portfolios and accounting and risk reporting thereof. The use of such services also provides us with access to extensive and high quality research into investments and capital markets that would be inefficient to derive internally. The responsibility for managing the outsourcing of the relationship with these third party service providers lies with the Group Chief Investment Officer.

Investment guidelines are established by the Investment Committee of the Group's Board of Directors; these then determine parameters within which the Group's investment managers must operate. Compliance with the investment guidelines is monitored by the internal investment management team on a monthly basis. Further details regarding the Group's investment guidelines are available in the Investment Risk section of LHL's 31 December 2020 consolidated financial statements, from page 139 of the 2020 Annual Report and Accounts: Investors – Lancashire Group.

The Group has entered into an outsourcing arrangement to support it in the processing and matching of some of its technical cash items and the processing of related endorsements and declarations and also credit control. The Group holds weekly review meetings with the provider and monthly strategy meetings, with a member of senior management in attendance, and furthermore receives regular detailed reports on progress.

IT
The IT function uses service providers to provide business continuity services off-site in the UK and Bermuda. Third parties, based in the UK, are also used to provide data back-up services and email scanning and archiving services. Additionally, third parties are used by the Group to advise on and test matters relating to the Group's IT security arrangements. The use of external providers for such services is considered best practice for IT continuity risk management.

B9: OTHER MATERIAL INFORMATION

Not applicable – all material information regarding the Governance Structure has been described in B1-B8 above.

C. Risk profile

The Group is exposed to risks from several sources. These include underwriting risk, market risk, liquidity risk, credit risk, operational risk and strategic risk. The primary risk to the Group is insurance underwriting risk. There have been no material changes to the Group's material risks or the measures used to assess these risks over the 2020 reporting period.

C1: UNDERWRITING RISK

Underwriting risk continues to dominate our risk profile. It has the highest impact on the regulatory capital requirements of the BMA BSCR as well as being the primary driver for our capital decisions.

The Group and Company underwrites worldwide, predominantly short-tail, insurance and reinsurance contracts that transfer insurance risk, including risks exposed to both natural and man-made catastrophes. The exposure in connection with insurance contracts is, in the event of insured losses, whether premiums will be sufficient to cover the loss payments and expenses.

Insurance risk is considered at an individual contract level, at a segment level, a geographic level and at an aggregate portfolio level. This ensures that careful risk selection, limits on concentration and appropriate portfolio diversification are accomplished.

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

The Group and Company's exposures to certain peak zone elemental losses are shown below. Net loss estimates are before income tax and net of reinstatement premiums and outwards reinsurance on a first occurrence return period basis.

LHL		100 year return period estimated net loss	250 year return period estimated net loss	100 year return period estimated net loss	250 year return period estimated net loss
Zones	Perils	2020 $m	2020 $m	2019 $m	2019 $m
Gulf of Mexico[1]	Hurricane	166.5	323.0	139.7	311.0
California	Earthquake	111.9	151.2	85.2	161.1
Non-Gulf of Mexico – U.S.	Hurricane	108.9	361.2	72.8	307.8
Pan-European	Windstorm	71.8	85.7	59.8	88.1
Japan	Earthquake	63.7	105.9	51.3	165.7
Japan	Typhoon	60.4	71.7	26.8	36.4
Pacific northwest	Earthquake	20.1	85.0	12.7	56.1

LICL (excl CCL 1998 quota share)		100 year return period estimated net loss	250 year return period estimated net loss	100 year return period estimated net loss	250 year return period estimated net loss
Zones	Perils	2020 $m	2020 $m	2019 $m	2019 $m
Gulf of Mexico[1]	Hurricane	91.0	215.8	68.9	187.9
California	Earthquake	55.4	81.6	34.6	93.9
Non-Gulf of Mexico – U.S.	Hurricane	61.3	284.2	38.9	214.6
Pan-European	Windstorm	48.6	59.3	36.5	52.1
Japan	Earthquake	36.6	65.7	26.2	123.2
Japan	Typhoon	39.3	48.8	11.7	18.2
Pacific North West	Earthquake	5.9	40.6	1.7	23.4

(1) Landing hurricane from Florida to Texas.

There can be no guarantee that modelled assumptions and techniques deployed in calculating these figures are accurate. There could also be an unmodelled loss which exceeds these figures. In addition, the models contain loss scenarios which could cause a larger loss to capital than the modelled expectation from the above return periods.

C. RISK PROFILE CONTINUED

The Group maintains economic capital models at the LICL, LUK and syndicate levels. These models are primarily focused on insurance risks, however, they are used to model other risks including market, credit and operational risks. The syndicate models are vetted by Lloyd's as part of its own capital and solvency regulations. Within these economic capital models, insurance risk accounts for the majority of the allocated risk capital, so this is the principal area where the Group and the Company stringently applies controls and reviews. For example, the Group places a large number of controls around monitoring risk levels across the business with the level of insurance risk tolerance per peril set by the respective Boards of Directors at both LHL and entity level.

The RRC reviews the PML's on a monthly basis and RDS's on a quarterly basis. They are also reported to the Group, LICL and LUK Boards through the quarterly Group CRO reporting. Any projected or actual breach of limits requires immediate action by management, with the risk owner being required to immediately contact the Group CRO with an explanation and mitigating plan. Actual breaches require a mitigating plan, which must be approved by the Group CRO and the Group CEO and are reported to Group management, the RRC and appropriate Board(s). There were no breaches to underwriting risk tolerance in 2020.

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

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

Monitoring
The continued effectiveness of the risk mitigation techniques is monitored by the LHL and LICL Boards through their review of the quarterly ORSA reports and by management through the bi-weekly RRC meetings.

Use of Special Purpose Vehicles
Although the majority of the Group's reinsurance arrangements are with highly rated counterparties a small number of special purpose vehicles were utilised for outwards reinsurance protection during 2020. These accounted for 5.8% (31 December 2019: 4.1%) of the Group's reinsurance cover purchases. The fully funded principle is met as all the reinsurance protections were fully collateralized up to the limit of the relevant contracts. The collateral can only be released post expiry of the contract with our agreement.

C2: MARKET RISK

Market risk relates to the uncertainty in the level or volatility of the market prices of financial instruments. Movements in investments resulting from changes in interest and inflation rates and currency exchange rates, amongst other factors, may lead to an adverse impact on the value of the investment portfolio. Investment guidelines are established by the Investment Committee of the Board of Directors to manage this risk. Investment guidelines set parameters within which the external investment managers must operate. Important parameters include guidelines on permissible asset classes, duration ranges, credit quality, currency, maturity, sectors, geographical, sovereign and issuer exposures. Compliance with guidelines is monitored on a monthly basis. Any adjustments to the investment guidelines are approved by the Group Investment Committee and the LICL Board of Directors.

C. RISK PROFILE CONTINUED

Prudent person principle
The BMA's Insurance Code of Conduct requires companies to invest assets in accordance with the 'prudent person principle'. The broad requirements relevant to the Group and Company are as follows:

- investment should be in assets whose risks can be properly identified, measured, monitored, managed, controlled, reported and taken into account when calculating the solvency capital requirement;
- investment should be carried out in such a way as to ensure the security, quality, liquidity and profitability of the portfolio as a whole;
- assets held to cover technical provisions should match the nature and duration of the insurance and reinsurance liabilities;
- conflicts of interest should be managed to ensure that the investment is made in the best interest of policy-holders;
- the use of derivatives should be restricted to reduction of risks or for efficient portfolio management;
- assets not traded in regulated financial markets should be kept to a minimum;
- the portfolio should be diversified in terms of asset class, issuer and geographical location; and
- there should not be excessive risk concentration in relation to an issuer or issuer group.

The investment portfolio includes highly rated securities, across a number of sectors and a number of types of fixed maturity securities, and has a high proportion of government backed securities. The Group also has a diversified low volatility multi-strategy portfolio of hedge funds and private debt funds. Strict guidelines govern investment policy and the portfolio is monitored closely in terms of security, quality, liquidity, profitability and duration.

Risk concentration is closely monitored to ensure that there is no excessive concentration with any one issuer or issuer group, although there is a degree of concentration with the U.S. government and agencies as well as the Group's investment in KHL. Total exposure to U.S. government treasury bonds was $384.1 million at 31 December 2020 (31 December 2019: $328.9 million), and comprises the main material exposure to a single issuer. KHL, given its unrated nature and not immaterial contribution to the Group's assets, also triggers a concentration risk charge. Concentration risk is not a material component of the Group's BSCR (2.7%) (31 December 2019: 5.7%) or the Company's (3.8%) (31 December 2019: <1%) BSCR charge.

Assets are held to match the duration of liabilities as far as possible. Given that the majority of liabilities are denominated in U.S. dollars there is naturally a significant amount of U.S. denominated assets.

Performance and accounting reports are received for all investments and a summary report is prepared for management, the Group Investment Committee and the LICL Board.

Mitigation
Our investment risk is mitigated through the following:

- investment strategy: our strategy is that investment income is not expected to be a significant driver of our returns. Our primary focus remains on underwriting as the engine of profits. Investment strategy, including investment risk tolerances, is approved annually and monitored on a quarterly basis by the Investment Committee and Board. A detailed strategic asset allocation study is performed biannually;
- investment guidelines: within the investment guidelines are subsets of guidelines for the portion of funds required to meet near-term obligations and cash flow needs following an extreme event. These guidelines add a further degree of requirements, including fewer allowable asset classes, higher credit quality, shorter duration and higher liquidity;
- investment Risk and Return Committee: the IRRC meets quarterly to ensure that the strategic and tactical investment actions are consistent with investment risk preferences, appetite, risk and return objectives and tolerances. The IRRC also helps further develop the risk tolerances to be incorporated in the ERM framework;
- modelling: periods of significant stress are modelled in order to better understand the investment portfolio's risks and exposures. The scenarios represent what could, and most likely will occur (albeit not in the exact form of the securities, which are based on historic periods of volatility);
- diversification: our portfolio is diversified across a number of sectors, geographical areas and types of investment; and
- external advisers: our principal expertise lies in underwriting so we use the services of internationally recognised investment managers who are experts in their fields. The Group's principal investment managers are signatories to the Principles for Responsible Investment.

