VALIDUS HOLDINGS LTD
Form 10-K
February 24, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014
Commission file number 001-33606
VALIDUS HOLDINGS, LTD.
(Exact name of registrant as specified in its charter)

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

29 Richmond Road, Pembroke, Bermuda HM 08
(Address of principal executive offices and zip code)
(441) 278-9000
(Registrant’s telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	Name of Each Exchange on Which Registered:
Common Shares, $0.175 par value per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No o
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No ý
Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant’s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2014 was $2,647.4 million computed upon the basis of the closing sales price of the Common Shares on June 30, 2014. For the purposes of this computation, shares held by directors and officers of the registrant have been excluded. Such exclusion is not intended, nor shall it be deemed, to be an admission that such persons are affiliates of the registrant.

As of February 20, 2015, there were 83,243,666 outstanding Common Shares, $0.175 par value per share, of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates information from certain portions of the registrant’s definitive proxy statement to be filed with the Securities and Exchange Commission within 120 days after the fiscal year ended December 31, 2014.

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

PART I

All amounts presented in this part are in thousands of U.S. dollars except as otherwise noted.

Item 1. Business

Overview

Validus Holdings, Ltd. was incorporated under the laws of Bermuda on October 19, 2005. Hereinafter, "the Company", "us" or "we" is used to describe any or all of Validus Holdings, Ltd. and its subsidiary companies. The Company conducts its operations worldwide through four operating segments which have been determined under U.S. GAAP segment reporting: Validus Re, AlphaCat, Talbot and Western World. Validus Re is a Bermuda-based reinsurance segment focused on short-tail lines of reinsurance. AlphaCat is a Bermuda-based investment adviser, managing capital from third parties and the Company in insurance linked securities and other investments in the property catastrophe reinsurance space. Talbot is a specialty insurance segment operating within the Lloyd's insurance market through Syndicate 1183. Western World is a specialty excess and surplus lines insurance segment operating within the U.S. commercial market.

We seek to establish ourselves as a leader in the global insurance and reinsurance markets. Our principal operating objective is to use our capital efficiently by underwriting primarily short-tail insurance and reinsurance contracts with superior risk and return characteristics. Our primary underwriting objective is to construct a portfolio of short-tail insurance and reinsurance contracts that maximizes our return on equity subject to prudent risk constraints on the amount of capital we expose to any single event. We manage our risks through a variety of means, including contract terms, portfolio selection, diversification criteria, including geographic diversification criteria, and proprietary and commercially available third-party vendor catastrophe models.

Since our formation in 2005, we have been able to achieve substantial success in the development of our business. Selected examples of our accomplishments are as follows:

- Raising approximately $1.0 billion of initial equity capital in December 2005 and underwriting $217.4 million in gross premiums written for the January 2006 renewal season;
- Building a risk analytics staff comprised of over 40 experts, many of whom have PhDs and Masters degrees in related fields;
- Developing Validus Capital Allocation and Pricing System (“VCAPS”), a proprietary computer-based system for modeling, pricing, allocating capital and analyzing catastrophe-exposed risks;
- Acquiring all of the outstanding shares of Talbot Holdings Ltd. on July 2, 2007;
- Completing an initial public offering (“IPO”) on July 30, 2007;
- Acquiring all of the outstanding shares of IPC Holdings Ltd. (“IPC”) on September 4, 2009;
- Raising $450.0 million of third party capital for PaCRe, Ltd. ("PaCRe") a Class 4 Bermuda reinsurer formed for the purpose of writing high excess property catastrophe reinsurance, on April 2, 2012 and a further $58.5 million on May 1, 2013;
- Acquiring all of the outstanding shares of Flagstone Reinsurance Holdings, S.A. ("Flagstone") on November 30, 2012;
- Acquiring all of the outstanding shares of Western World Insurance Group, Inc. ("Western World") on October 2, 2014;
- Successfully launching a series of sidecars beginning on May 25, 2011 and most recently, raising $127.0 million of third party capital for AlphaCat 2015, Ltd. ("AlphaCat 2015") on December 29, 2014; of which, $117.4 was funded as at December 31, 2014. The remaining commitment of $9.6 million will be called and deployed throughout 2015;
- Managing third party capital of $785.9 million for the AlphaCat Insurance Linked Securities ("ILS") funds as at December 31, 2014;

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- Delivering a 12.4% compounded annual growth in book value per diluted common share plus accumulated dividends from formation to December 31, 2014;
- Declaring a $2.00 special dividend per common share and per common share equivalent on February 6, 2013 and, on that same date, increasing the annual dividend by 20% from $1.00 to $1.20 per common share and per common share equivalent;
- Further increasing the annual dividend by an additional 6.7% from $1.20 to $1.28 per common share and per common share equivalent on February 3, 2015; and
- Repurchasing approximately 71.4 million common shares for an aggregate purchase price of approximately $2,284.8 million and paying an aggregate amount of $947.0 million in dividends from formation to February 20, 2015.

Our Operating Subsidiaries

The following chart shows how our Company and its principal subsidiaries operate:

For a complete list of the Company’s subsidiaries, see Exhibit 21.

(a) AlphaCat 2014 and AlphaCat 2015 are non-consolidated operating affiliates that are owned 19.6% and 20.0%, respectively, by the Company.
(b) One of the funds is consolidated and the remaining funds are owned 7.9%, 39.7% and 9.1% by the Company.
(c) The Company has an equity interest of 10% in PaCRe, the remaining 90% interest is held by third party investors.

Operating Segments
Validus Re: The Validus Re segment operates as a Bermuda-based provider of short-tail reinsurance products on a global basis. Validus Re concentrates on first-party property and other reinsurance risks commonly referred to as short-tail in nature due to the relatively brief period between the occurrence and payment of a claim.
Validus Reinsurance Ltd. was registered as a Class 4 insurer under The Insurance Act 1978 of Bermuda, amendments thereto and related regulations (the “Insurance Act”) in November 2005. It commenced operations with approximately $1.0 billion of equity capital and a balance sheet unencumbered by any historical losses relating to the 2005 hurricane season, the events of September 11, 2001, asbestos or other legacy exposures affecting our industry.
Validus Re entered the global reinsurance market in 2006 during a period of imbalance between the supply of underwriting capacity available for reinsurance on catastrophe-exposed property, marine and energy risks and demand for such reinsurance coverage.
On September 4, 2009, the Company acquired all of the outstanding shares of IPC. The primary lines in which IPC conducted business were property catastrophe reinsurance and, to a limited extent, property-per-risk excess, aviation (including satellite) and other short-tail reinsurance on a worldwide basis. For segmental reporting purposes, the results of IPC’s operations since the acquisition date have been included within the Validus Re segment in the Consolidated Financial Statements.
On November 30, 2012, the Company acquired all of the outstanding shares of Flagstone, strengthening the Company's leading property catastrophe reinsurance and short-tail specialty insurance platform. The primary lines in which Flagstone conducted business were property catastrophe reinsurance, property pro rata and per-risk excess and short-tail specialty and casualty reinsurance such as aviation, energy, personal accident and health, satellite, marine and workers' compensation catastrophe. For segmental reporting purposes, the results of Flagstone’s reinsurance operations since the acquisition date have been included within the Validus Re segment in the Consolidated Financial Statements. As part of this acquisition, the Company acquired Flagstone Reassurance Suisse, SA and renamed it Validus Reinsurance (Switzerland) Ltd ("Validus Re Swiss"). Validus Re Swiss is based in Zurich, Switzerland. Through this local presence, the Company is in a position to closely follow and respond effectively to the changing needs of the various European and Bermuda insurance markets. Validus Re Swiss is licensed by the Swiss Financial Market Supervisory Authority, or FINMA, in Switzerland. Validus Re Swiss is also licensed as a permit company in Bermuda under the Companies Act and is registered in Bermuda as a Class 4 insurer under the Insurance Act, operating through its Bermuda branch, which complements our Swiss-based underwriters with a separate Bermuda underwriting platform.
The following are the primary lines in which Validus Re conducts its business. Details of gross premiums written by line of business, are provided below:

(Dollars in thousands)	Year Ended December 31, 2014			Year Ended December 31, 2013			Year Ended December 31, 2012		
	Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)	
Property	$631,032	55.5	%	$744,630	59.9	%	$771,617	68.2	%
Marine	190,959	16.8	%	194,001	15.6	%	257,469	22.7	%
Specialty	314,919	27.7	%	303,891	24.5	%	102,873	9.1	%
Total	$1,136,910	100.0	%	$1,242,522	100.0	%	$1,131,959	100.0	%

Property: Validus Re underwrites property catastrophe reinsurance, property per risk reinsurance and property pro rata reinsurance.
Property catastrophe: Property catastrophe reinsurance provides reinsurance for insurance companies’ exposures to an accumulation of property and related losses from separate policies, typically relating to natural disasters or other catastrophic events. Property catastrophe reinsurance is generally written on an excess of loss basis, which provides coverage to insurance companies when aggregate claims and claim expenses from a single occurrence for a covered peril exceed a certain amount specified in a particular contract. Under these contracts, the Company provides protection to an insurer for a portion of the total losses in excess of a specified loss amount, normally up to a

maximum amount per loss and/or an aggregate amount across multiple losses, as specified in the contract. In the event of a loss, most contracts provide for coverage of a second occurrence following the payment of a premium to reinstate the coverage under the contract, which is referred to as a reinstatement premium. The coverage provided under excess of loss reinsurance contracts may be on a worldwide basis or limited in scope to specific regions or geographical areas. Coverage can also vary from “all property” perils, which is the most expansive form of coverage, to more limited coverage of specified perils such as windstorm-only coverage. Property catastrophe reinsurance contracts are typically “all risk” in nature, providing protection against losses from earthquakes and hurricanes, as well as other natural and man-made catastrophes such as floods, tornadoes, fires and storms. The predominant exposures covered are losses stemming from property damage and business interruption coverage resulting from a covered peril. Certain risks, such as war or nuclear contamination may be excluded, partially or wholly, from certain contracts. Gross premiums written on property catastrophe business during the year ended December 31, 2014 were $513.4 million.

Property per risk: Property per risk reinsurance provides reinsurance for insurance companies' excess retention on individual property and related risks, such as highly-valued buildings. Per risk reinsurance protects insurance companies on their primary insurance risks on a "single risk" basis. A "risk" in this context might mean the insurance coverage on one building or a group of buildings or the insurance coverage under a single policy which the reinsured treats as a single risk. Coverage is usually triggered by a large loss sustained by an individual risk rather than by smaller losses which fall below the specified retention of the reinsurance contract. Such property per risk coverages are generally written on an excess of loss basis, which provides the reinsured with protection beyond a specified amount up to the limit set within the reinsurance contract. Gross premiums written on property per risk business during the year ended December 31, 2014 were $27.5 million.

Property pro rata: Property pro rata contracts require that the reinsurer share the premiums as well as the losses and loss expenses in an agreed proportion with the cedant. Gross premiums written on property pro rata business during the year ended December 31, 2014 were $90.2 million.

Marine: Validus Re underwrites reinsurance on marine risks covering damage to or losses of marine vessels and cargo, third-party liability for marine accidents and physical loss and liability from principally offshore energy properties. Validus Re underwrites marine on an excess of loss basis and on a pro rata basis. Gross premiums written on marine business during the year ended December 31, 2014 were $191.0 million.

Specialty: Validus Re underwrites other lines of business depending on an evaluation of pricing and market conditions, which include aerospace and aviation, agriculture, financial, terrorism, life, accident and health, nuclear, workers' compensation, crisis management, contingency, motor, technical, composite and trade credit lines. The Company seeks to underwrite specialty lines with very limited exposure correlation with its property, marine and energy portfolios. With the exception of the aerospace and aviation, agriculture, financial and trade credit lines of business, which have a meaningful portion of its gross premiums written volume on a proportional basis, the Company's other specialty lines are written on an excess of loss basis. Gross premiums written on specialty business during the year ended December 31, 2014 were $314.9 million.

AlphaCat: AlphaCat Managers, Ltd. ("AlphaCat Managers") is an asset manager which has strategic relationships that leverage the Company's underwriting and investment expertise. As an asset manager, AlphaCat Managers' primary source of income is earned through management, performance and underwriting fees.

The AlphaCat segment is a core element within the Company's strategic initiative to expand into capital market activities by participating in the market for ILS. ILS are financial instruments whose fundamental value is determined by insurance losses caused by natural catastrophes such as major earthquakes and hurricanes. As the returns on ILS are primarily driven by natural catastrophes, when carefully structured, they are generally uncorrelated with the overall financial markets, making ILS an attractive asset class for capital market investors.

AlphaCat invests in private reinsurance transactions, as well as catastrophe bonds, a common type of ILS issued by insurance and reinsurance companies. AlphaCat leverages the Company's extensive business sourcing, underwriting, research and analytic capabilities to construct ILS portfolios subject to prudent risk constraints.

AlphaCat investors access this uncorrelated asset class through various funds and sidecars that participate in the market via AlphaCat Reinsurance Ltd. ("AlphaCat Re"), a Bermuda provider of fully collateralized property catastrophe reinsurance and retrocession capacity and AlphaCat Master Fund Ltd. ("AlphaCat Master Fund"), a Bermuda investment fund investing in reinsurance related capital markets transactions.

The various funds and sidecars are included in the results of the AlphaCat segment through either consolidation or as income from operating affiliates, depending on the assessment of accounting treatment under the appropriate U.S. GAAP guidance. The results of PaCRe are consolidated in the AlphaCat segment with the offsetting 90% third party ownership accounted for within noncontrolling interest.

During the first quarter of 2012, to better align the Company's operating and reporting structure with its strategy, there was a change in the Company's segment structure. This change included reporting the AlphaCat group of companies as a separate operating segment. The AlphaCat segment currently includes AlphaCat Re 2011 Ltd. ("AlphaCat Re 2011") (off-risk), AlphaCat Re 2012 Ltd. ("AlphaCat Re 2012") (off-risk), AlphaCat 2013, Ltd. ("AlphaCat 2013") (off-risk), AlphaCat 2014, Ltd. ("AlphaCat 2014"), AlphaCat 2015, Ltd. ("AlphaCat 2015"), PaCRe, the AlphaCat ILS funds and the BetaCat ILS funds.

The following are the primary financial indicators for the AlphaCat segment:

(Dollars in thousands)	Year ended December 31, 2014	Change	2013	Change	2012
Managed gross premiums written	$135,181	(7,965)	$143,146	(4,945)	$148,091
Other insurance related income	27,122	698	26,424	3,195	23,229
Income from operating affiliates	17,723	3,434	14,289	1,709	12,580

Managed gross premiums written: Managed gross premiums written includes gross premiums written by our non-consolidated affiliates, AlphaCat Re 2011 and AlphaCat Re 2012. A reconciliation of managed gross premiums written to gross premiums written, the most comparable U.S. GAAP financial measure, is presented in the section entitled "Non-GAAP Financial Measures." Managed gross premiums written for the year ended December 31, 2014 were $135.2 million.

Other insurance related income: Other insurance related income primarily includes third party and related party management and performance fee income. Other insurance related income for the year ended December 31, 2014 was $27.1 million.