Monitoring
The continued effectiveness of the risk mitigation techniques is monitored by the Investment Committee and by the Board through their review of the quarterly ORSA report and the quarterly management IRRC meetings.

We use a VaR metric as a risk appetite measure to monitor exposure within the investment portfolio. Following the onset of the COVID-19 pandemic, investment market volatility has been very high and as a result during 2020 the Investment Committee reviewed the appropriateness of the existing VaR metric. As a result of the review the LHL Board approved a change to the risk tolerance such that short-term spikes in volatility don't necessarily result in the need to take immediate corrective action that would result in unnecessary portfolio losses.

C3: CURRENCY RISK

The Group underwrites from two locations, Bermuda and London, although risks are assumed on a worldwide basis. Risks assumed are predominantly denominated in U.S. dollars.

The Group is exposed to currency risk to the extent its assets are denominated in different currencies to its liabilities. The Group is also exposed to non-retranslation risk on non-monetary assets such as unearned premiums and deferred acquisition costs. Exchange gains and losses can impact profit or loss.

We consider that the currency risk exposure is not sufficiently material to impact upon the resilience of our balance sheet either at a Group or entity level. The Group hedges monetary non-U.S. dollar liabilities primarily with non-U.S. dollar assets, but may also use derivatives to mitigate foreign currency exposures. The main foreign currency exposure relates to insurance obligations, cash holdings, investments, premiums receivable, dividends payable and the Group's Euro denominated subordinated loan notes.

Mitigation
Forward foreign currency contracts are used for the purposes of managing currency exposures. We monitor our currency risk exposure against set tolerances.

Monitoring
The continued effectiveness of the risk mitigation techniques is monitored by the Investment Committee and by the Board through their review of the quarterly ORSA report and the quarterly management IRRC meetings.

C4: CREDIT RISK

Credit risk is the risk that a counterparty may fail to pay, or repay, a debt or obligation. The Group and the Company is exposed to credit risk on the fixed maturity investment portfolio and derivative instruments, its inwards premiums receivable from insureds and cedants, and on any amounts recoverable from reinsurers.

The table below presents an analysis of the major exposures to counterparty credit risk, based on their rating. The table includes amounts due from policyholders and unsettled investment trades. The quality of these receivables is not graded but, based on management's historical experience, there is limited default risk associated with these amounts.

LHL	Financial assets 2020 $m	Receivables and other assets 2020 $m	Reinsurance recoverables 2020 $m	Financial assets 2019 $m	Receivables and other assets 2019 $m	Reinsurance recoverables 2019 $m
AAA	469.6	—	—	409.6	—	—
AA+, AA, AA-	650.8	0.4	4.4	471.2	—	—
A+, A, A-	591.7	28.0	229.0	509.6	133.2	200.3
BBB+, BBB, BBB-	291.8	—	3.0	204.9	—	—
Other[1]	107.1	401.9	102.3	85.2	285.9	127.2
Total	**2,111.0**	**430.3**	**338.7**	**1,680.5**	**419.1**	**327.5**

LICL	Financial assets 2020 $m	Receivables and other assets 2020 $m	Reinsurance recoverables 2020 $m	Financial assets 2019 $m	Receivables and other assets 2019 $m	Reinsurance recoverables 2019 $m
AAA	323.7	—	—	254.6	—	—
AA+, AA, AA-	493.2	—	—	340.0	—	—
A+, A, A-	363.0	4.1	52.9	337.0	—	57.9
BBB+, BBB, BBB-	214.2	—	—	146.7	—	—
Other[1]	106.6	171.2	76.1	84.9	153.3	86.8
Total	**1,500.7**	**175.3**	**129.0**	**1,163.2**	**153.3**	**144.7**

(1) Reinsurance recoveries classified as "other" are fully collateralised.

The COVID-19 pandemic has increased the risk of defaults across many industries and we continue to monitor credit risk during this time of volatility. While interest rates are at all-time lows and expected to remain low, credit spreads will remain volatile in the near term. As at 31 December 2020, the average credit quality of the fixed maturity portfolio was A+ (31 December 2019: A+).

Reinsurance Counterparties
The Group makes extensive use of both external and intra-group reinsurance as part of its overall risk return optimisation approach and accepts a degree of trade-off between mitigating underwriting risk and incurring counterparty risk. Overall, there is low exposure to credit risk as the majority of the large outwards reinsurance contracts are placed with highly rated reinsurers or are collateralised. The LHL Board of Directors has approved Group tolerance limits within which LICL operates and management has set preferences for exposures to a single external counterparty in respect of non-proportional reinsurance. All limits are monitored at the Group and individual entity level on a regular basis.

Mitigation
Credit risk on the fixed maturity portfolio is mitigated through the policy of investing in high credit quality issuers and limiting the amount of credit exposure with respect to particular ratings categories and any one issuer. Securities rated below a S&P or equivalent rating of BBB-/Baa3 may comprise no more than 15.0% of shareholders' equity. In addition, no one issuer, with the exception of the U.S. government and agency securities, other G10 government guaranteed securities (excluding Italy) and Australian sovereign debt should exceed 5.0% of shareholder's equity. The Group and the Company is therefore not exposed to any significant credit concentration risk on its investment portfolio, except for fixed maturity securities issued by the U.S. government and government agencies and other highly rated governments.

Credit risk on exchange-traded derivative instruments is mitigated by the use of clearing houses to reduce counterparty credit risk, requiring the posting of margins and settling of unrealised gains and losses daily. Credit risk on OTC derivatives is mitigated by monitoring the creditworthiness of the counterparties and by requiring collateral amounts exceeding predetermined thresholds to be posted for positions which have accrued gains.

Credit risk on inwards premiums receivable from insureds and cedants is managed by conducting business with reputable broking organisations, with whom the Group and the Company has established relationships, and by rigorous cash collection procedures. A broker approval process is in place. Binding authorities are subject to standard market controls including credit control. Credit risk from reinsurance recoverables is primarily managed by the review and approval of all reinsurer security by the RSC.

Monitoring
The continued effectiveness of the risk mitigation techniques is monitored by the Investment Committee and the Board of Directors through their review of the quarterly ORSA reports and the quarterly management IRRC meetings for credit risk in the investment portfolio, the RSC for credit risk relating to the reinsurance recoverables and the Broker Vetting Committee for credit risk relating to insurance intermediaries.

C5: LIQUIDITY RISK

Liquidity risk is the risk that cash may not be available to pay obligations when they are due without incurring an unreasonable cost. The main exposures to liquidity risk are with respect to insurance and investment activities. The Group is exposed if proceeds from financial assets are not sufficient to fund obligations arising from its insurance contracts. The Group can be exposed to daily calls on its available investment assets, principally to settle insurance claims and to fund trust accounts following a large catastrophe loss.

Exposures in relation to insurance activities are as follows:

- large catastrophic events, or multiple medium-sized events in quick succession, resulting in a requirement to pay a large value of claims within a relatively short time frame or to fund trust accounts;
- failure of insureds or cedants to meet their contractual obligations with respect to the payment of premiums in a timely manner; and
- failure of reinsurers to meet their contractual obligations with respect to the payment of claims in a timely manner.

Exposures in relation to investment activities are as follows:

- adverse market movements and/or a duration mismatch to obligations, resulting in investments being disposed of at a significant realised loss; and
- an inability to liquidate investments due to market conditions.

Subject to maintaining sufficient liquidity in aggregate across the Group's fully aligned entities, Lancashire has the ability to perform intra-group transactions in the event of temporary liquidity shortfalls at the individual entity level. This obviates incurring any costs that might result from raising entity-specific liquidity through external means.

As such, whilst the Group continues to monitor and report local liquidity levels against applicable stress events, Lancashire maintains the view that it is not necessary to cascade its formal risk tolerance and associated risk reporting requirements to the entity level and focuses on reporting overall Group liquidity to Group and entity boards. The Group has maintained liquidity in excess of this tolerance through its focus on maintaining a portfolio that is highly liquid, of overall short duration and highly creditworthy.

Mitigation
The Group manages its liquidity risks via its investment strategy to hold high quality, liquid securities, sufficient to meet its insurance liabilities and other near-term liquidity requirements. The creation of the core portfolio and core plus portfolios with their subset of guidelines aims to ensure funds are readily available to meet potential insurance liabilities in an extreme event plus other near-term liquidity requirements. In addition, the Group has established asset allocation and maturity parameters within the investment guidelines such that the majority of the investments are in high quality assets which could be converted into cash promptly and at minimal expense. The Group monitors market changes and outlook and reallocates assets as deemed necessary. The Group also monitors and reports Group liquidity against tolerances to the LICL Board. The Group also has a revolving credit facility that is available to both LICL and LUK to meet any short term liquidity needs. During 2019 the size of the facility was $75 million, this was reduced to $50 million in March 2020.

Monitoring
The continued effectiveness of the risk mitigation techniques is monitored by the Board's Investment Committee through quarterly investment performance reports and the Group and LICL Board through their review of the quarterly ORSA report plus the quarterly management IRRC meetings.

The Group has modelled a series of COVID-19 pandemic stress tests and assessed the potential impact on future cash flows and liquidity. As at 31 December 2020, the Group considers that it has more than adequate liquidity to pay its obligations as they fall due.

C6: OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes or systems. The Group and its subsidiaries have identified and evaluated their key operational risks and these are incorporated in the risk registers and modelled within the subsidiaries' capital models.

The Group has also established, and monitors compliance with, internal operational risk tolerances. The RRC reviews operational risk on at least an annual basis and operational risk is also covered in the Group CRO's quarterly ORSA report to the LHL Board and entity boards and in the LSL RCCC reporting.

Mitigation

In order to manage operational risks, the Group has implemented a robust governance framework. Policies and procedures are documented and identify the key risks and controls within processes. The Group's Internal Audit function provides independent feedback with regard to the accuracy and completeness of key risks and controls, and independently verifies the effective operation of these through substantive testing. All higher risk areas are subject to an annual audit while compliance with tax operating guidelines is audited quarterly. Frequency of consideration for audits for all other areas varies from quarterly at the most frequent to a minimum of once every four years, on a rotational basis.

Monitoring

The continued effectiveness of the risk mitigation techniques is monitored by the LHL and LICL Board through their review of the quarterly ORSA report and the quarterly risk register approval process plus the Board's input into the Company's strategy and business plan.

The COVID-19 pandemic has challenged the robustness of the Group's operational risk management framework. We are pleased with the Group's operational resilience and the business continuity arrangements that have been successfully demonstrated in the face of the COVID-19 pandemic. The majority of our employees have been working from home since March 2020 with no noticeable adverse impact on the Group's operating effectiveness. The Group recognises that it may be exposed to an increased level of operational cyber risk as a result of all employees working from home. The risk is being managed through enhanced monitoring of network activity, targeted staff training, a quarterly risk and control affirmation process, annual testing of business continuity plans and disaster recovery plans and a cyber security incident response plan.

C7: STRATEGIC RISK

The Group and Company has identified several strategic risks. These include:

- the risks that either the poor execution of the business plan or an inappropriate business plan in itself results in a strategy that fails to adequately reflect the trading environment, resulting in an inability to optimise performance, including reputational risk;
- the risks of the failure to maintain adequate capital, accessing capital at an inflated cost or the inability to access capital. This includes unanticipated changes in vendor, regulatory and/or rating agency models that could result in an increase in capital requirements or a change in the type of capital required; and
- the risks of succession planning, staff retention and key man risks.

Mitigation

Business plan risk – the Group and Company addresses the risks associated with the planning and execution of the business plan through a combination of the following:

- an iterative annual forward-looking business planning process with cross departmental involvement;
- evaluation and approval of the annual business plan by the Group and LICL Board of Directors;
- regular monitoring of actual versus planned results;
- periodic review and re-forecasting as market conditions change;
- responding to current events such as the COVID-19 pandemic and the impact on the business; and
- evaluation of climate change and the potential long-term implications/considerations for the business.

The forward looking business planning process covers a three year period from 2021 to 2023 and applies a number of sensitivity, stress and scenario tests. These tests include consideration of COVID-19 pandemic and climate change risks. The sensitivity and stress testing identified that even under the more extreme stress scenarios the Group had more than adequate liquidity and solvency headroom.

Capital management risk – risks associated with the effectiveness of the Group and Company's capital management are mitigated as follows:

- regular monitoring of current and prospective regulatory capital requirements and rating agency capital requirements;
- oversight of capital requirements by the Group and LICL Board of Directors;
- ability to purchase sufficient, cost effective reinsurance;
- maintaining contact with vendors, regulators and rating agencies in order to stay abreast of upcoming developments; and
- participation in industry groups such as the International Underwriters Association and the Association of Bermuda Insurers and Reinsurers.

Capital is increased or returned as appropriate. The retention of earnings generated leads to an increase in capital. Capital raising can include debt or equity and returns of capital may be made through dividends, share repurchases, a redemption of debt or any combination thereof. Other capital management tools and products available to the Group may also be utilised. All capital actions require approval by the Board of Directors.

The COVID-19 pandemic has contributed to a significant hardening in the market. On 10 June 2020, the group raised an additional $340.3 million of equity capital which will be used to fund organic growth and take advantage of the improved market opportunities during 2021. The Group's strategy is to maximise risk-adjusted returns for its shareholders across the long term by deploying more capital into a hardening market, in which pricing strengthens due to market capital constraints and to lower the amount of capital deployed in softer markets, where pricing is weaker due to oversupply. The return is generated within a broad framework of risk parameters.

Retention risk – the risks associated with succession planning, staff retention and key man risks are mitigated through a combination of resource planning processes and controls, including:

- the identification of key personnel with appropriate succession plans;
- the identification of key team profit generators and function holders with targeted retention packages;
- documented recruitment procedures, position descriptions and employment contracts;
- resource monitoring and the provision of appropriate compensation, including equity based compensation which vests over a defined time horizon; and
- training schemes.

Monitoring
The continued effectiveness of the risk mitigation techniques for other material risk is monitored by the Board through their review of the quarterly ORSA report and the quarterly capital paper. The Group Board's Nomination and Corporate Governance Committee is responsible for monitoring the adequacy of the Group's succession plans. The LICL Board is responsible for monitoring the adequacy of the Company's succession plans.

Group Risk
Group risks are any risks that may not have an impact at the individual entity level but have to be considered at the group level such as contagion risk or aggregation of business risks. Group risk is considered and evaluated by the LHL Board on a quarterly basis, as is the concentration of risk in each individual risk area (e.g. insurance, credit etc.). There are no significant risk concentrations at the Group level that are not otherwise reported above.

Mitigation & Monitoring
Group risks need to be considered on a case-by-case basis and as such there is no one size fits all mitigation strategy. The inclusion of group risk within the Group CRO's quarterly ORSA report ensures it is brought to the attention of the LHL Board and suitable mitigation plans can be put in place.

C8: STRESS TESTING AND SENSITIVITY ANALYSIS

Stress and scenario testing is a key part of the overall ERM framework and helps to provide a better understanding of the risks the Group is exposed to in both normal and stressed circumstances. It informs the development of risk appetites and tolerances and acts as a key input to capital management processes. The Group conducts sensitivity, stress (standard and reverse) and scenario testing on both a scheduled and ad-hoc basis as part of a number of the underlying components in the ERM and ORSA framework.

A range of sensitivity, stress and scenario testing techniques were applied throughout the year in response to specific actual and proposed changes to the business strategy and risk profile.

Sensitivity testing was conducted as part of the on-going development and validation of the internal model, methodology and assumptions across material risk categories. This was overseen by the RRC and involved management and subject matter experts from throughout the business.

Scenario testing was used to assess the risk, return and capital implications of alternative potential planning scenarios. It was supported by the use of modelling outputs and applied both within the annual business planning process and on an ad-hoc basis to support the evaluation of potential changes in business strategy. The scenarios covered the following key risk areas: insurance risk, investment risk, liquidity risk, operational risk and regulatory risk. They are, however, predominately underwriting focused which is deliberate given that underwriting is by far the most significant driver of the Group's tail risk and therefore is the natural focus in terms of stress testing the stability of the Group. The impact of climate-related risks, within the key risk areas, was considered as part of the scenario testing process.

Standard stress testing was used to evaluate the impact of extreme yet plausible events and scenarios that might impact the business in order to test the resilience of the plan and evaluate alternative risk mitigation arrangements. It is supported by the use of catastrophe models and was applied both during the business planning and ORSA processes and reported to the Board as part of the Group CRO's quarterly ORSA report.

Reverse stress testing was focussed on deliberately deconstructing the business model to test for vulnerabilities and potential events that could make it unviable. In addition to the consideration of extreme financial loss scenarios it considered the interaction of risks such as reputational and regulatory failures and loss of key resources that might combine to make the business model unviable. It utilised a combination of quantitative and qualitative techniques. Reverse stress testing to date has been focussed at the Group level to determine the full impact to the business.

As noted above, stress and scenario testing informs the development of risk appetites and tolerances and acts as a key input to the Group's capital management processes. The Group considers a wide range of measures when establishing the appropriate level of capital at the Group and individual entity level, this includes our internal view of economic and risk capital, applicable regulatory minimum capital requirements, the expectations of external rating agencies and the potential stress events or losses to which the Group is exposed. The target level of economic capital is set so as to ensure that Lancashire maintains headroom over the range of current and anticipated capital requirements that is appropriate to its risk profile at a given point in the cycle. This means that the results of stress testing and sensitivity analysis are communicated and acted upon as deemed appropriate through the business cycle and the ERM framework.

In addition to the scheduled and ad-hoc testing as part of our ORSA framework, the Group may at times be required to conduct stress/scenario testing and report outcomes in response to specific regulatory or rating agency requests.

In response to the COVID-19 pandemic, the Group initiated its Post Loss Response process. The process reviewed and assessed the potential implications for each class of business that the Group underwrites, across all its platforms, with involvement from underwriting, exposure management, actuarial, claims, treasury and finance teams. The output of this review formed the basis of our loss reserving. The current best estimate financial impact of COVID-19 is $42.2 million ($38.6 million for LICL), net of reinsurance and including the impact of reinstatement premiums. This constitutes 6.9% of our total net loss reserves and 2.7% of our net assets and relates primarily to our property segment.

To assess the Group's going concern, resilience and response to the COVID-19 pandemic, the financial stability of the Group was modelled for a period of at least 12 months and a number of sensitivity, stress and scenario tests were applied. This included, among other analysis, a best estimate forecast with scenario analysis covering the impact of reserve releases, attritional, large and catastrophe loss events alongside optimistic and pessimistic investment return scenarios. To further stress the financial stability of the Group, additional scenario testing was performed. This included modelling the breakeven capital requirements of our regulators and rating agencies, the impact of potential management actions to reduce the Group's exposure to climate change-related risks, the continuation of the COVID-19 pandemic throughout 2021 negatively impacting the economy, travel industry, global events and counterparty credit risk, the occurrence of a number of high severity loss events impacting all three of our underwriting platforms in 2021 and a reverse stress test scenario designed to render the business model unviable. The testing identified that even under the more severe but plausible stress scenarios, the Group had more than adequate liquidity and solvency headroom.

C9: OTHER MATERIAL INFORMATION

Not applicable – all material information regarding the Risk Profile has been described in C1-C8 above.

D. Solvency valuation

D1: ASSETS

The breakdown of total assets in the EBS balance sheet for the years ended 31 December 2020 and 2019 is as follows:

	LHL		LICL	
	2020 $m	2019 $m	2020 $m	2019 $m
Cash and cash equivalents	432.4	320.4	289.9	252.0
Quoted investments	1,649.3	1,332.7	1,367.3	1,052.8
Unquoted investments	207.4	192.9	207.4	192.9
Other assets	138.3	111.3	152.3	53.0
Investment in associate	127.2	108.3	n/a	n/a
Total assets	**2,554.6**	**2,065.6**	**2,016.9**	**1,550.7**

LICL applies a full "look through" approach to the 85% inter-company quota share agreement with CCL 1998 for BSCR EBS reporting purposes. This is done by adding 85% of each of CCL 1998's assets and liabilities on a line by line basis to LICL's IFRS balance sheet values. This approach was requested by the BMA and results in required regulatory capital requirements for LICL which more accurately reflect the risk associated with the CCL 1998 quota share agreement.