Income from operating affiliates: Income from operating affiliates includes income from our non-consolidated operating affiliates accounted for as equity method investments. At December 31, 2014, AlphaCat's non-consolidated operating affiliates were AlphaCat Re 2011, AlphaCat Re 2012, AlphaCat 2013, AlphaCat 2014, AlphaCat 2015 and three of the AlphaCat ILS funds. For further details on the operating affiliates, refer to Note 9 "Investments in affiliates" to the Consolidated Financial Statements in Part II, Item 8. Income from operating affiliates for the year ended December 31, 2014 was $17.7 million.

(Dollars in thousands)	Assets Under Management As at December 31, 2014	As at December 31, 2013
Related party	$346,907	$392,384
Third party	1,533,840	1,204,562
Total	$1,880,747	$1,596,946

Assets under management: Assets under management ("AUM") represents total assets managed by AlphaCat Managers on behalf of related and third party investors. AUM includes the assets of AlphaCat Re 2011, AlphaCat Re 2012, AlphaCat 2013, AlphaCat 2014, AlphaCat 2015, PaCRe, the AlphaCat ILS funds and the BetaCat ILS funds. AUM as at December 31, 2014 was $1.9 billion.

Talbot: On July 2, 2007, the Company acquired all of the outstanding shares of Talbot Holdings Ltd. Talbot Holdings Ltd. is the Bermuda parent of a specialty insurance group primarily operating within the Lloyd’s insurance market through Syndicate 1183. The acquisition provided the Company with significant benefits in terms of product line and geographic diversification as well as offering the Company broader access to underwriting expertise. Similar to Validus Re, Talbot writes primarily short-tail lines of business but, as a complement to Validus Re, focuses mostly on insurance, as opposed to reinsurance risks, and on specialty lines where Validus Re currently has limited or no presence (e.g., war, financial institutions, contingency and accident and health). In addition, Talbot provides the Company with access to the Lloyd’s marketplace where Validus Re does not operate. As a London-based insurer, Talbot also writes the majority of its premiums on risks outside the United States. Talbot’s team of underwriters have, in many cases, spent most of their careers writing niche, short-tail business and bring their expertise to bear on expanding the Company’s short-tail insurance franchise.

The Company has expanded and diversified its business through Syndicate 1183’s access to Lloyd’s license agreements with regulators around the world. Talbot Underwriting Risk Services Ltd. (London), Talbot Underwriting Services, (U.S.) Ltd. (New York), Talbot Underwriting (MENA) Ltd. (Dubai), Validus Reaseguros, Inc. (Miami), Validus Re Chile S.A. (Chile), Talbot Risk Services (Labuan) Pte Limited (Malaysia), and Talbot Risk Services Pte, Ltd. (Singapore and Australia), act as approved Lloyd’s coverholders for Syndicate 1183.

The following are the primary lines in which Talbot conducts its business. Details of gross premiums written by line of business are provided below:

(Dollars in thousands)	Year Ended December 31, 2014		Year Ended December 31, 2013		Year Ended December 31, 2012	
	Gross Premiums Written	Gross Premiums Written (%)	Gross Premiums Written	Gross Premiums Written (%)	Gross Premiums Written	Gross Premiums Written (%)
Property	$337,210	30.6 %	$345,831	31.7 %	$324,910	30.1 %
Marine	392,701	35.6 %	381,238	34.9 %	396,207	36.7 %
Specialty	371,859	33.8 %	364,821	33.4 %	357,519	33.2 %
Total	$1,101,770	100.0 %	$1,091,890	100.0 %	$1,078,636	100.0 %

Property: The main sub-classes within the property class are International and North American direct and facultative contracts, lineslips and binding authorities, together with a book of business written on a treaty reinsurance basis. The business written is mostly commercial and industrial insurance. Coverage provided includes all risks of direct physical loss or damage, business interruption and natural catastrophe perils. Property also includes onshore energy and construction business. Within the onshore energy sector, covered occupancies include oil, gas, petrochemicals, chemical, power generation and utilities and process industries. Coverage is typically all risks and includes machinery breakdown and business interruption where required. The primary focus within the construction line is on major capital projects, placed on a direct or facultative subscription basis. The business is mainly short-tail with premiums for reinsurance and direct and facultative business, substantially earned within 12 months and premiums for lineslips and binding authorities mainly earned within 12 months of the expiry of the contract, however there are a minority of risks with long-term policies. Gross premiums written on property business during the year ended December 31, 2014 were $337.2 million, including $55.2 million of treaty reinsurance.

Marine: The main types of business within the marine class are hull, cargo, offshore energy, marine and energy liabilities, yachts and a book of business written on a treaty reinsurance basis. Hull consists primarily of ocean going vessels and covers worldwide risks on an all risks or total loss only basis. Cargo consists of worldwide transits with a particular emphasis on oil cargo, project cargo, pre-launch satellite and space risks, specie, fine art and high value motor vehicles. Offshore energy covers a variety of oil and gas industry exploration and production risks. The marine and energy liability account provides cover for protection and indemnity clubs and a wide range of companies operating in the marine and energy sectors. Most business written is short-tail, enabling a quicker and more accurate picture of expected profitability than is the case for long-tail business. The marine and energy liability account, which makes up $59.8 million of the $392.7 million of gross premiums written during the year ended December 31, 2014, is the primary long-tail business in this class.

Specialty: This class consists of war (comprising marine & aviation war, political risks and political violence, including war on land), financial institutions, contingency, accident and health, aviation direct and aviation treaty. With the exception of aviation treaty, most of the business within the specialty class is written on a direct or facultative basis or under a binding authority through a coverholder. Gross premiums written on the specialty business during the year ended December 31, 2014 were $371.9 million.

War: The marine and aviation war account covers physical damage to aircraft and marine vessels caused by acts of war and terrorism. The political risk account deals primarily with expropriation, contract frustration/trade credit, kidnap and ransom, and malicious and accidental product tamper. The political violence account mainly insures physical loss to property or goods anywhere in the world, caused by war, terrorism or civil unrest. This class is often written in conjunction with cargo, specie, property, energy, contingency and political risk. The period of the risks can extend up to 36 months and beyond. Gross premiums written on war business during the year ended December 31, 2014 were $189.7 million.

Aviation: The aviation account insures major airlines, airport operations, aviation products and airports, general aviation, satellites and a book of business written on a treaty reinsurance basis. The coverage includes excess of loss treaties with medium to high attachment points. Gross premiums written on aviation business during the year ended December 31, 2014 were $93.5 million.

Financial Institutions: Talbot’s financial institutions team underwrites bankers blanket bond, commercial crime, computer crime, professional indemnity and directors’ and officers’ coverage for various types of financial institutions and similar companies. The team also provides professional indemnity and directors' and officers' coverage to a more general selection of clients. Bankers blanket bond and commercial crime insurance products are specifically designed to protect against direct financial loss caused by fraud/criminal actions and mitigate the damage such activities may have on the asset base of the insured. Computer crime insurance protects against the misappropriation of funds and assets via the insured's computer system. Professional indemnity insurance protects businesses in the event that legal action is taken against them by third parties claiming professional negligence. Directors’ and officers' insurance protects directors and officers against personal liability for losses incurred by a third party due to negligent performance by a director or officer. The financial institutions account is longer tail business as the periods of time between the occurrence, reporting and settlement of claims can be several years. Gross premiums written on financial institutions business for the year ended December 31, 2014 were $40.3 million.

Accident and Health: The accident and health account provides insurance in respect of individuals in both their personal and business activity together with corporations where they have an insurable interest relating to death or disability of employees or those under contract. Gross premiums written on accident and health business during the year ended December 31, 2014 were $26.4 million.

Contingency: The main types of covers written under the contingency account are event cancellation, non-appearance and prize indemnity business. Gross premiums written on contingency business during the year ended December 31, 2014 were $21.9 million.

Western World: On October 2, 2014, the Company acquired all of the outstanding shares of Western World, a U.S. based specialty excess and surplus lines insurance company. The acquisition provided the Company with enhanced access to the specialty U.S. commercial insurance market, the world's largest short-tail market, complementing the Company's existing market positions in both Bermuda reinsurance and the Lloyd's marketplace and increasing the Company's ability to leverage operational strengths in short-tail classes of business. In addition, the acquisition improves the Company's ability to manage (re)insurance cycles.

Western World primarily insures small to medium size commercial and institutional risks covering general liability, professional liability, products liability, miscellaneous malpractice and property classes through three wholly owned insurance subsidiaries: Western World Insurance Company ("WWIC"), Tudor Insurance Company ("Tudor") and Stratford Insurance Company ("Stratford"). WWIC, Tudor and Stratford are domiciled in New Hampshire. WWIC operates as a surplus lines insurer in all other jurisdictions. Tudor is licensed as a domestic surplus lines insurer in New Hampshire and is authorized to conduct business as a surplus lines insurer in all other jurisdictions. Stratford operates as an admitted insurer in 49 jurisdictions.

The following are the primary lines in which Western World conducts its business. Details of gross premiums written by line of business are provided below:

	Year Ended December 31, 2014 (a)		
(Dollars in thousands)	Gross Premiums Written	Gross Premiums Written (%)	
Property	$9,983	15.3	%
Liability	55,252	84.7	%
Total	$65,235	100.0	%

(a) The results of Western World have been included in the Company's consolidated results from the October 2, 2014 date of acquisition.

Property: This class consists of habitational and mercantile risks and is primarily offered on a package basis with the liability coverage. Gross premiums written on property business during the year ended December 31, 2014 were $10.0 million.

Liability: This class consists of occurrence-based coverage for contractors, dwellings, special events, manufacturers, social workers, drug clinics and exercise and health facilities. Coverage is also provided on a claims-made basis for lines such as directors' and officers', and errors and omissions liability. Gross premiums written on the liability business during the year ended December 31, 2014 were $55.3 million.

Enterprise Risk Management

Risk Management Framework: The Company believes in having a culture that embraces sound risk management practices at all levels of the organization. We have therefore implemented an Enterprise Risk Management ("ERM") framework (the "Framework") that is aligned with the Company's culture and responds to the needs of the business. The Framework has been established to identify, assess, quantify and manage risks and opportunities. In particular it is designed to:

- Establish the principles by which the Company can evaluate the risk/reward trade-offs associated with key strategic and tactical decisions.
- Establish a risk governance structure that, in respect of all activities related to ERM, operates with clearly defines roles and responsibilities.
- Establish minimum requirements that must be met by each of the Company's segments.
- Identify and assess all risks and causes of risks arising out of the Company's strategic initiatives, internal processes, and external environment.
- Establish a set of responses to manage the Company's risks within its stated risk appetite and risk tolerances.
- Establish procedures through which near-miss and actual incidents, that either have the potential to impact or have impacted the Company, are reported and reviewed in order to inform the risk identification and assessment process.

Risk Governance: Our risk governance philosophy reflects the overall governance of the Company, with the segments given broad autonomy over the management of their business, while adhering to the overall strategy of the Company. Similarly, the segments have broad operational latitude over their risk management functions while staying within the parameters set by the Company.

Our risk governance structure has the flexibility to allow integration of Western World into the Company while taking into account their long history, work culture and risk practices. Western World's existing risk management is complemented by our experience in implementing the Company's risk framework. We will leverage our regulatory experience in Bermuda and London to facilitate Western World's compliance with the U.S. Own Risk Solvency Assessment ("ORSA") requirements.

The Company's Board of Directors has established a separate Risk Committee ("RC") that is governed by a charter which is updated and reviewed periodically by the Board of Directors. The RC is responsible for, among other things, approving the Framework, working with management to ensure ongoing, effective implementation of the Framework and reviewing the Company's specific risk limits as defined in the Framework, including limits related to major categories of risk. The implementation of risk policies and oversight of risk management is the responsibility of the Group Risk Management Committee ("GRMC"). The GRMC reports to the RC and is governed by a charter that is reviewed and approved annually by the RC. The GRMC also has two subcommittees, the Model Risk Subcommittee and the Operational Risk Subcommittee, both of which are governed by charters that are reviewed annually by the RC. Various risk policies are in place to facilitate consistent risk assessment across the Company and to ensure that strategic business decisions are supported by effective modeling and analysis.

Risk Appetite: The Company's risk appetite is expressed through a series of qualitative and quantitative statements, principles, limits, and tolerances that, in the aggregate, convey the Company's risk and reward preferences and set the risk parameters within which the Company and its segments operate. The risk appetite is proposed by management and approved by the Board of Directors.

The significant quantitative measures include meeting minimum returns on capital and risk-adjusted capital over a full insurance industry cycle, managing the probability of break-even or better and meeting or exceeding budgeted net income over a calendar year, and managing the probability of losing specified percentages of shareholders' equity in a calendar year. They also include probability thresholds in respect of maintaining a buffer above regulatory and rating agency capital levels.

The Company also sets levels of concentration risks within its risk appetite, including those related to probable maximum losses, zonal aggregates and the contribution of various risk categories to the overall assessment of the Company's risk capital.

Risk Classification: Risks are broadly divided into those that the Company assumes explicitly and from which it derives income and those that are a by-product of the operating and business environment, from which the Company does not earn income.

The risks assumed are categorized as catastrophe, reserve and premium risks (also together referred to as insurance risk), market (or investment) risk and credit risk. The Company’s goal is to get adequately compensated for these risks, while creating optimal insurance and investment portfolios subject to the constraints of the Company’s risk appetite. The remaining risks are categorized as operational and strategic risks, which typically include emerging risks, for which the Company’s goal is to identify, assess and mitigate to the extent considered appropriate.

Risk Ownership: The Company's risk management philosophy is to entrust risk identification and control activities with the employees who have the responsibility for and expertise in the areas giving rise to each risk. This not only creates workflow efficiencies but also promotes awareness of and accountability for risk at all levels of the Company. As such, primary risk ownership is assigned to the managers of functional areas. The risk identification and control activities are embedded in the job descriptions of risk owners and control operators and monitored by the GRMC.

Risk Assessment, Control and Mitigation: The Company performs a regular risk assessment process that considers the likelihood and impact of causes of risk, both before and after the existence of relevant controls. The approaches used to identify and update causes of risk include scenario building, incident and near-miss reporting and market intelligence. Controls have been established to appropriately manage the likelihood and impact of risks, focused on those with the most significance and after considering the tolerance level established for each risk. New controls may also be designed as a result of the incident reporting process.

The Company also has in place policies, including underwriting, investment, and credit policies, to manage the assumption of risk. These policies provide for the Company's risk limits, tolerance levels and other guidelines, as well as the processes for ensuring compliance with the desired risk profile of the Company. The Company has at its disposal a variety of risk mitigation tools, including the purchase of reinsurance and retrocessional coverage, which it uses to ensure that its risk profile stays within prescribed limits and tolerance levels.

Exposure Management: In order to manage the assumption of insurance risk, the Company has established risk limits through both qualitative and quantitative considerations, including factors such as market share, history of and expertise in a class of business or jurisdiction, transparency and symmetry of available information, reliability of pricing models and availability and cost of reinsurance. These limits are reviewed at least annually and aligned to the overall risk appetite established by the Company's Board of Directors. In addition, a group exposure management policy is in place to ensure appropriate and consistent risk assessment and aggregation of exposures that accumulate between the operating companies in the group.