Financial assets

Money market funds and cash and cash equivalents are carried at amortised cost. Carrying amounts approximate fair value due to the short-term nature and high liquidity of the instruments. No adjustments are required for EBS valuation purposes.

Financial assets are held at fair value. Prices for the Group's investment portfolio are provided by a third-party investment accounting firm whose pricing processes and the controls thereon are subject to an annual audit on both the operation and the effectiveness of those controls. Various recognised reputable pricing sources are used including pricing vendors and broker-dealers. The pricing sources use bid prices where available, otherwise indicative prices are quoted based on observable market trade data. The prices provided are compared to the investment managers' pricing. The Group has not made any adjustments to any pricing provided by independent pricing services or its third-party investment managers for the year ended 31 December 2020.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Securities with quoted prices in active markets for similar assets or liabilities or securities are valued using other valuation techniques for which all significant inputs are based on observable market data. These instruments are valued via independent external sources using directly observable inputs to models or other valuation methods. The valuation methods used are typically industry accepted standards and include broker-dealer quotes and pricing models including present values and future cash flows with inputs such as yield curves, interest rates, prepayment speeds and default rates.

The estimated fair values of the Group's hedge funds are determined using a combination of the most recent NAVs provided by each fund's independent administrator and the estimated performance provided by each hedge fund manager. Independent administrators provide monthly reported NAVs with up to a one-month delay in valuation. The most recent NAV available for each hedge fund is adjusted for the estimated performance, as provided by the fund manager, between the NAV date and the reporting date. Historically estimated fair values incorporating these performance estimates have not been significantly different from subsequent NAVs. Given the Group's knowledge of the underlying investments and the size of the Group's investment therein, we would not anticipate any material variance between estimated valuations and the final NAVs reported by the administrators.

The estimated fair value of the Group's private investment funds are determined using statements received from each fund's investment managers on either a monthly or quarterly in arrears basis. In addition these valuations will be compared with benchmarks or other indices to assess the reasonableness of the estimated fair value of each fund. Given the Group's knowledge of the underlying investments and the size of the Group's investment therein, we would not anticipate any material variance between estimated valuations and the final NAVs reported by the investment managers.

Other assets

The carrying value of other assets approximates fair value due to the short-term nature of the receivables. No adjustments are required for EBS valuation purposes.

Investment in associate

The investment in LCM is accounted for as an associate and was originally recognised at cost and thereafter accounted for using the equity method. No adjustments are required for EBS valuation purposes.

Reclassification adjustments

Premium receivable balances that are not yet due are included in the cashflows used to calculate technical provisions and those which are due but not yet received are included in the EBS.

Reinsurance recoveries and unearned premiums on premium ceded are reclassified and explicitly included in the calculation of technical provisions (see section D2 below).

Valuation of intangible assets, deferred acquisition costs and prepaid expenses

Intangible assets, deferred acquisition costs and prepaid expenses are valued at nil for EBS valuation purposes.

D2: LIABILITIES

The breakdown of total liabilities in the EBS balance sheet for the years ended 31 December 2020 and 2019 is as follows:

	LHL		LICL	
	2020 \$m	2019 \$m	**2020 \$m**	2019 \$m
Best estimate loss and loss expense provisions	522.9	464.0	455.5	407.6
Technical provisions[1]	131.1	50.9	142.1	83.4
Insurance and reinsurance balances payable	22.5	27.4	66.3	74.7
Other liabilities and payables	80.2	82.9	48.4	19.6
Long-term debt	327.5	323.5	n/a	n/a
Total liabilities	**1,084.2**	**948.7**	**712.3**	**585.3**

(1) The Group risk margin of \$68.0 million (2019: \$49.1 million) and the LICL risk margin of \$60.1 million (2019 \$41.7 million) is included within the technical provisions balance.

INSURANCE AND REINSURANCE BALANCES PAYABLE

Insurance and reinsurance balances payable that are not yet due are included in the cashflows used to calculate technical provisions and those which are due but not yet paid are included in the EBS.

OTHER LIABILITIES AND PAYABLES

Other liabilities and payables are valued for EBS purposes on the same basis as for IFRS accounting purposes since the carrying value approximates economic value due to their short-term nature.

LONG TERM DEBT

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

VALUATION OF DEFERRED COMMISSION INCOME

Deferred commission income is valued at nil for EBS valuation purposes.

TECHNICAL PROVISIONS

The EBS basis technical provisions are comprised of three elements:

- claims provisions – the best estimate of loss reserves on events which have occurred by the balance sheet date including associated expenses and net of associated future premium;
- premium provisions – the best estimate reserves on the remaining exposure of contracts which the Group is obligated to at the balance sheet date including associated expenses and net of associated future premium; and
- risk margin or “market value margin” – an additional amount, in excess of the best estimate provisions, expected to be required by a third party in order to fund the future regulatory capital required to meet the obligations. This is calculated based on a cost of capital approach.

The valuation methodology for determining the technical provisions is consistent across all the BMA lines of business and is broadly a two-step process. The first step is determining the IFRS basis provisions, with the EBS provisions determined from these by applying a number of adjustments and additional data inputs. The use of the IFRS provisions is deemed a suitable starting point for the EBS technical provisions due to their significant scrutiny from internal and external parties prior to use.

IFRS provisions for the purpose of this document and the comparison to EBS results (both gross and ceded to reinsurers) include the earned provisions relating to events which have occurred at the valuation date (whether reported or not) plus associated loss adjustment expenses, plus non-monetary items corresponding to 100% of the unearned premium (i.e. unearned premium reserve, ‘UPR’) less an allowance for the acquisition costs already paid on this unearned premium (i.e. deferred acquisition costs, ‘DAC’). EBS then adjusts the above basis (separately for gross and ceded to reinsurers amounts) to move to a discounted actuarial best estimate cashflow approach (claims, expenses and premiums) on a legally obliged (rather than inception) basis allowing for the expected value of all possible outcomes. This removes the non-monetary items and replaces these with the cashflows expected to arise from these exposures including business to which the Group is legally obliged to accept but has yet to incept.

Provisions are valued separately depending on whether claims events have occurred or are yet to occur at the valuation date. Claims events which have occurred (whether reported to the insurer or not) are known as claims provisions. Provisions in respect of future claim events are known as premium provisions.

In addition to the above ‘best estimate’ of the future cashflows, a risk margin is added to represent the cost of capital required to run-off the existing obligations to expiry. This adjustment is designed to increase the best estimate to a market consistent value in line with the rest of the EBS balance sheet.

The actuarial function considers the process to determine both IFRS and EBS basis technical provisions as appropriate as assessed through the data governance framework and technical provision validation process. The overall approach to valuing and validating the technical provisions recognises the inherent uncertainty in assessing the size, timing and nature of future insurance cashflows, in particular for claims which have yet to occur.

The approach adopted recognises the principle of proportionality while ensuring compliance with the EBS regulations. The principle of proportionality permits insurers to choose and apply valuation methods which are:

- suitable to achieve the objective of deriving a market-consistent valuation according to EBS principles; but
- not more sophisticated than is needed in order to reach this objective.

The approach to deriving technical provisions adheres to this principle by focusing most effort on the material drivers of the valuation basis and the associated risks and sensitivities.

LEVEL OF UNCERTAINTY IN THE VALUATION OF TECHNICAL PROVISIONS

The main driver of uncertainty within the technical provisions is the final outcome of claims both in respect of events which have occurred (whether reported or not) and which may arise in future from unexpired exposure. Lancashire's business and underwriting model generally results in claims which are low frequency and high severity in nature making the available historical loss data volatile and less useful for predicting ultimate losses.

In most cases, reinsurance helps in reducing the uncertainty and exposure, particularly for known events where, while the gross outcome may be uncertain, the fact that reinsurance protection is in place, particularly excess of loss coverage, the net impact may be relatively stable and known. At the best estimate (i.e. mean) level it is generally expected that profit would be ceded to reinsurers as the reinsurance programme generally provides protection in more extreme (i.e. above mean) outcomes. Given the nature of the outwards reinsurance programme, this provides protection against low frequency, high severity events where, upon occurrence, the reinsurance generates significant benefits to the Group and the Company.

The EBS adjustments to the IFRS technical provisions introduce a number of areas of uncertainty either due to the uncertainty in the amounts and subjectivity of the approach or through future volatility which could vary the particular element significantly. The most appropriate approaches have been selected as described in this document.

UNCERTAINTY WITHIN THE CLAIMS PROVISIONS

In respect of claim events which have occurred, the lack of stable and reliable historical data makes predictions of ultimate losses, particularly for less well developed accident years or where there is ongoing dispute or litigation, especially uncertain. There is also a time lag inherent in reporting from the original claimant to the primary insurer to the broker and then to the reinsurer. In the case of proportional contracts, reliance is placed on an analysis of a contract's historical experience, industry information, and the professional judgement of underwriters in estimating reserves for these contracts. In addition, if available, reliance is placed partially on ultimate loss ratio forecasts as reported by insureds or cedants, which are normally subject to a quarterly or six-month lag.

As a result of the time lag described above, an estimate must be made of the technical provisions. Because of the degree of reliance that is necessarily placed on insureds or ceding companies for claims reporting, the associated time lag, the low frequency/high severity nature of much of the business that the Group writes, and the varying reserving practices among ceding companies, reserve estimates are highly dependent on management judgement and are therefore uncertain. During the loss settlement period, which may be years in duration, additional facts regarding individual claims and trends often will become known, and current laws and case law may change, with a consequential impact on reserving. The claims count on the types of insurance and reinsurance written, which are low frequency and high severity in nature, is generally low.

For certain catastrophic events there are greater uncertainties underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Complexity resulting from problems such as policy coverage issues, multiple events affecting one geographic area and the resulting impact on claims adjusting (including the allocation of claims to the specific event and the effect of demand surge on the cost of building materials and labour) by, and communications from, insureds or ceding companies, can cause delays to the timing with which the Group is notified of changes to loss estimates.

The majority of the technical provision estimate relates to potential claims on non-elemental risks where timing delays in insured or cedant reporting may mean losses could have occurred which the Group was not made aware of by the balance sheet date.

COVID-19 is an unprecedented event for the insurance industry that is still continuing, and the effects of COVID-19 as a loss event to the insurance and reinsurance markets remain both ongoing and uncertain. Reserving for the impacts of the COVID-19 pandemic is exceptionally difficult, both in estimating the direct impacts of the pandemic itself and also in allowing for additional reserves related to the secondary impacts of lockdowns on the costs of settling claims across all lines of business. Given the uncertainty noted above and the continuation of the impacts of the pandemic into 2021 our final COVID-19-related losses may be materially different from those booked to date.

UNCERTAINTY WITHIN THE PREMIUM PROVISIONS

In respect of unexpired exposure, the fact that claim events have yet to occur makes the final outcome on this exposure less certain. Under IFRS, the portion of premium related to the unexpired portion of the risk period is deferred and reflected in unearned premium. The 'best estimate cashflow' approach under EBS however requires provisioning for the expected level of future claims and expenses which will arise from this exposure which may then be offset by the future premium amounts.

As a result of the cashflow approach, the profit embedded in the unexpired exposures is realised immediately under the EBS, compared to IFRS which defers this until the exposure is recognised. While the profit outcome will ultimately be the same over time, the accounting treatment differs for the balance sheet. There is a greater uncertainty in the EBS balance sheet with regard to unexpired exposures than on the IFRS balance sheet as there is more reliance on assumptions about future claims experience.

DIFFERENCES BETWEEN VALUE FOR IFRS AND EBS PURPOSES

To determine the EBS technical provisions the Group takes the IFRS technical provisions and makes a number of adjustments. These adjustments are described below:

(I) IFRS PROVISIONS

Provisions for claims which have occurred by the valuation date (whether reported or not) are calculated using traditional actuarial methods on a gross and net of reinsurance basis. Attritional losses are reserved using claim development methods the Bornhuetter-Ferguson technique whilst large losses are reserved for using exposure analyses or claim development methods. A provision is also included for the expenses associated with settling these claims.

The unearned premium in respect of incepted business is deferred as a liability under IFRS, where this is deemed to be insufficient, an additional provision may also be held in excess of this.

The IFRS basis technical provisions are calculated quarterly by the actuarial function. This is overseen by the Reserve Committee who review the reserves, with particular attention to the large events, and the approach to determining these. The reserves are then approved by the Audit Committee. Each quarter's reserve setting process is supported by back testing of prior expectations against the actual observed experience. This is done based on the level of incurred claims (paid plus reported) compared to the amount that was anticipated for the quarter at the previous quarter end. This is used to support changes in the ultimate claim outcome estimates over time.

The Group engages an external actuary to conduct an independent review of the Group's claims reserves on an IFRS basis every six months. This analysis is included for comparison in the IBNR report to the Board. Significant differences between the two estimates are discussed in the report. The external auditors, KPMG LLP, also present a comparison of the Group's reserves to their own best estimates at the second and fourth quarter Board meetings. A similar comparison is also presented to the LICL Board by the Group Chief Actuary.

(II) MOVEMENT OF NOT YET DUE PREMIUM DEBTORS TO TECHNICAL PROVISIONS

In the IFRS statutory accounts future premiums inwards/outwards reside within the debtors/creditors balances in the balance sheet. Under the EBS cashflow approach, the future premium cashflows which are not due by the valuation date are reallocated to the technical provisions. Premium due at the valuation date remains in the debtors/creditors balances. All future (re)insurance payable and receivable balances are assumed to relate to the premium provisions within the EBS balance sheet.

(III) ADJUSTMENTS TO IFRS LOSS RESERVES FOR BASIS CHANGE

Adjustments to IFRS loss reserves for basis change comprises the following:

- Adjustment to actuarial best estimate

  The IFRS reserves are moved from management best estimate to a pure actuarial best estimate – this is done at a class of business level and separately for gross and reinsurance amounts.

- Allowance for events not in data

  The IFRS technical provisions allow for the best estimate of 'reasonably foreseeable' outcomes whereas the EBS requires the best estimate of 'all possible outcomes'. This implicitly includes a wider range of events in the future claim estimates and introduces the concept of an ENID allowance in the solvency provisions. This may include latent claims or very extreme high severity/low probability claims but more widely any event not observed in the historical data. An ENID uplift is calculated separately for each line of business and added to the claims provision to recognise the difference between IFRS and EBS bases. Given the generally short reporting and settlement periods of the business written the provisions for ENIDs within the claims provisions (i.e. in respect of events which have occurred) is expected to be lower than the equivalent ENID allowance within the premium provision.

- Inclusion of additional expenses

  The expense provisions are adjusted to include an allowance for all future expenses required to settle the existing insurance obligations on a going concern basis. This is higher than the loss adjustment expenses included within the IFRS provisions (typically split across 'allocated' – ALAE and 'unallocated' – ULAE provisions) as it includes items such as overheads and investment management fees. The ALAE provisions are included implicitly within loss reserves under both accounting and EBS bases.

  To calculate the additional expense requirement, in excess of the IFRS provisions, the Group performs an exercise to allocate historic expenses to the management of in-force business at that time. The in-force attributed expenses are then analysed as a percentage of the historical claim payments and future expense cashflows are generated by assuming the same percentage applies to the future claim payments. The Group has used the proportionality principle and concluded that the impact of expense inflation is negligible. This is due to the short-tailed nature of the business underwritten.

  Brokerage or other acquisition expenses associated with the existing premium debtors are determined when these are established in the accounts; as such these are booked net of acquisition costs. No further allowance for acquisition costs on (re)insurance receivables and payables is made in the technical provisions.

D. SOLVENCY VALUATION CONTINUED

(IV) PROFIT IN RESPECT OF LEGALLY OBLIGED FUTURE EXPOSURE

Profit in respect of legally obliged future exposure comprises of the following:

- Removal of UPR and DAC

  Under the EBS the full cashflows associated with the unearned premium provisions must be valued and accounted for rather than accounting for non-monetary items such as gross and ceded UPR and DAC. This removes an element of prudence in the accounting basis technical provisions and recognises the anticipated profit embedded within the business at the valuation date rather than deferring this recognition as the exposure is recognised. For the EBS technical provisions the accounting concepts of UPR and DAC are therefore replaced with the expected future claims and associated expenses arising from the unearned exposure described below.

- Inclusion of claims associated with UPR

  Gross and net premium provisions are calculated using expected ultimate ratios by line of business applied to the unearned premium. The loss ratios are sourced from the business plan and represent the best estimate view (i.e. mean of the distribution of future outcomes) of the losses likely to emerge in future periods and as such are deemed a reasonable assumption to use. The ENID uplift, see below, is applied to these ratios to move this to an 'all outcomes' basis.

- Inclusion of future reinsurance premium covering future exposure on existing legal obligations

  Credit is being taken in the technical provisions for recoveries on expected future claims events which have yet to occur. These events may occur a number of years in the future and are potentially covered by reinsurance to be purchased in these future years, notably ceded reinsurance contracts on a losses occurring basis. As a consequence, an allowance needs to be made in the technical provisions for the share of this planned future reinsurance premium which covers the future exposure on the existing obligations. This is done by apportioning the business plan future reinsurance premium spend between current and future inwards obligations.

  The future reinsurance premium spend, split between the risk premium and any brokerage/commissions (using ratios from the business plan) are added to the claims and expenses to determine the best estimate provision.

- Allowance for Events Not In Data

  Similar to the claims provisions (as described above), an ENID allowance is also added to the premium provision. This is done using a similar set of assumptions and processes to the claims provision, however, given the higher uncertainty in the premium provisions, the allowance for ENIDs is generally proportionally greater than the claims provisions.

- Future cashflow from unincepted legal obligations

  Contract boundaries for EBS purposes are defined as all contracts which the Group is legally obligated to accept as at the balance sheet date. It therefore includes contracts which may not have incepted but where the insurer no longer has a unilateral right to cancel the contract, reject the premium and amend the premiums or benefits payable under the contract to reflect the underlying risks. This means that in addition to the claims provisions and unearned portion of in-force business, cashflows also need to be considered in relation to business which has not incepted but where the rights as outlined above do not hold. Lancashire's underwriting system records such policies providing an up-to-date and accurate view of the nature and scale of this business.

  To determine the technical provision allowance for this element, the future premium on policies which have been agreed prior, but incept after, the valuation date is taken from the underwriting system as the exposure measure. Similar to the incepted approach with UPR, this unincepted future premium is multiplied by the ultimate loss ratio in the business plan and uplifted by the ENID ratios to determine the future claims. By applying a loss ratio to the full future premium an implicit assumption is made that there is no lapse risk, therefore all contracts which have been bound will be taken up. This is deemed suitable due to the use of the live underwriting system at the valuation date to indicate which policies are legally bound.

  The unincepted legal obligations receive a share of the allocated expenses as described above.

  The future premium is taken net of the acquisition cost and deducted from the claims and expenses to determine the best estimate provision. Note that in most cases the future premium on this business will exceed the expected claims and expenses. In this case the contribution of the unincepted premium provisions to the overall technical provisions will be negative.

D. SOLVENCY VALUATION CONTINUED

(V) ALLOWANCE FOR REINSURER DEFAULT

An allowance is added for credit default risk on reinsurance recoverables in the balance sheet. Recoverables are identified by class based on the gross and net future claims modelling as derived through the IFRS accounting and EBS reserving processes.

Use of simplified method

The following assumptions are made to derive the allowance:

- all counterparties have the same annual probability of default, equivalent to an A-rated counterparty in line with the BSCR calculation;
- a recovery rate of 50% upon default in line with the BSCR calculation;
- default occurring at a future date equal to the modified duration of the recoveries; and
- a constant probability of default in future years.