Three tools are used to measure and manage exposures:

- Absolute maximum limits - these are defined based on the underlying peril or coverage and include measures such as zonal aggregates, which convey the maximum contractual loss exposure.
- Probable maximum loss - these are defined where probabilistic event sets exist for underlying perils and are established for most natural catastrophe, aviation and offshore energy coverage, and conveys an extreme but likely loss exposure.
- Realistic disaster scenarios ("RDSs") - these are either prescribed by third parties or developed internally and convey a more intuitive view of potential loss outcome.

The Company will often use multiple tools to validate its exposure measurement and ensures that at least one of these tools is available for each class of business.

Model Validation Framework: The Company relies extensively on a wide range of models to support key decisions made across the business. We have therefore implemented a Model Validation Framework to establish a uniform set of validation and governance standards that ensure the quality and reliability of key models across the Company.

Portfolio Optimization: The Company has developed a comprehensive and integrated Economic Capital Model ("ECM") framework to facilitate the consistent assessment of risk, including risks classified as operational. This framework includes assessment at the individual operating company level, as well as across the Company. Using the ECM framework, the Company is able to assess the impact on risk appetite metrics of key strategic and tactical decisions as well as the risk return trade-offs associated with these decisions, including growth strategy, new product launch, business mix and retrocession strategy, mergers and acquisitions, planning and budgeting, investment strategy and capital management.

It is the goal of the Company to make the most efficient use of its capital and to achieve an adequate return for its shareholders. To that end, the Company seeks to maximize net income given the amount of capital at risk and subject to the risk limits, tolerance levels and other constraints that are imposed by our business, regulatory, and rating agency environments. The Company has therefore put in place portfolio optimization procedures, including the integrated use of the ECM within the annual planning process, in order to help shape portfolios that optimize their respective risk return profiles.

Underwriting Risk Management

The Company's underwriters manage risk by paying close attention to a number of qualitative and quantitative indicators. Our in-house pricing platform, VCAPS, provides reinsurance underwriters with a real-time view of the risk-adjusted profitability of each account. This allows them to examine the effects of contract terms and conditions as well as analyze the contribution of a contract to our overall risk capital and its impact on the projected incurred loss for one of our key stress scenarios. In addition, Talbot maintains a suite of pricing models for the direct and facultative underwriting teams that includes VCAPS and other proprietary models, as well as models licensed from third parties. The Company believes that giving our underwriters the tools to make sound decisions at every turn is critical to our long-term success. To that end, we strive to create an environment that promotes close cooperation between our underwriting, catastrophe modeling, risk, claims, and actuarial functions.

All of the Company’s underwriters adhere to a strict set of underwriting guidelines and letters of authority that specifically address the limits of their underwriting authority and their referral criteria. The Company’s current underwriting guidelines and letters of authority include:

- lines of business that a particular underwriter is authorized to write;
- exposure limits by line of business;
- contractual exposures and limits requiring mandatory referrals; and
- levels of analysis to be performed by lines of business.

In general, our underwriting approach is to:

- seek high quality clients who have demonstrated superior performance over an extended period;
- evaluate our clients’ exposures and make adjustments where their exposure is not adequately reflected;
- apply the comprehensive knowledge and experience of our entire underwriting team to make progressive and cohesive decisions about the business they underwrite; and
- employ our well-founded and carefully maintained market contacts within the Company to enhance our robust distribution capabilities.

Our underwriters have the responsibility to analyze all submissions and determine if the related potential exposures meet with both the Company’s risk profile line size and aggregate limitations, in line with the business plan. In order to ensure compliance, we run appropriate management information reports and all lines are subject to regular audits.

All of the companies managed by AlphaCat are subject to investment or underwriting guidelines. These guidelines are established in the offering documentation of each AlphaCat company. AlphaCat manages investment portfolios in accordance with guidelines, which are subject to oversight by the respective company's board of directors. AlphaCat leverages the Company's underwriting and analytical resources. However, all investment and underwriting decisions are ultimately made by AlphaCat. When services are provided to AlphaCat by the Company's underwriting teams, the relevant underwriting risk management framework outlined in this section applies.

Use of Models

A pivotal factor in determining whether to found and fund the Company was the opportunity for differentiation based upon superior risk management expertise; specifically, managing catastrophe risk and optimizing our portfolio to generate attractive returns on capital while controlling our exposure to risk, and assembling a management team with the experience and expertise to do so. The Company’s proprietary models are current with emerging scientific trends. This has enabled the Company to gain a competitive advantage over those reinsurers who rely exclusively on commercial models for pricing and portfolio management. The Company has made a significant investment in expertise in the risk modeling area to capitalize on this opportunity. The Company has assembled an experienced group of professional experts who operate in an environment designed to allow them to use their expertise as a competitive advantage. While the Company uses both proprietary and commercial probabilistic models, catastrophe risk is ultimately subject to absolute aggregate limitations as discussed above.

Commercial Vendor Models: The Company licenses two major commercial vendor models (RMS and AIR) to assess the adequacy of risk pricing and to monitor its overall exposure to risk in correlated geographic zones. The vendor models enable the Company to aggregate exposures by correlated event loss scenarios, which are probability-weighted. This enables the generation of exceedance probability curves for the portfolio and major geographic areas. Once exposures are modeled using one of the vendor models, the other model is used as both a reasonability check and as validation of the loss scenarios developed and reported by the first. The two commercial models each have unique strengths and weaknesses. For example, it is sometimes necessary to impose changes to frequency and severity.

The Company also uses its quantitative expertise to improve the reliability of the vendor model outputs and expedite scientific review and operationalization of their findings to formulate its view of risk in the following areas:

- Ceding companies may often report insufficient data and many reinsurers may not be sufficiently critical in their analysis of this data. The Company generally scrutinizes data for anomalies that may indicate insufficient data quality. These circumstances are addressed by either declining the program or, if the variances are manageable, by modifying the model inputs and outputs and pricing to reflect insufficient data quality;
- Performing independent checks on the accuracy of reported building characteristics through third-party tools;
- Prior to making overall adjustments for changes in climate variables, other variables are carefully examined (for example, demand surge, storm surge, and secondary uncertainty); and
- To properly quantify risk, we frequently adjust vendor models in advance of their updates based on the latest scientific studies and claims data.

In addition, many risks, such as second-event covers, aggregate excess of loss, or attritional loss components, cannot be fully evaluated using the vendor models. In order to better evaluate and price these risks, the Company has developed proprietary analytical tools, such as VCAPS and other models and data sets.

Proprietary Models: In addition to making frequency and severity adjustments to the vendor model outputs, the Company has implemented a proprietary pricing and risk management tool, VCAPS, to assist in pricing submissions and monitoring risk aggregation.

To supplement the analysis performed using vendor models, VCAPS uses the gross loss output of catastrophe models to generate a 100,000-year simulation set, which is used for both pricing and risk management. This approach allows more precise measurement and pricing of exposures. The two primary benefits of this approach are:

- VCAPS takes into account annual limits, event/franchise/annual aggregate deductibles, and reinstatement premiums. This allows for more accurate evaluation of treaties with a broad range of features, including both common (reinstatement premium and annual limits) and complex features (second or third event coverage, aggregate excess of loss, attritional loss components, covers with varying attachment across different geographical zones or lines of businesses and covers with complicated structures); and
- VCAPS use of 100,000-year simulations enables robust pricing of catastrophe-exposed business. This is possible in real-time operation because the Company has designed a computing hardware platform and software environment to accommodate the significant computing needs.

In addition to VCAPS, the Company uses other proprietary models and other data in evaluating exposures. The Company cannot assure that the models and assumptions used by the software will accurately predict losses. Further, the Company cannot assure that the software is free of defects in the modeling logic or in the software code. In addition, the Company has not been granted copyright or other legal protection for VCAPS.

Geographic Diversification

The Company actively manages its aggregate exposures by geographic or risk zone to maintain a balanced and diverse portfolio of underlying risks. The coverage the Company is willing to provide for any risk located in a particular zone is limited to a predetermined level, thus limiting the net aggregate loss exposure from all contracts covering risks believed to be located in any zone. Contracts that have “worldwide” territorial limits have exposures in several geographic zones. Generally, if a proposed contract would cause the limit to be exceeded, the contract would be declined, regardless of its desirability, unless the Company buys reinsurance or retrocessional coverage, thereby reducing the net aggregate exposure to the maximum limit permitted or less.

The following table sets forth the gross premiums written allocated to the territory of coverage exposure:

	Year Ended December 31, 2014 Gross Premiums Written						
(Dollars in thousands)	Validus Re	AlphaCat	Talbot	Western World (d)	Eliminations	Total	%
United States	$442,314	$30,987	$108,458	$65,235	$(11,026)	$635,968	27.0 %
Worldwide excluding United States (a)	76,129	7,331	139,570	—	(1,334)	221,696	9.4 %
Australia and New Zealand	20,257	1,019	9,736	—	—	31,012	1.3 %
Europe	58,236	3,005	45,615	—	(2,305)	104,551	4.4 %
Latin America and Caribbean	54,053	—	116,281	—	(23,958)	146,376	6.2 %
Japan	43,310	608	4,116	—	(608)	47,426	2.0 %
Canada	3,670	215	10,194	—	(214)	13,865	0.6 %
Rest of the world (b)	21,467	—	93,012	—	—	114,479	4.8 %
Sub-total, non United States	277,122	12,178	418,524	—	(28,419)	679,405	28.7 %
Worldwide including United States (a)	179,564	92,016	96,187	—	(22,463)	345,304	14.6 %
Other locations non-specific (c)	237,910	—	478,601	—	(13,902)	702,609	29.7 %
Total	$1,136,910	$135,181	$1,101,770	$65,235	$(75,810)	$2,363,286	100.0 %

(a) Represents risks in two or more geographic zones.

(b) Represents risk in one geographic zone.

(c) The other locations non-specific category refers to business for which an analysis of exposure by geographic zone is not applicable, such as marine and aerospace risks, since these exposures can span multiple geographic areas and, in some instances, are not fixed locations.

(d) The results of Western World have been included in the Company's consolidated results from the October 2, 2014 date of acquisition.

The effectiveness of geographic zone limits in managing risk exposure depends on the degree to which an actual event is confined to the zone in question and on the Company’s ability to determine the actual location of the risks believed to be covered under a particular insurance or reinsurance contract. Accordingly, there can be no assurance that risk exposure in any particular zone will not exceed that zone’s limits. Further control over diversification is achieved through guidelines covering the types and amount of business written in product classes and lines within a class.

Reinsurance Management

The Company enters into reinsurance agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks and enable it to underwrite policies with higher limits. The ceding of the insurance risk does not legally discharge the Company from its primary liability for the full amount of the policies, and the Company is therefore required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance agreement.

Validus Re Retrocession: Validus Re monitors the opportunity to purchase retrocessional coverage on a continual basis and employs the VCAPS modeling system to evaluate the effectiveness of risk mitigation and exposure management relative to the cost. This coverage may be purchased on an indemnity basis as well as on an index basis (e.g., industry loss warranties ("ILWs")). Validus Re also considers and at times uses alternative retrocessional structures, including collateralized quota share facilities ("sidecars") and other capital markets products (e.g., catastrophe bonds), where the pricing and terms are attractive.

When Validus Re buys retrocessional coverage on an indemnity basis, payment is for an agreed upon portion of the losses actually suffered. In contrast, when Validus Re buys an ILW cover, which is a reinsurance contract in which the payout is dependent on both the insured loss of the policy purchaser and the measure of the industry-wide loss, payment is made only if both Validus Re and the industry suffer a loss, as reported by one of a number of independent agencies, in excess of specified threshold amounts. With an ILW, Validus Re bears the risk of suffering a loss while receiving no payment under the ILW if the industry loss was less than the specified threshold amount.

AlphaCat: AlphaCat has ceded only a minimal level of business to third parties and will typically write contracts on a net retention basis only.

Talbot Ceded Reinsurance: The reinsurance program is reviewed by the reinsurance purchasing team on an on-going basis in line with the main business planning process. This process incorporates advice and analytical work from our brokers, actuarial and capital modeling teams.

The review and any subsequent modification to the program is based upon the following:

- budgeted underwriting for the coming year;
- loss experience from prior years;
- loss information from the coming year's individual capital assessment calculations;
- expected changes to risk limits and aggregation limits and any other changes to Talbot's risk tolerance;
- scenario planning;
- changes to capital requirements; and
- RDSs prescribed by Lloyd's.

The main type of reinsurance purchased is losses occurring; however, for a few lines of business, where the timing of the loss event is less easily verified or where such cover is available, risk attaching policies are purchased.

The type, quantity and cost of cover of the proposed reinsurance program is reviewed by the Chief Executive Officer of the Talbot group, and ultimately authorized by the Talbot Underwriting Ltd. ("TUL") Board.

The reinsurance program is purchased in the months prior to the beginning of the covered period. All reinsurance contracts arranged are authorized for purchase by the Talbot Managing Director. Slips are developed prior to inception to ensure that optimum cover is achieved. After purchase, cover notes are reviewed by the relevant class underwriters and presentations made to all underwriting staff to ensure they are aware of the boundaries of the cover.

Western World Ceded Reinsurance: The reinsurance program is managed by senior management. Western World uses brokers to provide guidance on modeling, prices and preparing contract terms and conditions. The main type of reinsurance purchased is excess of loss on a risk attaching basis. Western World utilizes reinsurance to reduce earnings volatility, protect capital and to limit the exposure to risk concentration.

Distribution

Although we conduct some business on a direct basis with our treaty and facultative reinsurance clients, most of our business is derived through insurance and reinsurance intermediaries ("brokers"), who access business from clients and coverholders. We are able to attract business through our recognized lead capability in most classes we underwrite, particularly in classes where such lead ability is rare.

Currently, our largest broker relationships, as measured by gross premiums written, are with Aon Benfield Group Ltd., Marsh & McLennan and Willis Group Holdings Ltd. The following table sets forth the Company's gross premiums written by broker:

	Year Ended December 31, 2014 Gross Premiums Written						
(Dollars in thousands)	Validus Re	AlphaCat	Talbot	Western World (a)	Eliminations	Total	%
Name of Broker							
Aon Benfield Group Ltd.	$342,882	$17,151	$152,521	$—	$(37,768)	$474,786	20.1 %
Marsh & McLennan	413,619	44,142	216,103	—	(1,368)	672,496	28.5 %
Willis Group Holdings Ltd.	240,646	48,951	141,553	—	(5,328)	425,822	18.0 %
Sub-total	997,147	110,244	510,177	—	(44,464)	1,573,104	66.6 %
All Others/Direct	139,763	24,937	591,593	65,235	(31,346)	790,182	33.4 %
Total	$1,136,910	$135,181	$1,101,770	$65,235	$(75,810)	$2,363,286	100.0 %

(a) The results of Western World have been included in the Company's consolidated results from the October 2, 2014 date of acquisition.

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Reserve for Losses and Loss Expenses

For insurance and reinsurance companies, a significant judgment made by management is the estimation of the reserve for losses and loss expenses. The Company establishes its reserve for losses and loss expenses to cover the estimated incurred liability for both reported and unreported claims.

The following tables show certain information with respect to the Company's gross and net reserves:

(Dollars in thousands)	As at December 31, 2014		
	Gross Case Reserves	Gross Incurred But Not Reported Reserves	Total Gross Reserve for Losses and Loss Expenses
Property (a)	$628,289	$472,122	$1,100,411
Marine	426,631	399,417	826,048
Specialty	273,450	441,237	714,687
Liability (a)	166,953	426,295	593,248
Total	$1,495,323	$1,739,071	$3,234,394

(a) The reserves for losses and loss expenses of Western World are consolidated from the October 2, 2014 date of acquisition.

(Dollars in thousands)	As at December 31, 2014		
	Net Case Reserves	Net Incurred But Not Reported Reserves	Total Net Reserve for Losses and Loss Expenses
Property (a)	$545,699	$399,418	$945,117
Marine	398,121	362,971	761,092
Specialty	246,693	394,296	640,989
Liability (a)	158,473	351,257	509,730
Total	$1,348,986	$1,507,942	$2,856,928

(a) The reserves for losses and loss expenses of Western World are consolidated from the October 2, 2014 date of acquisition.

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

The nature of the Company's high excess of loss and catastrophe business can result in loss expenses and payments that are both irregular and significant. Such losses are part of the normal course of business for the Company. Adjustments to reserves for individual years can also be irregular and significant. Conditions and trends that have affected development of liabilities in the past may not necessarily occur in the future. Accordingly, it is inappropriate to extrapolate future redundancies or deficiencies based upon historical experience. See Part I, Item 1A, "Risk Factors" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements."

The tables below present the development of the Company's unpaid losses and loss expense reserves on both a net and gross basis. The cumulative redundancy (deficiency) calculated on a net basis differs from that calculated on a gross basis. As different reinsurance programs cover different underwriting years, net and gross loss experience will not develop proportionately. The top line of each table shows the estimated liability, net and gross of reinsurance recoveries, as at the balance sheet date for each of the indicated years. This represents the estimated amounts of losses and loss expenses, including IBNR, arising in the current and all prior years that are unpaid at that date. The tables also show the re-estimated amount of the previously recorded reserve liability based on experience as of the balance sheet date of each succeeding year. The estimate changes as more information becomes known about the frequency and severity of claims for individual years. The cumulative redundancy (deficiency) represents the aggregate change with respect to that liability originally estimated, as of December 31, 2014. The lower portion of each table also reflects the cumulative paid losses relating to these reserves. Conditions and trends that have affected development of liabilities in the past may not necessarily occur in the future.

Analysis of Losses and Loss Expense Reserve Development Net of Recoveries

	Years Ended December 31,								
(Dollars in thousands)	2006	2007	2008	2009	2010	2011	2012 (b)	2013	2014 (d)
Estimated liability for unpaid losses and loss expenses, net of reinsurance recoverable	$77,363	$791,713	$1,096,507	$1,440,369	$1,752,839	$2,258,658	$3,077,606	$2,660,245	$2,856,928
Net loss reserves disposed							(36,519)		
Liability re-estimated as of: (c)									
One year later	60,106	722,010	1,018,930	1,283,759	1,596,720	2,083,378	2,835,639	2,408,038	
Two years later	54,302	670,069	937,696	1,181,987	1,451,448	1,954,084	2,662,571		
Three years later	50,149	606,387	902,161	1,085,664	1,404,349	1,860,323			
Four years later	46,851	584,588	847,935	1,053,327	1,361,282				
Five years later	45,946	547,965	827,153	1,013,019					
Six years later	45,199	544,656	825,567						
Seven years later	44,567	538,439							
Eight years later	43,605								
Cumulative redundancy (deficiency) (a)	33,758	253,274	270,940	427,350	391,557	398,335	378,516	252,207	
Cumulative paid losses, net of reinsurance recoveries, as of: (c)									
One year later	$27,180	$216,469	$353,476	$384,828	$476,779	$631,889	$916,796	$816,823	
Two years later	34,935	320,803	562,831	634,041	741,940	1,047,879	1,446,139		
	39,520	350,521	662,319	744,324	902,507	1,264,608			

Three years later					
Four years later	41,746	374,788	722,652	818,184	1,002,242
Five years later	41,901	390,895	753,899	854,823	
Six years later	43,571	403,540	769,119		
Seven years later	43,794	409,234			
Eight years later	43,164				

(a) See Part II Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for further discussion.

(b) The reserves for losses and loss expenses of Flagstone are consolidated from the November 30, 2012 date of acquisition.

(c) The impact of foreign currency exchange rate movements is excluded from the re-estimated liability and from paid losses.

(d) The reserves for losses and loss expenses of Western World are consolidated from the October 2, 2014 date of acquisition.

Analysis of Losses and Loss Expense Reserve Development Gross of Recoveries

	Years Ended December 31,								
(Dollars in thousands)	2006	2007	2008	2009	2010	2011	2012 (b)	2013	2014 (d)
Estimated gross liability for unpaid losses and loss expenses	$77,363	$926,117	$1,305,303	$1,622,134	$2,035,973	$2,631,143	$3,517,573	$3,030,399	$3,234,394
Gross loss reserves disposed							(36,590)		
Liability re-estimated as of: (c)									
One year later	60,106	846,863	1,223,018	1,484,646	1,854,565	2,422,343	3,266,832	2,719,232	
Two years later	54,302	791,438	1,164,923	1,385,533	1,705,995	2,257,704	3,066,429		
Three years later	50,149	745,624	1,134,043	1,288,915	1,648,273	2,157,008			
Four years later	46,851	721,730	1,079,842	1,252,042	1,574,858				
Five years later	45,946	675,884	1,055,033	1,198,135					
Six years later	45,199	668,266	1,034,276						
Seven years later	44,567	661,445							
Eight years later	43,605								
Cumulative redundancy (deficiency)(a)	33,758	264,672	271,027	423,999	461,115	474,135	414,554	311,167	
Cumulative paid losses, gross of reinsurance recoveries, as of: (c)									
One year later	$27,180	$245,240	$437,210	$455,182	$557,894	$807,296	$1,065,485	$961,061	
Two years later	34,935	394,685	706,249	709,309	878,406	1,279,820	1,687,413		
Three years later	39,520	452,559	825,159	864,918	1,057,705	1,574,951			
Four years later	41,746	480,277	898,338	950,013	1,187,167				
Five years later	41,901	496,511	933,825	1,002,614					
Six years later	43,571	509,513	964,380						
Seven years later	43,794	517,630							
Eight years later	43,165								

(a) See Part II Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" for further discussion.

(b)

The reserves for losses and loss expenses of Flagstone are consolidated from the November 30, 2012 date of acquisition.

(c) The impact of foreign currency exchange rate movements is excluded from the re-estimated liability and from paid losses.

(d) The reserves for losses and loss expenses of Western World are consolidated from the October 2, 2014 date of acquisition.

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

	Years Ended December 31,		
(Dollars in thousands)	2014 (a)	2013	2012 (c)
Reserve for losses and loss expenses, beginning of year	$3,030,399	$3,517,573	$2,631,143
Losses and loss expenses recoverable	(370,154)	(439,967)	(372,485)
Net reserves for losses and loss expenses, beginning of year	2,660,245	3,077,606	2,258,658
Net loss reserves acquired (disposed)	525,091	(36,519)	639,641
Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in:			
Current year	1,024,256	999,380	1,174,415
Prior years (b)	(252,207)	(205,448)	(174,969)
Total incurred losses and loss expenses (b)	772,049	793,932	999,446
Less net losses and loss expenses paid in respect of losses occurring in:			
Current year	(245,084)	(244,682)	(182,146)
Prior years	(816,823)	(916,796)	(653,874)
Total net paid losses	(1,061,907)	(1,161,478)	(836,020)
Foreign exchange	(38,550)	(13,296)	15,881
Net reserve for losses and loss expenses, end of year	2,856,928	2,660,245	3,077,606
Losses and loss expenses recoverable	377,466	370,154	439,967
Reserve for losses and loss expenses, end of year	$3,234,394	$3,030,399	$3,517,573

(a) The reserves for losses and loss expenses of Western World are consolidated from the October 2, 2014 date of acquisition.

(b) Upon closing the acquisition of Western World, an adjustment of $15,586 was made to increase net reserves to reflect fair value. This adjustment was amortized to income through a reduction in losses and loss expenses of $4,607 during the year ended December 31, 2014. The remaining fair value adjustment will be amortized in 2015.

(c) The reserves for losses and loss expenses of Flagstone are consolidated from the November 30, 2012 date of acquisition.

Validus Re and AlphaCat: Validus Re and AlphaCat's loss reserves are established based upon an estimate of the total cost of claims that have been incurred, including estimates of unpaid liability on known individual claims, the costs of additional case reserves ("ACRs") on claims reported but not considered to be adequately reserved in such reporting and amounts that have been incurred but not yet reported. ACRs are used in certain cases and are calculated based on management's estimate of the required case reserve on an individual claim less the case reserves reported by the client. The Validus Re Loss Reserve Committee follows catastrophe event ultimate loss reserve estimation procedures for the investigation, analysis, estimation and approval of ultimate loss reserving resulting from any material catastrophe event.

For reported losses, Validus Re and AlphaCat establish case reserves within the parameters of the coverage provided in the impacted reinsurance contracts. Where there is a reported claim for which the reported case reserve is determined to be insufficient, Validus Re and AlphaCat will book an ACR or individual claim IBNR estimate that is adjusted as claims notifications are received. Information is obtained from various sources including brokers, proprietary and third party vendor models and internal data regarding reinsured exposures related to the geographic location of the event, as well as other sources. Validus Re and AlphaCat use generally accepted actuarial techniques in its IBNR estimation process. Validus Re and AlphaCat also use historical insurance industry loss emergence patterns, as well as estimates of future trends in claims severity, frequency and other factors, to aid it in establishing loss reserves.

Loss reserves represent estimates, including actuarial and statistical projections at a given point in time, of the expectations of the ultimate settlement and administration costs of claims incurred. Such estimates are not precise in that, among other things, they are based on predictions of future developments and estimates of future trends in loss severity and frequency and other variable factors such as inflation, litigation and tort reform. This uncertainty is heightened by the low frequency high severity nature of the business written by Validus Re and AlphaCat, thereby providing limited claims loss emergence patterns that directly pertain to Validus Re's and AlphaCat's operations. This continues to necessitate the partial use of industry loss emergence patterns in deriving IBNR, which contribute to the inherent uncertainty within the loss reserve estimation process and therefore will differ from actual experience. Further, expected losses and loss ratios are typically developed in part by using outputs from vendor and proprietary computer models and these expected losses and loss ratios are a significant component in the calculation of IBNR. Finally, the uncertainty surrounding estimated costs is greater in cases where large, unique events have been reported and the associated claims are in early stages of resolution. As a result of these uncertainties, it is likely that the ultimate liability will differ from such estimates, perhaps materially.

Talbot: Talbot's loss reserves are established based upon an estimate of the total cost of claims that have been incurred, including case reserves and IBNR. Talbot uses generally accepted actuarial techniques in its IBNR estimation process. ACRs are not generally used.

Talbot performs internal assessments of liabilities on a quarterly basis. Talbot's loss reserving process involves the assessment of actuarial estimates of gross ultimate losses on both an ultimate basis (i.e., ignoring the period during which premium earns) and an earned basis, split by underwriting year and class of business, and generally also between attritional, large and catastrophe losses. These estimates are made using a variety of generally accepted actuarial projection methodologies, as well as additional qualitative consideration of future trends in frequency, severity and other factors. The gross estimates are used to estimate ceded reinsurance recoveries, which are in turn used to calculate net ultimate losses as the difference between gross and ceded. These figures are subsequently used by Talbot's management to help it assess its best estimate of gross and net ultimate losses.

Western World: Western World's loss reserves are established based upon an estimate of the total cost of claims incurred, including case reserves and IBNR. Case reserves are established by Western World claims personnel. The amount of the reserve is based on a case-by-case evaluation of the type of claim involved, the circumstances surrounding each claim and the policy provisions relating to the type of loss. The estimate reflects the informed judgment of such personnel based on their knowledge, experience and Western World's established reserving practices. Until the claim is resolved, these estimates are revised as deemed appropriate by the responsible claims personnel based on subsequent developments and periodic reviews of the case. IBNR reserves are established based on generally accepted actuarial techniques. These techniques assume that past experience, adjusted for the effects of current developments, such as trends in loss costs or in the legal and claims environment, are an appropriate basis for predicting future events.

As with Validus Re and AlphaCat, Talbot and Western World's loss reserves represent estimates, including actuarial and statistical projections at a given point in time, of the expectations of the ultimate settlement and administration costs of claims incurred. Such estimates are not precise in that, among other things, they are based on predictions of future developments and estimates of future trends in loss severity and frequency and other variable factors such as inflation, litigation and tort reform. The uncertainty surrounding estimated costs is also greater in cases where large, unique events have been reported and the associated claims are in the early stages of resolution. As a result of these uncertainties, it is likely that the ultimate liability will differ from such estimates, perhaps materially.

In respect of the risks related to the reserve for losses and loss expenses for all segments, see Part I, Item 1A, "Risk Factors" Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements." Loss reserves are reviewed regularly and adjustments to reserves, if any, will be recorded in earnings in the period in which they are determined. Even after such adjustments, the ultimate liability may exceed or be less than the revised estimates.

Notable loss events: For disclosure purposes, only those loss events which aggregate to more than a certain threshold on a consolidated basis are disclosed separately and included in the reserve for notable loss events and reserve for potential development on notable loss events tables. Notable loss events are first determined at the respective operating segments based on segment thresholds and are then aggregated and only disclosed if it is determined that they reach the consolidated threshold for notable loss event disclosure. The Company increased the consolidated threshold for disclosure of notable loss events effective January 1, 2011, from $5.0 million to $15.0 million. The Company further increased the threshold for disclosure of notable loss events effective January 1, 2013 from $15.0 million to $30.0 million.

Non-notable loss events: For disclosure purposes, only those loss events which aggregate to more than $15.0 million but less than $30.0 million on a consolidated basis are disclosed separately and included in the Company's analysis of losses and loss expenses. Non-notable loss events are first determined at the respective operating segments based on segment thresholds and are then aggregated and only disclosed if it is determined that they reach the consolidated threshold for non-notable loss event disclosure. As noted above, effective January 1, 2013, the Company increased the consolidated threshold for disclosure of notable loss events from $15.0 million to $30.0 million. Therefore, the effective date for the disclosure of non-notable loss events which aggregate to more than $15.0 million but less than $30.0 million on a consolidated basis is January 1, 2013.

During 2010 and 2011, given the complexity and severity of notable loss events in each of those years, an explicit reserve for potential development on notable loss events ("RDE") was included within the Company’s IBNR reserving process. As uncertainties surrounding initial estimates on notable loss events have developed, this reserve has been allocated to specific notable loss events, to the point where the reserve had been fully allocated at December 31, 2013. No RDE has been established for 2012, 2013 or 2014 notable loss events.