This adjustment and the assumptions used to derive it ensure consistency between the technical provisions and BSCR calculations. Further, the approach is deemed proportionate given the generally low utilisation of outwards third party reinsurance at the mean (as the technical provisions target) and also the low levels of industry default data on which to derive another, more representative and accurate assumption.

(VI) ALLOWANCE FOR DISCOUNTING AT RISK FREE RATES

The undiscounted future claim, premium and expense amounts are derived, as described above, by class of business and the most material currencies. All non-material currencies are grouped together and discounted using a U.S. dollar risk-free yield curve.

Cashflow patterns are applied to these to determine the timing of payments and receipts. The claim and premium cashflow patterns have been parameterised from historical data and expense cashflow pattern assumptions are described above. Reinsurance recoveries are assumed to occur 3 months after the gross claim cashflow. Future calendar quarter cashflows are generated for all technical provision elements until all payments/receipts are assumed to have been settled.

The present value of the projected cash flows is determined by discounting each currencies' cashflows using yield curves which are published quarterly on the BMA's website. The unadjusted risk-free yield curves are used.

(VII) RISK MARGIN

The best estimate technical provisions on the EBS basis are supplemented by the risk margin, representing the cost of capital which a third party would incur in taking over and running the existing obligations to expiry. The risk margin is calculated by determining the cost of providing an amount of eligible capital equal to the BSCR necessary to support the Group's current insurance obligations over their lifetime. This is derived by assuming the obligations are transferred to a 'reference undertaking' at the valuation date who has no existing obligations, does not intend to write further business and is able to invest assets to minimise its market risk. All associated outwards reinsurance is also assumed to be transferred. The rate used to determine the cost of providing the amount of eligible capital is called the Cost-of-Capital rate and is prescribed in the EBS Regulations (currently at 6%).

The key judgement for the calculation of the risk margin is determining the starting BSCR and further, how the future BSCR, in respect of the obligations at the valuation date, develops over time.

The starting t=0 BSCR is scaled to remove risk associated with business not yet bound and market risk is removed completely. Operational and counterparty default risks remain. The risks are re-aggregated in line with the BSCR correlation matrix. Future BSCRs are adjusted to remove insurance risks associated with the underwriting of new business and its remaining exposure which would be nil after the first year on obligated business at the t=0 valuation date.

(VIII) USE OF SIMPLIFIED METHOD

The future BSCR charges for each calendar year will reduce more slowly than the run-off of future claims. For example, an element of operational risk would remain more 'fixed' than the claims run-off would represent and further, reserve risk is likely to increase proportionally as technical provisions reduce as any single claim would increase the overall volatility and the provisions which take longer to settle are likely to be on more contentious claims. To account for this, the Group assumes the BSCRs beyond time 0 are reduced proportional to the square root of the remaining claims reserves since time 0.

This simplification is used as the explicit calculation of every year's BSCR to run-off would hugely increase the complexity required to calculate the technical provisions. As the Group would have zero unavoidable market risk, reserve risk would be the largest driver of the BSCR in runoff. The counterparty default risk is highly correlated with underwriting risk; therefore in a run-off situation with no underwriting risk, the counterparty default risk would also reduce significantly. The operational risk would also be expected to reduce in run-off as the business volumes and reserves declined. As the BSCR would be driven by reserving risk, an approach to derive the future BSCRs which is a function of the run-off of the technical provisions is deemed appropriate. The slower BSCR decay pattern (using the square root of the payment pattern) allows for the increasing volatility of risk as the provisions reduce (e.g. due to a 'fixed' nature of operational risk and the likelihood for more uncertainty in the reinsurance recoveries on the claims which take longer to settle).

The calculation is then completed by discounting the future BSCRs using the risk-free yield curves provided by the BMA and applying the cost of capital (6%). The risk margin is the sum of each future year's discounted cost of capital. For reporting purposes, this is then allocated to class in proportion to the net future claims.

(IX) OTHER CASHFLOWS

Cashflows relating to salvage and subrogation, and those relating to tax payments to be charged to policyholders or which are required to settle insurance or reinsurance obligations are judged to be immaterial based on past history and are therefore excluded from the technical provision calculation.

Reinsurance recoverables

Reinsurance recoverables consist of amounts due from reinsurers for third party reinsurance. They comprise reinsurers' share of premium and claims provisions and are calculated explicitly in the process using a similar methodology as the underlying gross claims and premium provisions.

Reinsurance recoveries on gross reported claims are determined when the gross losses are assessed. The recoveries on future unreported claims (on both incepted and unincepted but legally obliged unearned business) are determined by applying reinsurance/gross claims ratios to the gross claims. The ratios are sourced from the Group's business plan consistently with the gross amounts. An allowance is given for credit default risk on reinsurance recoverables as described above.

Reinsurance recoverables are included in the liability table above, shown net within the best estimate loss and loss expense provisions.

Material changes in calculation assumptions

No material changes have been made to the methods and processes used in the calculations of the technical provisions since 2019 year-end. The assumptions used in the process do however change from period to period due to internal and external factors such as change in business mix, claims events and perceived profitability of the business underwritten.

D3: OTHER MATERIAL INFORMATION

Not applicable – there are no other material valuation assumptions that are not already covered in D1 and D2 above.

E. Capital management

E1: MANAGEMENT OF CAPITAL

The Group actively reviews the level and composition of capital on an ongoing basis. Decisions on optimal capital levels are also an integral part of the Group's business planning process which covers a 3 year time horizon. Internal methods have been developed to review the profitability of classes of business and their estimated capital requirements and the capital requirements of the combination of a wide range of other risk categories.

The key aim of the Group's capital management process is to maintain a strong balance sheet, whilst:

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

The subsidiary operating entities also conduct capital requirement assessments under internal measures and in compliance with local regulatory requirements. All capital actions require approval by the Board of Directors. The retention of earnings generated also leads to an increase in capital.

There have been no material changes in the approach to capital management over the reporting period.

E2: ELIGIBLE CAPITAL

(I) ELIGIBLE CAPITAL BY TIER

	LHL		LICL	
	2020 $m	2019 $m	2020 $m	2019 $m
Tier 1				
Fully paid common shares	122.0	101.5	1.0	1.0
Contributed surplus	1,200.4	868.0	1,125.5	840.5
Statutory economic surplus	148.0	147.3	178.0	124.0
Excess encumbered assets transferred to Tier 2	(82.3)	(127.3)	(146.1)	(124.1)
Total Tier 1 capital	**1,388.1**	**989.5**	**1,158.4**	**841.4**
Tier 2				
Excess encumbered assets deducted from Tier 1	82.3	127.3	146.1	124.1
Total Tier 2 capital	**82.3**	**127.3**	**146.1**	**124.1**
Total eligible capital	**1,470.4**	**1,116.8**	**1,304.5**	**965.5**

Tier 1 capital is basic capital which includes fully paid up capital shares and contributed surplus, plus statutory economic surplus and minority interest, subject to certain adjustments. As at 31 December 2020 LHL and LICL continued to hold excess encumbered assets, that are effectively treated as Tier 2 capital. These excess assets were predominantly held in LICL's U.S. MBRT.

On 10 June 2020, LHL issued 39,568,089 new common shares, raising a total of $340.3 million, $19.8 million of which is included in share capital and $320.5 million of which is included in contributed surplus, net of offering expenses. The capital augments our already robust capital base and remains at our disposal to fund new underwriting opportunities in 2021.

1,500,000 new common shares at par value of $0.7 million and a total value of $15.0 million were issued to fund future RSS exercises.

(II) ELIGIBLE CAPITAL COMPOSITION AND REGULATORY MINIMUMS

The Act stipulates certain minimum capital requirements needed to meet the Minimum Margin of Solvency ("MSM") and the Enhanced Capital Requirement ("ECR"). The Act requires that Tier 1 capital contributes at least 80% to the MSM and 60% to the ECR. The Company currently meets both these requirements as Tier 1 capital covers over 100% of both the MSM and ECR.

(III) ELIGIBLE CAPITAL TRANSITIONAL ARRANGEMENTS

The Group and Company's eligible capital is not subject to any transitional arrangements under the BMA's Eligible Capital Rules.

(IV) ELIGIBLE CAPITAL ENCUMBRANCES

Not applicable.

(V) ELIGIBLE CAPITAL ANCILLARY INSTRUMENTS

Not applicable – the Group and Company had not issued any additional instruments as at 31 December 2020. See F1 for details of the fixed rate junior subordinated notes which were issued by LHL in March and April 2021.

(VI) IDENTIFICATION OF DIFFERENCES IN SHAREHOLDER'S EQUITY – IFRS ACCOUNTING VERSUS AVAILABLE STATUTORY CAPITAL AND SURPLUS

	LHL		LICL	
	2020 $m	2019 $m	2020 $m	2019 $m
Shareholder's equity – IFRS accounting	1,538.9	1,194.2	1,285.7	951.7
Non-admitted assets removed	(156.6)	(159.5)	(0.4)	(1.9)
Valuation adjustments relating to technical provisions	88.1	82.1	19.1	16.4
Cathedral Capital (1998) Limited[1]	n/a	n/a	0.1	(0.7)
Shareholder's equity – Total Statutory Economic Capital and Surplus	**1,470.4**	**1,116.8**	**1,304.5**	**965.5**

(1) As noted in Section D1, LICL applies a full "look through" approach to the 85% inter-company quota share arrangement with CCL 1998 for BSCR EBS reporting purposes.

E3: REGULATORY CAPITAL REQUIREMENTS

AMOUNT OF MSM AND ECR AT THE END OF THE REPORTING PERIOD:

LHL	2020 $m	2020 %[1]	2019 $m	2019 %[1]
Minimum Margin of Solvency	180.2	816%	138.0	809%
Enhanced Capital Requirement	667.9	220%	495.9	225%

LICL	2020 $m	2020 %[1]	2019 $m	2020 %[1]
Minimum Margin of Solvency	158.5	823%	115.3	837%
Enhanced Capital Requirement	633.9	206%	445.2	217%

(1) Coverage ratio of Available Statutory Capital and Surplus.