The requirement for a reserve for potential development on notable loss events in a period is a function of (a) the number of significant events occurring in that period and (b) the complexity and volatility of those events. Complexity and volatility factors considered include the following:

• Contract complexity;
• Nature and number of perils arising from an event;
• Limits and sub limits exposed;
• Quality, timing and flow of information received from each loss;
• Timing of receipt of information to the Company;
• Information regarding retrocessional covers;
• Assumptions, both explicit and implicit, regarding future paid and reported loss development patterns;
• Frequency and severity trends;
• Claims settlement practices; and
• Potential changes in the legal environment.

Each of these factors may lead to associated volatility for each notable loss event as well as consideration of the total reserve for loss events in the aggregate. Consequently, all of these factors are considered in the aggregate for the events occurring in the period, recognizing that it is more likely that one or some of the events may deteriorate significantly, rather than all deteriorating proportionately. The establishment of each period's requirement for a reserve for potential development on notable loss events takes place as part of the quarterly evaluation of the Company’s overall reserve requirements. It is not directly linked in isolation to any one significant/notable loss. The reserve for potential development on notable loss events is evaluated by our in-house actuaries as part of their normal process of setting indicated reserves at the end of each reporting period. In ensuing periods, senior management and the in-house actuaries revisit and re-estimate certain events previously considered in the catastrophe loss event process as well as events that have subsequently emerged in the most recent period. To the extent that there has been adverse development on a notable loss event, if there is RDE remaining from that accident year, an allocation from the respective accident year RDE will be made to the notable loss event. If there is no remaining RDE relating to the accident year of the loss, then adverse development will be recorded for the notable loss event through the Statements of Comprehensive Income.

Changes to the reserve for potential development on notable loss events are considered in light of changes to previous loss estimates from notable loss events in this re-estimation process. To the extent that there are continued complexity and volatility factors relating to notable loss events in the aggregate, additions to the RDE may be established for a specific accident year, as illustrated in the RDE roll forward table which can be found in Item. 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Investment Management

The Company manages its investment portfolio on a consolidated basis. As we provide predominantly short-tail insurance and reinsurance coverage, we could become liable to pay substantial claims on short notice. Accordingly, we follow a conservative investment strategy designed to emphasize the preservation of invested assets and provide sufficient liquidity for the prompt payment of claims. Our Board of Directors, led by our Finance Committee, Chief Financial Officer and Chief Investment Officer oversees our investment strategy and has established investment guidelines for us. The investment guidelines dictate the portfolio’s overall objectives, benchmark portfolios, eligible securities, duration, use of derivatives, inclusion of foreign securities, diversification requirements and average portfolio rating. Management and the Finance Committee periodically review these guidelines in light of our investment goals and consequently they may change at any time.

Substantially all of the fixed maturity investments held at December 31, 2014 were publicly traded. At December 31, 2014, the average duration of the Company’s fixed maturity and short term investment portfolio, excluding assets held in trust on behalf of operating affiliates, was 2.16 years (December 31, 2013: 1.84 years). Management emphasizes capital preservation for the portfolio and maintains a significant allocation of short-term investments. At December 31, 2014, the average rating of the portfolio was AA- (2013: AA-). At December 31, 2014, the total fixed maturity portfolio was $5.5 billion (2013: $5.5 billion), of which $2.5 billion (2013: $2.5 billion) was rated AAA.

Claims Management

Claims management includes the receipt of initial loss notifications, generation of appropriate responses to claim reports, identification and handling of coverage issues, determination of whether further investigation is required and, where appropriate, retention of legal representation, establishment of case reserves, approval of loss payments and notification to reinsurers.

Validus Re and AlphaCat: The role of our claims department is to investigate, evaluate and, if validated, pay claims efficiently. Our claims director has implemented claims handling guidelines and reporting and control procedures. The primary objectives of the claims department are to ensure that each claim is evaluated, processed and appropriately documented in a timely and efficient manner and information relevant to the management of the claim is retained.

Talbot: Where Talbot is the lead syndicate on business written, the claims adjusters will, in accordance with the respective policies, assess, investigate, appoint third party experts (including attorneys, loss adjusters or other experts) as required and communicate the Company's actions or findings to the Broker who represents the insured. The Company will also establish adequate reserves and promptly pay valid claims in accordance with the applicable "Lloyd's Claims Scheme" and "Lloyd's Claims Management Principles and Minimum Standards."

Where Talbot is not the lead syndicate, the claims handling and case reserves are established in accordance with the applicable "Lloyd's Claims Scheme" and "Lloyd's Claims Management Principles and Minimum Standards." Claims and claims movements are reviewed and monitored by the Talbot claims department. Claim financial reports are received daily from the "Xchanging" system pursuant to a centralized contract with Lloyd's.

Western World: The claims handling process is a vital component of Western World's products and is a key part of the relationship between the insured and Western World. It is the policy of the Western World to investigate, analyze and resolve all claims promptly, fairly and efficiently. Western World's claims philosophy is to provide the highest quality customer service by employing experienced staff specialized in claims handling.

Competition

The insurance and reinsurance industries are highly competitive. We compete with major U.S., Bermuda, European and other international insurers and reinsurers and certain underwriting syndicates and insurers. We encounter competition in all of our classes of business but there is less competition in those of our lines where we are a specialist underwriter. The Company competes with insurance and reinsurance providers such as:

- Alleghany Corporation, Allied World Assurance Company Holdings, Limited., Arch Capital Group, Limited., Argo Group International Holdings, Ltd., Aspen Insurance Holdings Limited, AXIS Capital Holdings Limited, Endurance Specialty Holdings Ltd., Everest Re Group Limited, Montpelier Re Holdings Ltd., PartnerRe Ltd., Platinum Underwriters Holdings Ltd., and RenaissanceRe Holdings Ltd.;
- Amlin plc, Catlin Group Limited, Hiscox and others in the Lloyd’s market;
- Asset managers and reinsurers who provide collateralized reinsurance and retrocessional coverage;
- Treaty and direct insurers, in not only the London but also the global market, that compete with Lloyd’s on a worldwide basis;
- Various capital markets participants who access insurance and reinsurance business in securitized form, including through special purpose entities or derivative transactions; and
- Government-sponsored insurers and reinsurers.

Competition varies depending on the type of business being insured or reinsured and whether the Company is in a leading or following position. Competition in the types of business that the Company underwrites is based on many factors, including:

- Premiums charged and other terms and conditions offered;
- Services provided;
- Financial ratings assigned by independent rating agencies;
- Speed of claims payment;
- Reputation;
- Perceived financial strength; and
- The experience of the underwriter in the line of insurance or reinsurance written.

Increased competition could result in fewer submissions, lower premium rates, lower share of allocated cover, and less favorable policy terms, which could adversely impact the Company’s growth and profitability. Capital market participants have created alternative products such as catastrophe bonds that are intended to compete with reinsurance products. The Company is unable to predict the extent to which these new, proposed or potential initiatives may affect the demand for products or the risks that may be available to consider underwriting.

Regulation
The following is a discussion of the regulatory environment and certain key requirements in the jurisdictions of our significant operating subsidiaries.
Bermuda
General: As a holding company, Validus Holdings, Ltd. is not subject to Bermuda insurance regulation. However, the Insurance Act 1978 and its related regulations (the "Insurance Act") regulates the Company’s operating insurance subsidiaries in Bermuda, and it provides that no person may carry on any insurance business in or from within Bermuda unless registered as an insurer by the Bermuda Monetary Authority (the “BMA”) under the Insurance Act. The Insurance Act makes no distinction between insurance and reinsurance business. The Company has eight Bermuda licensed insurance subsidiaries: Validus Reinsurance, Ltd., a Class 4 insurer; Validus Reinsurance (Switzerland) Ltd (Bermuda Branch) (formerly known as Flagstone Réassurance Suisse S.A. (Bermuda Branch)), a Class 4 insurer; PaCRe, Ltd., a Class 4 insurer; IPCRe Limited ("IPCRe") (formerly known as Validus Re Americas, Ltd.), a Class 3A insurer; Validus Re Americas, Ltd. (formerly known as Longhorn Re, Ltd.), a Class 3A insurer; Talbot Insurance (Bermuda), Ltd. ("TIBL"), a Class 3 insurer; AlphaCat Reinsurance, Ltd., a Class 3 insurer; and Mont Fort Re Ltd., a Class 3 insurer. The Company also has investments in two Bermuda-based insurance affiliates, AlphaCat Re 2011, Ltd. and AlphaCat Re 2012, Ltd., each licensed as a Special Purpose Insurer (“SPI”) under the Insurance Act.
Regulation of Class 3, 3A and 4 insurers: Significant aspects of the Bermuda insurance regulatory framework and requirements imposed on Class 3, 3A and Class 4 insurers are noted below.
Principal Representative and Principal Office: The Insurance Act requires that every insurer appoint and maintain a principal representative resident in Bermuda and maintain a principal office in Bermuda. It is the duty of the principal representative on his reaching a view that there is a likelihood of the insurer for which the principal representative acts becoming insolvent or that a reportable event has, to the principal representative's knowledge, occurred, to immediately notify the BMA and to make a report in writing to the BMA within 14 days of the prior notification setting out all the particulars of the case that are available to the principal representative.
Where there has been a significant loss which is reasonably likely to cause the insurer to fail to comply with its enhanced capital requirement, the principal representative must also furnish the BMA with a capital and solvency return reflecting an enhanced capital requirement prepared using post-loss data. The principal representative must provide this within 45 days of notifying the BMA regarding the event.
Approved Independent Auditor: Class 3, 3A and 4 insurers must appoint an independent auditor who will annually audit and report on the statutory financial statements and the statutory financial return of the insurer, both of which are required to be filed annually with the BMA. The independent auditor must be approved by the BMA.
Approved Loss Reserve Specialist: Class 3, 3A and 4 insurers are required to submit an opinion of their approved loss reserve specialist with their statutory financial return in respect of their losses and loss expense provisions. The loss reserve specialist, who will normally be a qualified casualty actuary, must be approved by the BMA.
Annual Financial Statements, Annual Statutory Financial Return and Annual Capital and Solvency Return: Class 3, 3A and 4 insurers must prepare annual statutory financial statements as prescribed in the Insurance Act. The statutory financial statements are separate from the annual financial statements prepared in accordance with GAAP Standards defined and discussed further below. Class 3, 3A and 4 insurers are also required to prepare and file with the BMA statutory financial returns unless granted an exemption under section 56 of the Insurance Act. The statutory financial return includes, among other items, a report of the approved independent auditor on the statutory financial statements of such insurer, a statutory solvency certificate, the statutory financial statements, the opinion of the loss reserve specialist, a special purpose business solvency certificate in relation to any special purpose business undertaken, and in the case of Class 3A and 4 insurers only a schedule of reinsurance ceded. In addition, Class 3A and 4 insurers are required to file a capital and solvency return in respect of their general business which shall include, amongst other items, the regulatory risk based capital model, a schedule of net reserves for losses and loss expense provisions by line of business and a schedule of premiums written by line of business, a schedule of risk management and schedules of fixed income securities. Class 3A and 4 insurers are also required to file audited annual financial statements, prepared in accordance with either International Financial Reporting Standards, generally accepted accounting principles (GAAP) that apply in Bermuda, Canada, the United Kingdom or the United States of America or such other GAAP as the BMA may recognize (together “GAAP Standards”), which are published on the BMA website.

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Minimum Solvency Margins: The value of the general business assets of licensed insurers must exceed the amount of its general business liabilities by an amount greater than the prescribed minimum solvency margin (“MSM,”) being equal to the greater of:
Class 4:
(a)$100,000,000;
(b)50% of net premiums written (being gross premiums written less any premiums ceded by the insurer for reinsurance, but the insurer may not deduct more than 25% of gross premiums when computing net premiums written);
(c)15% of net losses and loss expense provisions and other insurance reserves (general business); or
(d)25% of the insurer's enhanced capital requirement.
Class 3 and 3A:
(a)$1,000,000;
(b)20% of net premiums written up to $6,000,000 (being gross premiums written less any premiums ceded by the insurer for reinsurance); or where net premiums written exceed $6,000,000, $1,200,000 plus 15% of the net premiums written in excess of $6,000,000; or
(c)15% of net losses and loss expense provisions and other insurance reserves (general business)
and in the case of Class 3A insurers only 25% of the insurer's enhanced capital requirement.
Minimum Liquidity Ratio: The Insurance Act provides a minimum liquidity ratio for general business insurers. An insurer engaged in general business is required to maintain the value of its relevant assets at not less than 75% of the amount of its relevant liabilities. Relevant assets include, but are not limited to, cash and time deposits, quoted investments, unquoted bonds and debentures, investments in mortgage loans on real estate, investment income due and accrued, accounts and premiums receivable, reinsurance balances receivable and funds held by ceding reinsurers. There are certain categories of assets which, unless specifically permitted by the BMA, do not automatically qualify as relevant assets, such as investments in and advances to affiliates. The relevant liabilities are total general business insurance reserves and total other liabilities less deferred income tax, sundry liabilities (by interpretation, those not specifically defined), letters of credit, guarantees and other instruments.
Enhanced Capital Requirement: Class 3A and 4 insurers are required to maintain available statutory capital and surplus with respect to its general business at a level equal to or in excess of its enhanced capital requirement (“ECR”) which is calculated at the end of its relevant year by reference to the Bermuda Solvency Capital Requirement (“BSCR”) model or an approved internal capital model. The BSCR employs a standard mathematical model that correlates risk underwritten by Bermuda insurers to the capital that is dedicated to the business. The ECR is equal to the higher of each insurer's MSM or the BSCR/approved internal capital model. The BMA expects Class 3A and 4 insurers to operate at or above a target capital level (“TCL”) which exceeds the insurer's ECR. The TCL for a Class 3A and 4 insurer is set at 120% of its ECR.
Eligible Capital: To enable the BMA to better assess the quality of an insurer’s capital resources, Class 3A and 4 insurers must maintain available capital in accordance with a '3 tiered capital regime'. All capital instruments are classified as either basic or ancillary capital which in turn are classified into one of three tiers (Tiers 1, 2 and 3) based on their "loss absorbency" characteristics ("Tiered Capital Requirements"). Eligibility limits are then applied to each tier in determining the amounts eligible to cover regulatory capital requirement levels. The highest capital is classified as Tier 1 Capital, lesser quality capital is classified as either Tier 2 Capital or Tier 3 Capital. Under this regime, not more than certain specified percentages of Tier 1, Tier 2 and Tier 3 Capital may be used to satisfy the Class 3A and 4 insurers' MSM and ECR requirements.
Group Supervision: The BMA may, in respect of an insurance group, determine whether it is appropriate for it to be the group supervisor of that group. For purposes of the Insurance Act, an insurance group is defined as a group of companies that conducts insurance business. The BMA may make such determination where it ascertains that (i) the group is headed by a "specified insurer" (that is to say, it is headed by either a Class 3A, 3B, 4 or Class C, D or E insurer or another class of insurer designated by order of the BMA); or (ii) where the insurance group is not headed by a "specified insurer" whether it is headed by a parent company which is incorporated in Bermuda; or (iii) where the parent company of the group is not a Bermuda incorporated company, whether the BMA is satisfied that the insurance group is directed and managed from Bermuda or the insurer with the largest balance sheet total in the insurance group

is a specified insurer. Where the BMA determines that it should act as the group supervisor, it shall designate a specified insurer that is a member of the insurance group to be the "designated insurer" in respect of that insurance group and it shall give written notice to the designated insurer and other competent authorities that it is the group supervisor.