Changes to the BMA's BSCR calculation methodology came into force for the 2019 year-end reporting period but as part of the transition to the new methodology the BMA is phasing the implementation over a 3-year period. The 2020 and 2019 ECR noted above reflects the transitional required capital which represents a proportion of the difference between the BSCR based on the old methodology and the new methodology.

The responsibility for Lancashire's Group supervision switched from the PRA to the BMA effective 1 January 2019.

Both LHL and LICL have held capital in excess of their regulatory requirements throughout 2020 and 2019.

E4: INTERNAL CAPITAL MODEL

Not applicable – the Group and Company has not applied to have its internal capital model approved to determine its regulatory capital requirements.

F. Significant events

F1: DESCRIPTION OF EVENTS

DEBT ISSUANCE

LHL issued $450 million of junior subordinated notes in March 2021. The notes have been approved by the BMA as Tier 2 Ancillary capital. The proceeds of the notes will be used to repay the Group's existing senior and junior debt, which totals approximately $327.5 million, with the surplus available to support new underwriting opportunities. The Group's existing debt instruments were not approved for regulatory capital purposes so the impact of the issuance on the Group's and LICL's regulatory capital position will be favourable. Including the $450 million of junior subordinated notes as Tier 2 Ancillary capital would increase the 31 December 2020 total eligible capital to $1,920.4 million and materially increase the ECR ratio.

OTHER EVENTS

There have been no other significant events that are material to the Group or the Company that have taken place since the end of the 2020 financial year to the date of filing this Financial Condition Report.

However, on 9 February 2021, the Board of Directors declared the payment of an ordinary dividend of $0.10 per common share, which will result in an aggregate payment of approximately $24.4 million. The dividend will be paid on 4 June 2021 to shareholders of record on 7 May 2021.

Appendix 1: Glossary

ABIR
Association of Bermuda Insurers and Reinsurers

THE ACT
The Insurance Act 1978 and related regulations

ADDITIONAL CASE RESERVES (ACR)
Additional reserves deemed necessary by management

AFS
Available for sale

AGGREGATE
Accumulations of insurance loss exposures which result from underwriting multiple risks that are exposed to common causes of loss

AIR
AIR Worldwide

A.M. BEST COMPANY (A.M. BEST)
A.M. Best is a full-service credit rating organisation dedicated to serving the financial services industries, focusing on the insurance sector

BOARD OF DIRECTORS
Unless otherwise stated refers to the Company's Board of Directors

BMA
Bermuda Monetary Authority

BSCR
Bermuda Solvency Capital Requirement

BSX
Bermuda Stock Exchange

CCL 1998
Cathedral Capital (1998) Limited

CEDED
To transfer insurance risk from a direct insurer to a reinsurer and/or from a reinsurer to a retrocessionaire

CEO
Chief Executive Officer

CFO
Chief Financial Officer

CHANGE IN FCBVS
The IRR of the change in FCBVS in the period plus accrued dividends

CISSA
Commercial insurer solvency self-assessment

THE COMPANY
Lancashire Insurance Company Limited

CRO
Chief Risk Officer

DEFERRED ACQUISITION COSTS
Costs incurred for the acquisition or the renewal of insurance policies (e.g. brokerage and premium taxes) which are deferred and amortised over the term of the insurance contracts to which they relate

DURATION
Duration is the weighted average maturity of a security's cash flows, where the present values of the cash flows serve as the weights. The effect of the convexity, or sensitivity, of the portfolio's response to changes in interest rates is also factored in to the calculation

EBS
Economic balance sheet

ECR
Enhanced Capital Requirement

ENID
Events Not In Data

ERM
Enterprise Risk Management

EXCESS OF LOSS
Reinsurance or insurance that indemnifies the reinsured or insured against all or a specified portion of losses on an underlying insurance policy in excess of a specified amount

EXPENSE RATIO
Ratio, in per cent, of other operating expenses to net premiums earned

FACULTATIVE REINSURANCE
A reinsurance risk that is placed by means of a separately negotiated contract as opposed to one that is ceded under a reinsurance treaty

FAL
Funds at Lloyd's

FCA
Financial Conduct Authority

FULLY CONVERTED BOOK VALUE PER SHARE (FCBVS)
Calculated based on the value of the total shareholders' equity attributable to the Group and dilutive restricted stock units as calculated under the treasury method, divided by the sum of all shares and dilutive restricted stock units, assuming all are exercised

FVTPL
Fair value through profit or loss

GROSS PREMIUMS WRITTEN
Amounts payable by the insured, excluding any taxes or duties levied on the premium, including any brokerage and commission deducted by intermediaries

THE GROUP OR THE LANCASHIRE GROUP
LHL and its subsidiaries

GSSA
Group Solvency Self-Assessment

ICAEW
Institute of Chartered Accountants of England and Wales

IFRS
International Financial Reporting Standard(s)

INCURRED BUT NOT REPORTED (IBNR)
These are anticipated or likely losses that may result from insured events which have taken place, but for which no losses have yet been reported. IBNR also includes a reserve for possible adverse development of previously reported losses

IRR
Internal rate of return

IRRC
Investment Risk and Return Committee

KHL
Kinesis Holdings I Limited

APPENDIX 1: GLOSSARY CONTINUED

KRL
Kinesis Reinsurance I Limited

LCM
Lancashire Capital Management

LHL (THE GROUP)
Lancashire Holdings Limited

LICL (THE COMPANY)
Lancashire Insurance Company Limited

LOC
Letter of credit

LOSSES
Demand by an insured for indemnity under an insurance contract

LTIP
Long term incentive plan

LSE
London Stock Exchange

LUK
Lancashire Insurance Company (UK) Limited

MBRT
Multi-beneficiary reinsurance trust

MSM
Minimum margin of solvency

NAV
Net asset value

NET ACQUISITION COST RATIO
Ratio, in per cent, of net acquisition expenses to net premiums earned

NET LOSS RATIO
Ratio, in per cent, of net insurance losses to net premiums earned

NET PREMIUMS WRITTEN
Net premiums written is equal to gross premiums written less outwards reinsurance premiums written

ORSA
Own Risk and Solvency Assessment

OTC
Over the counter

PML
Probable maximum loss. The Group's exposure to certain peak zone elemental losses

PRO-RATA/PROPORTIONAL
Reinsurance or insurance where the reinsurer or insurer shares a proportional part of the original premiums and losses of the reinsured or insured

QST
Quota Share Treaty

RDS
Realistic Disaster Scenarios

RPI
Renewal Price Index

RETROCESSION
The reinsurance of the reinsurance account

RMS
Risk Management Solutions

RRC
Risk and Return Committee

RSC
Reinsurance Security Committee

RSS
Restricted share scheme

SHARP
Lancashire's in house aggregation system

SYNDICATE 2010
Lloyd's Syndicate 2010 managed by CUL. The Group provides capital to support 59.7% of the stamp

SYNDICATE 3010
Lloyd's Syndicate 3010 managed by CUL. The Group provides capital to support 100.0% of the stamp

TOTAL SHAREHOLDER RETURN (TSR)
The IRR of the increase/(decrease) in share price in the period, measured in U.S. dollars, adjusted for dividends

TPS
Technical provisions

UMCC
Underwriting and Marketing Conference Call

UNEARNED PREMIUMS (UPR)
The portion of premium income that is attributable to periods after the balance sheet date is deferred and amortised to future accounting periods

UNL
Ultimate net loss

VAR
Value At Risk

Appendix 2: Key person biographies

PETER CLARKE – LHL NON-EXECUTIVE CHAIRMAN

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

MICHAEL DAWSON – LHL NON-EXECUTIVE DIRECTOR

Michael Dawson has more than 35 years' experience in the insurance industry, having started his career at Lloyd's in 1979. He joined Cox Insurance in 1986 where he was the Chief Executive from 1995 to 2002. In 1991, Mr Dawson formed and became the underwriter of Cox's and subsequently Chaucer's specialist nuclear syndicate 1176. Between 2005 and 2008 Mr Dawson was appointed Chief Executive of Goshawk Insurance Holdings PLC and its subsidiary Rosemont Re, a Bermuda reinsurer. Mr Dawson served on the Council of Lloyd's from 1998 to 2001 and on the Lloyd's Market Board from 1998 to 2002.

SIMON FRASER – LHL SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR

Simon Fraser was Head of Corporate Broking at Merrill Lynch and subsequently Bank of America Merrill Lynch until his retirement in 2011. He began his career in the City in 1986 with BZW and joined Merrill Lynch in 1997. He led initial public offerings, rights issues, placings, demergers and mergers and acquisitions transactions during his career and advised many UK companies on stock market and LSE issues. Mr Fraser has an MA degree in modern history from the University of St Andrews.

SAMANTHA HOE-RICHARDSON – LHL NON-EXECUTIVE DIRECTOR

Samantha Hoe-Richardson since 2014 has been Chair of the Audit Committee. Prior to this, she was Head of Environment & Sustainability for Network Rail and formerly Head of Environment for Anglo American plc, one of the world's leading mining and natural resources companies. She was also a director and founder of Anglo American Zimele Green Fund (Pty) Ltd, which supports entrepreneurs in South Africa. Prior to her role with Anglo American, Ms Hoe-Richardson worked in investment banking and audit and she holds a master's degree in nuclear and electrical engineering from the University of Cambridge. She also has a Chartered Accountancy qualification.

ROBERT LUSARDI – LHL NON-EXECUTIVE DIRECTOR

Robert Lusardi spent the first phase of his career as a senior investment banker specialising in the insurance and asset management industries. From 1998 until 2005 he was a member of the Executive Management Board of XL Group plc, first as Group CFO then as a segment CEO; from 2005 until 2010 he was an EVP of White Mountains (an insurance merchant bank) and CEO of certain subsidiaries; and from 2010 to 2015 he was CEO of PremieRe Holdings LLC (a private insurance entity). He has been a director of ten insurance-related entities. He received his BA and MA degrees in Engineering and Economics from Oxford University and his MBA from Harvard University.