The BMA is our group supervisor and Validus Reinsurance, Ltd. is the "designated insurer" of our group. The BMA maintains a register of particulars for every insurance group for which it acts as the group supervisor detailing: the name and address of the designated insurer; name and address of each member company of the insurance group falling within the scope of group supervision; the name and address of the principal representative of the insurance group in Bermuda; the name and address of other competent authorities supervising other member companies of the insurance group; and the name and address of the insurance group auditors. The designated insurer must notify the BMA of any changes to the details entered on the register in respect of that insurance group.

As group supervisor, the BMA will perform a number of functions including (i) coordinating the gathering and dissemination of essential or relevant information including disseminating information which is of importance for the supervisory task of other competent authorities; (ii) carrying out a supervisory review and assessment of the financial situation of the insurance group; (iii) carrying out an assessment of the insurance group's compliance with the rules on solvency, risk concentration, intra-group transactions and governance systems; (iv) planning and coordinating, with other competent authorities concerned, supervisory activities in respect of the insurance group; (v) coordinating any enforcement action that may be taken against the insurance group or any of its members; and (vi) planning and coordinating meetings of colleges of supervisors in order to facilitate the carrying out of the functions described above.

Group Actuary: Every insurance group is required to submit an annual group actuarial opinion when filing its group statutory financial return. The group actuary must be approved by the BMA.

Group Solvency: The Insurance (Prudential Standards) (Insurance Group Solvency Requirement) Rules 2011 and Insurance (Group Supervision) Rules 2011 (together, "Group Rules"), will apply to us so long as the BMA remains our group supervisor. The BMA has implemented and imposed many of the additional requirements described in this section as part of its efforts to gain equivalence under Solvency II. Solvency II is an EU directive covering the capital adequacy, risk management and regulatory reporting for insurers and was adopted by the European Parliament in April 2009. The BMA will now wait until further notice to implement Solvency II as a result of the delay in the implementation of Solvency II in Europe. In addition, through the Group Rules, the BMA may take action which affects the Company.

Group Financial Statements, Group Statutory Financial Return and Annual Capital and Solvency Return: Every insurance group is required to prepare an annual group statutory financial return which must be submitted to the BMA by the designated insurer within five months after its financial year end (unless specifically extended). The Group Rules prescribe the rules pertaining to the preparation and substance of the group statutory financial statements (which include, in statutory form, a group balance sheet, a group income statement, a group statement of capital and surplus, and notes thereto). The statutory financial return shall include, among other items, a report of the approved group auditor, an opinion of a group actuary where applicable, an insurance group business solvency certificate, an insurance group cover sheet, particulars of ceded reinsurance comprising the top ten unaffiliated reinsurers for which the group has the highest recoverable balances and any reinsurer with recoverable balances exceeding 15% of the insurance group's statutory capital and surplus, particulars of qualifying members, a list of non-insurance financial regulated entities owned by the group and details of all adjustments applied to the group financial statements in the form of a reconciliation of amounts reported as total assets, total liabilities, net income and total statutory capital and surplus.

Every insurance group must also prepare and submit a group capital and solvency return (the "Group Capital and Solvency Return") which comprises the group BSCR model or outputs from an approved group internal capital model, along with the returns prescribed in the applicable schedules to the Group Rules. The Group Capital and Solvency Return is submitted by the designated insurer on behalf of the group and must include a declaration signed by two directors of the parent company, one of which may be the chief executive, and either the chief risk officer of the parent company, or the chief financial officer of the parent company.

Every insurance group must prepare and submit, on an annual basis, consolidated audited financial statements including notes to the financial statements of the parent company of the group prepared under GAAP Standards ("Group Financial Statements"). The Group Financial Statements must be audited annually by the group's approved auditor who must prepare an auditor's report in accordance with generally accepted auditing standards. The designated insurer is required to file with the BMA annually the audited Group Financial Statements within five months from the end of the relevant financial year (unless specifically extended). The Group Financial Statements are published by the

BMA on its website.

Group Quarterly Financial Returns: In addition to the annual filings, the designated insurer is required to prepare and file, on behalf of the group, quarterly financial returns no later than the end of the month of each May, August and November for the first, second and third quarters respectively. The quarterly financial return shall consist of (a) quarterly unaudited (consolidated) group financial statements in respect of its business for each financial quarter where such statements are the most recent produced by the group, and must not reflect a financial position that exceeds two months and (b) details of material intra-group transactions and risk concentrations, including among other things, details surrounding reinsurance and retrocession arrangements and the ten largest exposures to unaffiliated counterparty risk and other unaffiliated counterparty exposures exceeding 10% of the insurer's statutory capital and surplus.

Group Solvency Margin and Group Enhanced Capital Requirements ("Group ECR"): An insurance group must ensure that the value of the insurance group's assets exceeds the amount of the group's liabilities by the aggregate of: (i) the individual minimum margin of solvency of each qualifying member of the group controlled by the parent company; and (ii) the parent company's percentage shareholding in the member multiplied by the member's MSM, where the parent company exercises significant influence over a member of the group but does not control the member (the "Group MSM"). A member is a qualified member of the insurance group if it is subject to solvency requirements in the jurisdiction in which it is registered.

Insurance groups are required to maintain available statutory capital and surplus to an amount that is equal to or exceeds the value of its group enhanced capital requirement ("Group ECR") which is calculated at the end of its relevant year by reference to the Group BSCR model or an approved internal capital model provided that the Group ECR shall at all times be an amount equal to or exceeding the Group MSM. The Group ECR is being phased in over a period of six years which commenced with the 2013 financial year end. For the 2014 financial year end the applicable Group ECR is equivalent to 60% of the amount determined by the Group BSCR or an approved internal capital model. This requirement will increase by increments of 10% in each of the following four years until 100% of the amount determined by the Group BSCR or an approved internal capital model for the ECR is required for the 2018 financial year end.

The BMA expects insurance groups to operate at or above a group TCL which exceeds the Group ECR. The TCL for insurance groups is set at 120% of its Group ECR.

Group Eligible Capital: Under the Tiered Capital Requirements described above, not more than certain specified percentages of Tier 1, Tier 2 and Tier 3 Capital may be used by an insurance group to satisfy the Group's MSM and Group ECR requirements.

Restrictions on Dividends and Distributions: A Class 4 insurer shall not declare or pay any dividends of more than 25% of its total statutory capital and surplus, as shown on its previous financial year statutory balance sheet, unless at least seven days before payment of the dividends it files with the BMA an affidavit confirming that it will continue to meet its relevant margins. If it failed to meet any of its relevant margins on the last day of any financial year, a Class 3, 3A and 4 insurer shall not, without the approval of the BMA, declare or pay any dividends during the next financial year. In addition, Class 3, 3A and 4 insurers must obtain the BMA's prior approval before reducing its total statutory capital, as shown in its previous year's financial statements, by 15% or more.

Furthermore, under the Companies Act, a Bermuda company may only declare or pay a dividend, or make a distribution out of contributed surplus as the case may be, if the company has no reasonable grounds for believing that it is, or would after the payment be, unable to pay its liabilities as they become due, or if the realizable value of its assets would not be less than its liabilities.

The BMA Insurance Code of Conduct: The BMA Insurance Code of Conduct establishes duties and standards which must be complied with by all insurers licensed under the Insurance Act. The Code is divided into six categories, including:

- Proportionality Principle;
- Corporate Governance;
- Risk Management;
- Governance Mechanism;
- Outsourcing; and
- Market Discipline and Disclosure.

Failure to comply with the requirements under the Code will be a factor taken into account by the BMA in determining whether an insurer is conducting its business in a sound and prudent manner as prescribed by the Insurance Act and may result in the BMA exercising its powers of intervention and investigation.

Notification of Material Changes: Class 3, 3A and 4 insurers are required to give advance notice to the BMA of their intention to effect a material change within the meaning of the Insurance Act. For the purposes of the Insurance Act, the following changes are material: (i) the acquisition or transfer of insurance business being part of a scheme falling under section 25 of the Insurance Act or section 99 of the Companies Act 1981; (ii) the amalgamation with or acquisition of another firm; (iii) engaging in unrelated business that is retail business; (iv) acquisition of controlling interest in an undertaking that is engaged in non-insurance business which offers services and products to persons who are not affiliates of the insurer; (v) outsourcing all or substantially all of the functions of actuarial, risk management, compliance, and internal audit; (vi) outsourcing of all or a material part of an insurer's underwriting activity, (vii) transfer other than by way of reinsurance of all or substantially all of a line of business; and (viii) expansion into a material new line of business.

No Class 3, 3A or 4 insurer shall take any steps to give effect to a material change, unless it has first served notice on the BMA that it intends to effect such material change and before the end of 14 days, either the BMA has notified such company in writing that it has no objection to such change or that period has lapsed without the BMA having issued a notice of objection.

Designated insurers are also required to give notice to the BMA if any member of its group intends to give effect to any material change as defined in clauses (ii) through (viii) above. The designated insurer shall notify the BMA of any material change, effected by a member of the group, within 30 days of such material change taking effect.

BMA's Powers of Investigation, Intervention and Obtaining Information: The BMA may require a registered person or a designated insurer to provide such information or reports the BMA may reasonably require with respect to matters that are likely to be material to the performance of its functions under the Insurance Act. In addition, it may require such person's auditor, underwriter, accountant or any other person with relevant professional skill to prepare a report on any aspect pertaining thereto.

The BMA has certain powers of investigation relating to insurers and their insurance groups which it may exercise in the interest of such insurer's policyholders or potential policyholders. The BMA has certain powers of intervention relating to registered persons including insurers if: (a) there is any significant risk of insolvency; (b) there has been a breach of the Insurance Act or the registered person's license conditions; (c) the minimum criteria for the registered person is not or has not been fulfilled; (d) any controller provisions pursuant to the Insurance Act have been breached; or (e) an insurer is in breach of its ECR. In such circumstances the BMA may give the registered person such directions as it sees fit in order to safeguard the interests of the registered person's clients and potential clients. In addition, if it appears to the BMA that a designated insurer is in breach of the Insurance Act or regulations or rules applicable to it, the BMA may give the designated insurer such directions as the BMA sees fit in order to safeguard the interests of policyholders and potential policyholders of the insurance group. The BMA may disclose certain information relating to the business or other affairs of any person to authorities in countries or territories outside Bermuda to exercise functions corresponding to the BMA's functions under the Insurance Act and in certain other limited circumstances.

Securities: Securities may be offered or sold in Bermuda only in compliance with the provisions of the Investment Business Act 2003, and Exchange Control Act 1972, and related regulations of Bermuda which regulate the sale of securities in Bermuda. In addition, specific permission is required from the BMA, pursuant to the provisions of the Exchange Control Act 1972 and related regulations, for all issuances and transfers of securities of Bermuda companies, other than in cases where the BMA has granted a general permission. The BMA, in its policy dated June 1, 2005, provides that where any equity securities, which would include our ordinary shares, of a Bermuda company are listed on an appointed stock exchange (the New York Stock Exchange is deemed to be an appointed stock exchange under Bermuda law), general permission is given for the issue and subsequent transfer of any securities of a company from and/or to a non-resident, for as long as any equity securities of the company remain so listed. The ordinary shares of the Company are listed on the New York Stock Exchange.

Notwithstanding the above general permission, the BMA has granted the Company permission, subject to our ordinary or voting shares being listed on an appointed stock exchange, to issue, grant, create, sell and transfer any of our shares, options, warrants, depositary receipts, rights, loan notes, debt instruments and other securities of the Company, to and among persons who are either resident or non-resident of Bermuda for exchange control purposes.

Shareholder Controller and other Notifications: Under the Insurance Act each shareholder controller or prospective shareholder controller will be responsible for notifying the BMA in writing if the shareholder controller becomes a controller, directly or indirectly, of 10%, 20%, 33% or 50% ("shareholder controller") of the Company and/or any of the Company's Bermuda insurance subsidiaries. The BMA may serve a notice of objection on any existing controller of the Company or any of the Company's Bermuda insurance subsidiaries if it appears to the BMA that the person is no longer a fit and proper person to be such a controller. The Company's Bermuda insurance subsidiaries are required to notify the BMA in writing in the event of any person becoming or ceasing to be a controller or officer of the insurer. In addition the group's designated insurer in respect of its parent company of the insurance group, is required to notify the BMA in the event of any person becoming or ceasing to be an officer of the insurer or of the parent company of the group. An officer includes a director, chief executive, or senior executive performing duties of underwriting, actuarial, risk management, compliance, internal audit, finance or investment matters. A controller includes a managing director, or a chief executive of the insurer or of another company of which it is a subsidiary, or any other person in accordance with whose directions or instructions the directors or controllers of the insurer or a company of which the insurer is a subsidiary are accustomed to act, including any person who holds, or is entitled to exercise, 10% or more of the voting shares or voting power or is able to exercise a significant influence over the management of the insurer or a company of which the insurer is a subsidiary pursuant to the provisions of the Insurance Act.

United States

General: Western World's operating subsidiaries are domiciled in the state of New Hampshire. Western World Insurance Company operates as a surplus lines insurer in all other jurisdictions. Tudor Insurance Company is licensed as a domestic surplus lines insurer in New Hampshire and is authorized to conduct business as a surplus lines insurer in all other jurisdictions. Stratford Insurance Company operates as an admitted insurer in 49 jurisdictions. Talbot operates within the Lloyd’s insurance market through Syndicate 1183, and Lloyd’s operations are subject to regulation in the United States in addition to being regulated in the United Kingdom, as discussed further below. The Lloyd’s market is licensed to engage in insurance business in Illinois, Kentucky and the U.S. Virgin Islands and operates as an eligible excess and surplus lines insurer in all states and territories except Kentucky and the U.S. Virgin Islands. Validus Reaseguros, Inc. and Validus Re America (New Jersey) Inc. are licensed reinsurance intermediaries in Florida and New York, respectively.

Much of state insurance regulation follows model statutes or regulations developed or amended by the National Association of Insurance Commissioners ("NAIC") which is governed by the chief insurance regulators of each U.S. jurisdiction. Through the NAIC, state insurance regulators establish standards, best practices and coordinate regulatory oversight.

Holding Company Regulation: Western World's operating subsidiaries are subject to the insurance holding company laws of the state of New Hampshire. These regulations generally provide that each insurance company in the system is required to register with the state insurance department and furnish information concerning the operations of companies within the holding company system which may materially affect the operations, management or financial condition of the insurers within the system. All transactions within a holding company system affecting insurers must be fair and reasonable and notice to the state insurance department is required prior to the consummation of certain material transactions between an insurer and any entity in its holding company system. In addition, certain of such transactions cannot be consummated without prior approval from the state insurance department, or its failure to disapprove after receiving notice. The holding company acts also prohibit any person from directly or indirectly acquiring control of a U.S. insurance company unless that person has filed an application with specified information with the insurance company’s domiciliary commissioner and has obtained the commissioner’s prior approval. Under most states’ statutes, including New Hampshire, acquiring 10% or more of the voting securities of an insurance company or its parent company is presumptively considered an acquisition of control of the insurance company, although such presumption may be rebutted. Accordingly, any person or entity that acquires, directly or indirectly, 10% or more of the voting securities a U.S. insurance company without the prior approval of the commissioner will be in violation of these laws and may be subject to injunctive action requiring the disposition or seizure of those securities by the commissioner or prohibiting the voting of those securities, or to other actions that may be taken by the commissioner.

In 2010, the NAIC adopted amendments to the Insurance Holding Company System Regulatory Act and Regulation, which, among other changes, introduce the concept of “enterprise risk” within an insurance holding company system. If and when the amendments are adopted by a particular state, the amended Insurance Holding Company System Regulatory Act and Regulation would impose more extensive informational requirements on parents and other affiliates of licensed insurers or reinsurers with the purpose of protecting them from enterprise risk, including requiring an annual enterprise risk report by the ultimate controlling person identifying the material risks within the insurance holding company system that could pose enterprise risk to the licensed companies. The amended Insurance Holding Company System Regulatory Act also requires any controlling person of a U.S. insurance company seeking to divest its controlling interest in the insurance company to file with the commissioner a confidential notice of the proposed divestiture at least 30 days prior to the cessation of control; after receipt of the notice, the commissioner shall determine those instances in which the parties seeking to divest or to acquire a controlling interest will be required to file for or obtain approval of the transaction. The amended Insurance Holding Company System Regulatory Act and Regulation must be adopted by the individual states for the new requirements to apply to U.S. domestic insurers and reinsurers. To date, only certain states, including New Hampshire, have enacted legislation adopting the amended Insurance Holding Company System Regulatory Act in some form.

Enterprise Risk: The NAIC has increased its focus on risks within an insurer’s holding company system that may pose enterprise risk to the insurer. “Enterprise risk” is defined as any activity, circumstance, event or series of events involving one or more affiliates of an insurer that, if not remedied promptly, is likely to have a material adverse effect upon the financial condition or the liquidity of the insurer or its insurance holding company system as a whole. As noted above, the NAIC recently adopted amendments to its Model Insurance Holding Company System Regulatory Act and Regulation, which include, among other amendments, a requirement for the ultimate controlling person to file an enterprise risk report. In 2012, the NAIC adopted the Risk Management and ORSA Model Act, which requires domestic insurers to maintain a risk management framework and establishes a legal requirement for domestic insurers to conduct an ORSA in accordance with the NAIC's ORSA Guidance Manual. The ORSA Model Act provides that domestic insurers, or their insurance group, must regularly conduct an ORSA consistent with a process comparable to the ORSA Guidance Manual process. The ORSA Model Act also provides that, no more than once a year, an insurer's domiciliary regulator may request that an insurer submit an ORSA summary report, or any combination of reports that together contain the information described in the ORSA Guidance Manual, with respect to the insurer and/or the insurance

group of which it is a member. If and when the ORSA Model Act is adopted by a particular state, the ORSA Model Act would impose more extensive filing requirements on parents and other affiliates of domestic insurers.
Statutory Accounting Practices: Statutory accounting practices, or “SAP,” are a basis of accounting developed to assist U.S. insurance regulators in monitoring and regulating the solvency of insurance companies. It is primarily concerned with measuring an insurer’s surplus to policyholders. Accordingly, statutory accounting focuses on valuing assets and liabilities of insurers at financial reporting dates in accordance with appropriate insurance law and regulatory provisions applicable in each insurer’s domiciliary state. U.S. GAAP concerns an insurer’s solvency, but it also concerns other financial measurements, such as income and cash flows. Accordingly, U.S. GAAP gives more consideration to appropriate matching of revenue and expenses and accounting for management’s stewardship of assets than does SAP. As a direct result, different assets and liabilities and different amounts of assets and liabilities will be reflected in financial statements prepared in accordance with U.S. GAAP as opposed to SAP.
Statutory Accounting Practices established by the NAIC and adopted, in part, by the New Hampshire insurance regulator, determine, among other things, the amount of statutory surplus and statutory net income of Western World's insurance company subsidiaries and thus determine, in part, the amount of funds they have available to pay dividends.
Restrictions on Dividends and Distributions: The ability of an insurer to pay dividends or make other distributions is subject to insurance regulatory limitations of the insurance company’s state of domicile. Generally, such laws limit the payment of dividends or other distributions above a specified level. Dividends or other distributions in excess of such thresholds are “extraordinary” and are subject to prior regulatory approval. Such dividends or distributions may be subject to applicable withholding or other taxes. Refer to Note 26 "Statutory and regulatory requirements" to the Consolidated Financial Statements in Part II, Item 8.
Insurance Regulatory Information System Ratios: The NAIC Insurance Regulatory Information System (“IRIS”) was developed by a committee of state insurance regulators and is intended primarily to assist state insurance departments in executing their statutory mandates to oversee the financial condition of insurance companies operating in their respective states. IRIS identifies 13 industry ratios (referred to as “IRIS ratios”) and specifies “usual values” for each ratio. Departure from the usual values of the IRIS ratios can lead to inquiries from individual state insurance commissioners as to certain aspects of an insurer’s business. Our insurance subsidiaries have consistently met the majority of the IRIS ratio tests.
Risk-Based Capital Requirements: In order to enhance the regulation of insurer solvency, the NAIC adopted in December 1993 a formula and model law to implement risk-based capital requirements for property and casualty insurance companies. These risk-based capital requirements are designed to assess capital adequacy and to raise the level of protection that statutory surplus provides for policyholder obligations. The risk-based capital model for property and casualty insurance companies measures three major areas of risk facing property and casualty insurers:

- underwriting, which encompasses the risk of adverse loss developments and inadequate pricing;
- declines in asset values arising from credit risk; and
- declines in asset values arising from investment risks.

An insurer will be subject to varying degrees of regulatory action depending on how its statutory surplus compares to its risk-based capital calculation. For equity investments in an insurance company affiliate, the risk-based capital requirements for the equity securities of such affiliate would generally be our U.S.-based subsidiaries’ proportionate share of the affiliate’s risk-based capital requirement.

Under the approved formula, an insurer’s total adjusted capital is compared to its authorized control level risk-based capital. If this ratio is above a minimum threshold, no company or regulatory action is necessary. Below this threshold are four distinct action levels at which a regulator can intervene with increasing degrees of authority over an insurer as the ratio of surplus to risk-based capital requirement decreases. The four action levels include:

- insurer is required to submit a plan for corrective action;
- insurer is subject to examination, analysis and specific corrective action;
- regulators may place insurer under regulatory control; and

- regulators are required to place insurer under regulatory control.

Western World’s surplus (as calculated for statutory purposes) is above the risk-based capital thresholds that would require either company or regulatory action.

Guaranty Funds: Most states require all admitted insurance companies to participate in their respective guaranty funds which cover certain claims against insolvent insurers. Solvent insurers licensed in these states are required to cover the losses paid on behalf of insolvent insurers by the guaranty funds and are generally subject to annual assessments in the states by the guaranty funds to cover these losses.

Federal Regulation: Although state regulation is the dominant form of regulation for insurance business, the federal government in recent years has shown some concern over the adequacy of state regulation. It is not possible to predict the future impact of any potential federal regulations or other possible laws or regulations on our U.S. based subsidiaries' capital and operations, and such laws or regulations could materially adversely affect their business. In addition, a number of federal laws affect and apply to the insurance industry, including various privacy laws and the economic and trade sanctions implemented by the Office of Foreign Assets Control ("OFAC"). OFAC maintains and enforces economic sanctions against certain foreign countries and groups and prohibits U.S. persons from engaging in certain transactions with certain persons or entities. OFAC has imposed civil penalties on persons, including insurance companies, arising from violations of its economic sanctions program.

The Dodd-Frank Wall Street Reform and Consumer Protection Act: The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") created the Federal Insurance Office ("FIO") within the Department of Treasury, which is not a federal regulator or supervisor of insurance, but monitors the insurance industry for systemic risk, consults with the states regarding insurance matters and develops federal policy on aspects of international insurance matters. The Dodd-Frank Act also created a uniform system for non-admitted insurance premium tax payments based on the home state of the policyholder and provides for single state regulation for financial solvency and credit for reinsurance as discussed below.

Credit for Reinsurance: Certain provisions of the Dodd-Frank Act, which became effective on July 21, 2011, provide that only the state in which a primary insurer is domiciled may regulate the financial statement credit for reinsurance taken by that primary insurer. U.S. domiciled ceding companies typically receive full credit for outwards reinsurance protections in their statutory financial statements with respect to liabilities ceded to admitted U.S. domestic reinsurers. However, most states in the U.S. do not confer full credit for outwards reinsurance protections for liabilities ceded to non-admitted or unlicensed reinsurers, unless the reinsurer specifically collateralizes its obligations to the ceding company or is an authorized or trusteed reinsurer in the ceding company's state of domicile through the establishment of a Multi-Beneficiary Reinsurance Trust ("MBRT").

In December 2014, the Company established a MBRT to collateralize its (re)insurance liabilities associated with and for the benefit of U.S. domiciled cedants, and was approved as a trusteed reinsurer in the State of New Jersey. As a result, cedants domiciled in that state will receive automatic credit in their regulatory filings for the reinsurance provided prospectively by the Company. Following the approval by the State of New Jersey, in 2015, we expect to submit applications in most other U.S. states and territories, respectively, to become a trusteed reinsurer. It is our intention over time to transition U.S. domiciled cedants with outstanding letters of credit to the MBRT and therefore reduce our reliance on letters of credit. Through Lloyd's, Talbot is also an accredited reinsurer in all states and territories of the United States. Lloyd's maintains various trust funds in the state of New York to protect its U.S. business and is therefore subject to regulation by the New York Department of Financial Services, which acts as the domiciliary department for Lloyd's U.S. trust funds. There are deposit trust funds in other states to support Lloyd's reinsurance and excess and surplus lines insurance business.

As a result of the requirements relating to the provision of credit for reinsurance, our reinsurance operations are indirectly subject to certain regulatory requirements imposed by jurisdictions in which ceding companies are domiciled. In addition, the insurance and reinsurance regulatory framework of Bermuda and the insurance of U.S. risk by companies based in Bermuda and not licensed or authorized in the United States recently has become the subject of increased scrutiny in many jurisdictions, including the United States. We are not able to predict the future impact of changes in the laws and regulation to which we are or may become subject on the Company's financial condition or results of operations.

Tax Regulations: Talbot is subject to a Closing Agreement between Lloyd’s and the U.S. Internal Revenue Service pursuant to which Talbot is subject to U.S. federal income tax to the extent its income is attributable to U.S. agents who have authority to bind Talbot. Specifically, U.S. federal income tax is imposed on 35% of its income attributable to U.S. binding authorities (70% for Illinois or Kentucky business).

Other Regulations: AlphaCat Managers, Ltd. is a licensed insurance manager and is registered as an investment adviser with the U.S. Securities and Exchange Commission under the U.S. Investment Advisers Act of 1940, as amended. AlphaCat Managers, Ltd. is also registered as a "commodity pool operator" with the Commodity Futures Trading Commission (the "CFTC") and is a member of the National Futures Association.

United Kingdom

On April 1, 2013, the UK Financial Services Authority (“FSA”) ceased to exist in its current form and two new focused regulators were established, namely the Financial Conduct Authority (“FCA”) and the Prudential Regulation Authority (“PRA”), both of which fall under the Financial Services Markets Act 2000.

The Financial Conduct Authority (“FCA”) has a strong mandate for promoting confidence and transparency in financial services and gives greater protection for consumers of financial services.

The Prudential Regulation Authority (“PRA”) is responsible for the day-to-day supervision of financial institutions that are subject to significant prudential regulation. It adopts a more judgment-focused approach to regulation so that business models can be challenged, risks identified and action taken to preserve financial stability. The PRA also has an insurance objective of contributing to the securing of an appropriate degree of protection for those who are or may become policyholders.

In relation to insurance, the FCA and PRA both regulate insurers, insurance intermediaries and Lloyd’s itself. The FCA, PRA and Lloyd’s have common objectives in ensuring that the Lloyd’s market is appropriately regulated. To minimize duplication, there are arrangements with Lloyd’s for co-operation on supervision and enforcement.

Talbot’s underwriting activities are therefore regulated by both the FCA and PRA as well as being subject to the Lloyd’s “franchise” rules. All three have powers to remove their respective authorization for Talbot to manage Lloyd’s syndicates. Lloyd’s approves annually Syndicate 1183’s business plan and any subsequent material changes, and the amount of capital required to support that plan. Lloyd’s may require changes to any business plan presented to it or additional capital to be provided to support the underwriting (known as Funds as Lloyd’s).

Talbot Risk Services Pte, Ltd. operates in Singapore to source business in the Far East under the Lloyd’s Asia Scheme. The Lloyd’s Asia Scheme was established by the Monetary Authority of Singapore to encourage members of Lloyd’s to expand insurance activities in Asia.

An EU directive covering the capital adequacy, risk management and regulatory reporting for insurers, known as Solvency II was adopted by the European Parliament in April 2009. The proposed implementation date has been changed more than once, but is it now intended to come into force on January 1, 2016. Insurers and reinsurers have been and continue to undertake a significant amount of work to ensure that they meet the new requirements and this may divert resources from other operational roles. Talbot's implementation plans are materially complete, as Lloyd's requires that businesses in the Lloyd's market must be materially Solvency II compliant by January 1, 2015 and fully compliant with the tests and standards for internal model approval by February 28, 2015. Talbot is currently engaged in the review process with Lloyd's and expects to achieve compliance with the agreed time line. If the review process results in noncompliance, there is a risk that it may result in prudential measures being taken by Lloyd's in respect of Talbot.

Switzerland

Our Swiss reinsurance subsidiary, Validus Reinsurance (Switzerland) Ltd ("Validus Re Swiss") (formerly Flagstone Réassurance Suisse SA), is a société anonyme headquartered in Zurich, Switzerland as of February 1, 2014.

Regulation and Supervision: Validus Re Swiss obtained its reinsurance license from the Swiss Federal Office of Private Insurance (now the Swiss Financial Market Supervisory Authority or "FINMA") in December 2006. The conduct of reinsurance business by a company headquartered in Switzerland requires a license granted by FINMA. In principle, licensing and supervision requirements are imposed on Validus Re Swiss as a standalone legal entity.

In general, FINMALaw is an overarching statute applying in as far as there is no contrary provision in the sectoral laws for insurance and reinsurance. Sectoral laws are those laws germane to a particular industry sector such as, for example, insurance, reinsurance and banking. Aside from some inconsequential amendments under FINMALaw unifying cross sectoral issues, the existing sectoral laws governing insurance and reinsurance continue in force, substantially unchanged.

The various legal and regulatory requirements that must be satisfied, are set forth primarily by the three following sets of rules and regulations: the Federal Insurance Supervisory Law (“ISL”); the Federal Private Insurance Supervision Ordinance (“ISO”); and the FINMA Insurance Supervision Ordinance, as well as by various implementing directives and circulars. In general, the approach is principles based and allows for consideration of a justified application by management in relation to such principles.