SALLY WILLIAMS – LHL NON-EXECUTIVE DIRECTOR

Sally Williams has more than 30 years' experience in the financial services sector, with extensive risk, compliance and governance experience, having held senior positions with Marsh, National Australia Bank and Aviva. Ms Williams is a chartered accountant and spent the first 15 years of her career with PricewaterhouseCoopers, where she was a director specialising in financial services risk management and regulatory relationships. She also undertook a two-year secondment from PwC to the Supervision and Surveillance Department at the Bank of England.

ALEX MALONEY – LHL CHIEF EXECUTIVE OFFICER

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

NATALIE KERSHAW – LHL CHIEF FINANCIAL OFFICER

Natalie Kershaw joined Lancashire in December 2009 as the Group Financial Controller and has also held the positions of Chief Financial Officer of Lancashire Insurance Company Limited and Group Chief Accounting Officer. She has 20 years' experience of the insurance/reinsurance sector with previous roles at Swiss Re, ALAS (Bermuda) Ltd and PwC. Natalie graduated from Jesus College, Oxford University in 1996 with a first class degree in Geography and is a Fellow of the Institute of Chartered Accountants in England and Wales.

BEVERLEY TODD – LICL NON-EXECUTIVE CHAIRMAN

Beverley was appointed to the LICL Board in February 2016. Beverley has extensive experience of international insurance and reinsurance, specifically with JLT Insurance Management where she has held senior roles in Bermuda and Florida. In particular, she has a detailed knowledge of Bermuda's insurance regulatory framework which will be invaluable in her role as Chairman of the LICL Board of Directors. Beverley was educated in England and received her Bachelors of Arts in Business Administration (Honours) from South Bank University in London; Beverley is a member of the Chartered Institute of Management Accountants of England and Wales and brings with her significant insurance accounting expertise; she additionally holds the Associate in Risk Management (ARM) and the CPCU designations as well as the Institute of Directors Certificate in Company Direction.

APPENDIX 2: KEY PERSON BIOGRAPHIES CONTINUED

HAYLEY JOHNSTON – LICL CHIEF EXECUTIVE OFFICER

Hayley Johnston joined Lancashire in September 2007 as a member of the underwriting team. In May 2014 Hayley was appointed Chief Underwriting Officer for Lancashire Insurance Company (UK) Limited, in addition to her Outwards Reinsurance Manager role. Previously she was responsible for the underwriting of the Marine and Aviation accounts and from May 2011 acted as the Deputy Chief Underwriting Officer for Lancashire Insurance Company (UK) Limited. Hayley previously worked for Axis Specialty Europe where she was the Underwriting Manager and Outwards Reinsurance Manager for their European headquarters based in Dublin, Ireland. Hayley became CEO of Lancashire Insurance Company Limited in 2020.

JENNIFER WILSON – LICL CHIEF FINANCIAL OFFICER

Jennifer joined Lancashire in April 2010 and is the LICL Chief Financial Officer, in addition to the Head of Planning & Analysis for the Group. Jennifer previously worked as a consultant and spent much of her time from 2007 onwards providing consulting services to Lancashire. Jennifer graduated from the University of Alberta with a Bachelor of Commerce and gained her Chartered Accountancy qualification from the Institute of Chartered Accountants of Alberta. In 2018 she obtained a Certificate and Diploma in Company Direction from the Institute of Directors.

BENJAMIN READDY – GROUP CHIEF ACTUARY

Ben joined Lancashire in June 2010. Ben's role includes leading the capital modelling and reserving processes for the Lancashire Group and he is also involved in Group's ERM strategy and approach, and responsible for rating agency capital models & relationships. Prior to joining Lancashire, Ben was a Senior Manager in the PwC's actuarial consulting practice in Bermuda and before moving to Bermuda worked for PwC's actuarial practice in London. Prior to joining PwC in 2005, Ben spent five years at Lloyd's of London as a manager within the Franchise Performance Directorate. Ben is a Fellow of the Institute of Actuaries (FIA) and holds a BSc (Hons) degree in Mathematics from the University of Warwick.

JAMES IRVINE – CHIEF UNDERWRITING OFFICER

James joined Lancashire in April 2010 as a member of the underwriting team in London and transferred to the Bermuda office in 2011. He was appointed Deputy Chief Underwriting Officer for Lancashire Insurance Company Limited in September 2017 and became Chief Underwriting Officer in October 2018. James has helped to build the treaty reinsurance book at Lancashire and also worked on Lancashire's collateralised sidecars which were essentially a predecessor to the establishment of Kinesis. Prior to Lancashire, James worked at Guy Carpenter in London, working exclusively with US clients placing business into the London market. James is ARe qualified and holds an MA in Business Management from Durham Business School and a BA (Hons) degree in English Literature.

PAUL GREGORY – GROUP CHIEF UNDERWRITING OFFICER

Paul Gregory joined Lancashire in May 2007 as a member of the underwriting team and has led the underwriting operations for the Group since May 2014. On joining, Paul was responsible for underwriting the Energy account and assisting in the development of Lancashire Middle East. In January 2009, Paul was appointed Chief Underwriting Officer of Lancashire Insurance Company (UK) Limited and was responsible for all lines of business written from the Lancashire London office. Paul participated in the Marsh Graduate Scheme in 2001 as an Account Executive in the Energy Team which was followed by experience as an Underwriter in the Energy team at AIG in 2005. Paul has also worked closely with the Cathedral management team in the development of Syndicate 3010 and the Group's Lloyd's strategy.

JOHN CADMAN – GROUP GENERAL COUNSEL AND CHIEF EXECUTIVE OFFICER, LANCASHIRE INSURANCE COMPANY (UK) LIMITED

John Cadman joined Lancashire in March 2013. He is responsible for all legal issues affecting the group and is Chief Executive Officer of Lancashire Insurance Company (UK) Limited. Prior to joining Lancashire, John was a partner in the corporate department of CMS Cameron McKenna LLP, a City law firm, and between 1998 and 2007 was a partner at Barlow Lyde & Gilbert. John is an English qualified lawyer and qualified as a solicitor in 1990. John is an experienced corporate and transactional lawyer and advised numerous insurance and reinsurance entities on legal issues during his time in private practice.

CHRISTOPHER HEAD – GROUP COMPANY SECRETARY AND HEAD OF CORPORATE AFFAIRS

Christopher Head joined Lancashire in September 2010. He was appointed Company Secretary of Lancashire Holdings Limited in 2012 and advises on issues of corporate governance and generally on legal affairs for the Group. He also advises on the structuring of Lancashire's third-party capital underwriting initiatives which have included the Accordian and Kinesis facilities. Prior to joining Lancashire, he was in-house Counsel with the Imagine Insurance Group, advising specifically on the structuring of reinsurance transactions. He transferred to Max at Lloyd's in 2008 as Lloyd's and London Counsel. Between 1998 and 2006, Chris was Legal Counsel at KWELM Management Services Limited, where he managed an intensive programme of reinsurance arbitration and litigation for insolvent members of the HS Weavers underwriting pool. Chris is a UK Solicitor having worked until 1998 at Barlow Lyde and Gilbert in the Reinsurance and International Risk Team. Chris has a history MA and legal qualification from Cambridge University.

STEVE YEO – GROUP HEAD OF CLAIMS

Steve Yeo joined Lancashire in February 2008 and is responsible for providing Operational & Technical leadership and control of all Group claim activity as well as participating in the calculation and development of IBNR. Steve has extensive experience in the insurance industry having previously worked within the AIG Property & Energy Major Loss Team in London where he specialised in handling large, complex CAR and Operational losses across a wide range of offshore and onshore energy and commercial property risks.

SAMANTHA CHURCHILL – GROUP HEAD OF INTERNAL AUDIT

Samantha Churchill joined Lancashire in January 2019 and is the Group Head of Internal Audit. Prior to joining Lancashire Samantha spent 16 years in Insurance Internal Audit functions including Brit Insurance and RSA and most recently as Deputy Head of Internal Audit for Tokio Marine Kiln. Samantha qualified as a chartered accountant with PricewaterhouseCoopers within the financial services division and is a fellow of the ICAEW.

APPENDIX 2: KEY PERSON BIOGRAPHIES CONTINUED

DENISE O'DONOGHUE – GROUP CHIEF INVESTMENT OFFICER

Denise O'Donoghue joined Lancashire in June 2007 and is responsible for all aspects of the investment portfolio and treasury functions for the group. Denise is also a member of the Investment Committee. Prior to joining Lancashire, Denise was at Oil Insurance Limited managing the investment portfolio and heavily involved in all capital market transactions. Prior to Oil, Denise was at Zurich Investment Services, and obtained her CFA designation while working there.

LOUISE WELLS – GROUP CHIEF RISK OFFICER

Louise has been with Lancashire since September 2011 and is responsible for the Group's ERM function, having previously held the role of Head of Internal Audit. Prior to joining Lancashire, Louise spent almost 6 years at Lloyd's of London acting as Deputy Head of Internal Audit, Senior Risk Executive and Chief Risk Officer of Centrewrite. Louise has over 20 years audit and risk experience within the insurance market having worked in London, Sydney and Bermuda.

NICHOLAS NEBARD – GROUP ASSISTANT COMPANY SECRETARY AND MONEY LAUNDERING REPORTING OFFICER AND HEAD OF LICL COMPLIANCE

Nick joined Lancashire in February 2017 and is responsible for the Group's Bermuda compliance function. He has over 20 years of experience in the UK and Bermuda insurance markets. He spent the previous 8 years at XL Catlin where duties included the implementation and maintenance of the group's ERM framework at the local level across the Americas & Bermuda region and overseeing regulatory and operational compliance issues for XL Catlin's Bermuda operations. Prior to joining XL Catlin, Nick spent 8 years at the UK's Financial Services Authority in both supervisory and technical specialist roles within the insurance sector. He is ACII qualified, a certified member of the Institute of Risk Management and holds a BA (Hons) degree in Planning and Local Economic Development from Coventry University.