Under Swiss rules and regulations, Swiss reinsurance companies are generally subject to many, but not all, of the same provisions that apply to direct insurers, and include the following obligations:

Adequacy of Financial Resources: ISL Article 9 and ISO, sets out the minimum capital requirements and solvency requirements. The minimum capital for a reinsurance firm is CHF 10 million.

In addition, Validus Re Swiss must keep adequate disposable and unencumbered capital resources to cover its entire activities. In calculating the solvency margin, account is taken of the risks to which the firm is exposed, the insurance classes involved, the extent of the business, the geographical scope and internationally recognized principles (ISL Article 9). Solvency is determined based on two independent methodologies:

Solvency I: This involves calculating a margin applying defined percentages to a base of the higher of gross annual premium or gross claims for the last three available years and comparing coverage in terms of admissible “own funds” as determined under ISL Article 37.

The Swiss Solvency Test ("SST"): Under this approach, a company's capital is considered adequate if its risk bearing capital ("RBC") exceeds its target capital ("TC"). RBC is defined as the difference between assets at a market-consistent value and discounted best estimated liabilities. TC is defined as the sum of a market value margin and the difference between the discounted one-year RBC and the current year RBC. The SST involves a sophisticated analysis to calculate the market-consistent valuation of all assets and liabilities with a methodological approach to risk categories (insurance risk, credit risk, etc.) subjecting them to scenario stress tests at a basic level in the context of the standard regulatory approach but, where appropriate (for instance mandatory for reinsurance companies), permitting the use of internal models in the overall management of risk, once such models are validated. The validation of internal models is a general process which FINMA has pursued with all regulated firms over the past years and is ongoing.

The SST is very close to the “Solvency II” standard of the European Union. On February 1, 2010, Switzerland was formally recognized as equivalent by the EU committee of supervisors, the Committee of European Insurance and Occupational Pensions Supervisors (“CEIOPS”), firstly as regards the EU Reinsurance Directive of 2005 regulating pure reinsurers and secondly as regards its supervisory regime.

For the SST all assets of Validus Re Swiss are considered. There is no direct constraint on permitted investments since the provisions regarding assets linked to reserves in the ISL do not apply to reinsurance firms. However, the use of derivative instruments is required to be fully considered as part of the risk management processes and limited to reducing investment or insurance risk or to secure investment efficiencies.

Sound Corporate Governance, Risk Management and Internal Control System: In addition to quantitative risk measures, FINMA requires full qualitative governance and control of risk in the firm. This includes requirements as to the ongoing fitness, propriety and competence of the directors and senior management, observance of ethical standards, objective and appropriate remuneration procedures, management of conflicts of interests, independence and adequate resourcing of control functions (including the responsible actuary, the risk management function and the internal audit function), as well as clear terms of reference and systems of delegation and report throughout.

ISL and ISO each require the appointment of a Responsible Actuary - an independent and properly qualified actuary responsible for ensuring that solvency margins are calculated correctly, proper accounting principles are used, and adequate technical reserves are established and that this person report to the Board periodically.

Insurance companies are required to implement documented procedures for risk management and internal control. While FINMA does not require a specific quantitative outcome in relation to operational risk, the firm is expected to undertake proper analysis and to account for it.

Supervisory Process: The supervisory process includes the following requirements:

Annual Reporting: Validus Re Swiss is required to prepare an annual report at the end of each financial year on the solvency margins available, as well as an annual report on the calculation of target capital and on risk bearing capital. Validus Re Swiss files a corporate report incorporating financial statements prepared and audited in accordance with Swiss accounting rules and a supervisory report in the prescribed format. The supervisory report is to be submitted to FINMA by June 30 of each year in electronic form together with the annual report.

Ad Hoc Notifications: FINMA requires ad hoc notifications of all changes to the firm's scheme of operations which include the following: any changes to company statutes, details of its organizational structure or business activities (including expansion into new jurisdictions; changes involving at least a 10% equity holding or at least 10% of votes in the Company, or where there is a change of control allowing persons to exert a significant influence on the Company's commercial activities; changes in management personnel, including the Responsible Actuary).

In addition, Validus Re Swiss is required to notify changes in levels of control of it upstream or by it downstream at 10%, 20%, 33% or 50% in terms of capital or voting rights.

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There is a general duty to notify FINMA of all matters of which it might want to be advised (FINMALaw Article 29). This includes all material solvency matters, which are specified by circular to include a breach of solvency requirements, fluctuations of 10% or more in terms of assets, technical provisions, or of a significant retrocession contract of the company as well as redemption of any hybrid debt instruments; and any regulatory or criminal investigations brought against the company or the senior management or other significant events.
External Auditor Involvement: Audit firms are subjected to approval and supervision by FINMA and are a significant agent in the supervisory process applying to reinsurance companies (FINMALaw 24 et seq.). Auditors report both to the governing body of the company and to FINMA. They report to the Board on the financial statements of the company and on regulatory shortcomings with a requirement for remediation. Material shortcomings are reported directly to FINMA. A standardized audit report on these topics is prescribed by FINMA Directive. Failure to have an audit conducted in accordance with legal requirements, to fulfill the legal duty of cooperation with auditors or for the auditors to perform their role properly (including whistle blowing or failing to identify regulatory breaches) all attract criminal sanctions.
Intervention and Enforcement by the Regulator. FINMALaw provides for a wider range of supervisory intervention tools than previously provided for under the ISL such as the commencement of formal proceedings, including orders to comply with the law, leading up to withdrawal of license, declarations of unfitness for individuals, disgorgement and the appointment of independent specialists to investigate and implement remediation.
Capital Structure and Dividends: Validus Re Swiss is funded by equity in the form of paid in capital by shares and in share premium. Under Swiss corporate law as modified by insurance supervisory law, a non-life insurance company is obliged to contribute to statutory legal reserves a minimum of 20% of any annual profit up to 50% of statutory capital, being paid in share capital. Validus Re Swiss has been substantially funded by share premium. As of the date of this Annual Report we are advised that, share premium can be distributed to shareholders without being subject to withholding tax. However, the distribution of any special dividend to shareholders remains subject to the approval of FINMA which has regard to the maintenance of solvency and the interests of reinsureds and creditors.
Employment Practices
The following table details our personnel by geographic location as at December 31, 2014:

Location	Validus Re	AlphaCat	Talbot	Western World	Corporate	Total	%	
London, England	—	—	259	—	65	324	39.8	%
New Jersey, United States	—	—	—	208	—	208	25.6	%
Pembroke, Bermuda	70	9	—	—	59	138	17.0	%
New York, United States	2	—	14	1	18	35	4.3	%
Republic of Singapore	10	—	20	—	—	30	3.7	%
Waterloo, Canada	—	—	—	—	24	24	2.9	%
Miami, United States	14	—	4	—	—	18	2.2	%
Dubai, United Arab Emirates	—	—	12	—	—	12	1.5	%
Santiago, Chile	—		8	—		8	1.0	%
Toronto, Canada	—	—	—	—	7	7	0.9	%
Zurich, Switzerland	5	—	—	—	—	5	0.6	%
Dublin, Ireland	3	—	—	—	—	3	0.3	%
Boston, United States	—	—	—	2	—	2	0.2	%
Total	104	9	317	211	173	814	100.0	%

We believe our relations with our employees are excellent.

Available Information

The Company files periodic reports, proxy statements and other information with the SEC. The public may read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The SEC's website address is http://www.sec.gov. The Company's common shares are traded on the NYSE under the symbol "VR." Similar information concerning the Company can be reviewed at the office of the NYSE at 20 Broad Street, New York, New York, 10005. The Company's website address is http://www.validusholdings.com. Information contained in this website is not part of this report.

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are available free of charge, including through our website, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. Copies of the charters for the audit committee, the compensation committee, the corporate governance and nominating committee, the finance committee and the risk committee, as well as the Company's Corporate Governance Guidelines, Code of Business Conduct and Ethics for Directors, Officers and Employees (the "Code"), which applies to all of the Company's Directors, officers and employees, and Code of Ethics for Senior Officers, which applies to the Company's principal executive officer, principal accounting officer and other persons holding a comparable position, are available free of charge on the Company's website at http://www.validusholdings.com or by writing to Investor Relations, Validus Holdings, Ltd., 29 Richmond Road, Pembroke, HM 08, Bermuda. The Company will also post on its website any amendment to the Code and any waiver of the Code granted to any of its directors or executive officers to the extent required by applicable rules.

Item 1A. Risk Factors

Risks Related to Our Company

Claims on policies written under our short-tail insurance lines that arise from unpredictable and severe catastrophic events could adversely affect our financial condition or results of operations.

The majority of our gross premiums written to date are in short-tail lines, many of which have the potential to accumulate, which means we could become liable for a significant amount of losses in a brief period. The short-tail policies we write expose us to claims arising out of unpredictable natural and other catastrophic events, whether arising from natural causes such as hurricanes, windstorms, tsunamis, severe winter weather, earthquakes and floods, or man-made causes such as fires, explosions, acts of terrorism, war or political unrest. Many observers believe that the Atlantic basin is in the active phase of a multi-decade cycle in which conditions in the ocean and atmosphere, including warmer-than-average sea-surface temperatures and low wind shear, enhance hurricane activity. This increase in the number and intensity of tropical storms and hurricanes can span multiple decades (approximately 20 to 30 years). These conditions may translate to a greater potential for hurricanes to make landfall in the U.S. at higher intensities over the next several years. In addition, climate change may be causing changes in global temperatures, which may in the future increase the frequency and severity of natural catastrophes and the losses resulting therefrom. Although the frequency and severity of catastrophes are inherently unpredictable, we use state-of-science understanding of climate change and other climate signals for pricing and risk aggregation.

The extent of losses from catastrophes is a function of both the number and severity of the insured events and the total amount of insured exposure in the areas affected. Increases in the value and concentrations of insured property, the effects of inflation and changes in cyclical weather patterns may increase the severity of claims from natural catastrophic events in the future. Similarly, changes in global political and economic conditions may increase both the frequency and severity of man-made catastrophic events in the future. Claims from catastrophic events could reduce our earnings and cause substantial volatility in our results of operations for any fiscal quarter or year, which could adversely affect our financial condition, possibly to the extent of eliminating our shareholders' equity. Our ability to write new reinsurance policies could also be affected as a result of corresponding reductions in our capital. Underwriting is inherently a matter of judgment, involving important assumptions about matters that are unpredictable and beyond our control, and for which historical experience and probability analysis may not provide sufficient guidance. One or more catastrophic or other events could result in claims that substantially exceed our expectations and which would become due in a short period of time, which could materially adversely affect our financial condition, liquidity or results of operations.

Emerging claim and coverage issues could adversely affect our business.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until sometime after we have issued insurance or reinsurance contracts that are affected by the changes. For example, a (re)insurance contract might limit the amount that can be recovered as a result of flooding. However, if the flood damage was caused by an event that also caused extensive wind damage, the quantification of the two types of damage is often a matter of judgment. Similarly, one geographic zone could be affected by more than one catastrophic event. In this case, the amount recoverable from an insurer or reinsurer may in part be determined by the judgmental allocation of damage between the events. Given the magnitude of the amounts at stake, these types of issues occasionally necessitate judicial resolution. In addition, our actual losses may vary materially from our current estimate of the loss based on a number of factors, including receipt of additional information from insureds or brokers, the attribution of losses to coverages that had not previously been considered as exposed and inflation in repair costs due to additional demand for labor and materials. As a result, the full extent of liability under an insurance or reinsurance contract may not be known for many years after such contract is issued and a loss occurs. Our exposure to this uncertainty is greater in our longer tail lines (marine and energy liabilities, aviation products and airports (aviation direct), financial institutions, construction, political risk and liability).

We depend on ratings from third party rating agencies. Our financial strength rating could be revised downward, which could affect our standing among brokers and customers, cause our premiums and earnings to decrease and limit our ability to pay dividends on our common shares.

Third-party rating agencies assess and rate the financial strength of insurers and reinsurers based upon criteria established by the rating agencies, which criteria are subject to change. The financial strength ratings assigned by rating agencies to insurance and reinsurance companies represent independent opinions of financial strength and ability to meet policyholder obligations and are not directed toward the protection of investors. Ratings have become an increasingly important factor in establishing the competitive position of insurance and reinsurance companies. Insurers and intermediaries use these ratings as one measure by which to assess the financial strength and quality of insurers and reinsurers. These ratings are often a key factor in the decision by an insured or intermediary of whether to place business with a particular insurance or reinsurance provider. These ratings are not an evaluation directed toward the protection of investors or a recommendation to buy, sell or hold our common shares.

If our financial strength rating is reduced from current levels, our competitive position in the (re)insurance industry could suffer, and it would be more difficult for us to market our products. A downgrade could result in a significant reduction in the number of (re)insurance contracts we write as our customers and brokers that place such business, move to other competitors with higher financial strength ratings.

The substantial majority of reinsurance contracts issued through reinsurance brokers contain provisions permitting the ceding company to cancel such contracts in the event of a downgrade of the reinsurer by A.M. Best below “A-” (Excellent). We cannot predict in advance the extent to which this cancellation right would be exercised, if at all, or what effect any such cancellations would have on our financial condition or future operations, but such effect could be material and adverse. Consequently, substantially all of Validus Re’s business could be affected by a downgrade of our A.M. Best rating below “A-”.

The indenture governing our Junior Subordinated Deferrable Debentures would restrict us from declaring or paying dividends on our common shares if we are downgraded by A.M. Best to a financial strength rating of “B” (Fair) or below or if A.M. Best withdraws its financial strength rating on any of our material insurance subsidiaries. A downgrade of the Company’s A.M. Best financial strength rating below “B++” (Fair) would also constitute an event of default under our credit facilities. Either of these events could, among other things, reduce the Company’s financial flexibility.

If our risk management and loss limitation methods fail to adequately manage exposure to losses from catastrophic events, our financial condition and results of operations could be adversely affected.

We manage exposure to catastrophic losses by analyzing the probability and severity of the occurrence of catastrophic events and the impact of such events on our overall (re)insurance and investment portfolio. We use various tools to analyze and manage the reinsurance exposures assumed from insureds and ceding companies and risks from a catastrophic event that could have an adverse effect on our investment portfolio. VCAPS, our proprietary risk modeling software, enables us to assess the adequacy of reinsurance risk pricing and to monitor the overall exposure to insurance and reinsurance risk in correlated geographic zones. There can be no assurance that the models and assumptions used by the software will accurately predict losses. Further, there can be no assurance that the models are free of defects in the modeling logic or in the software code. In addition, we have not sought copyright or other legal protection for VCAPS.

In addition, much of the information that we enter into the risk modeling software is based on third-party data that may not be reliable, as well as estimates and assumptions that are dependent on many variables, such as assumptions about building material and labor demand surge, storm surge, the expenses of settling claims (known as loss adjustment expenses), insurance-to-value and storm intensity. Accordingly, if the estimates and assumptions that are entered into the proprietary risk model are incorrect, or if the proprietary risk model proves to be an inaccurate forecasting tool, the losses we might incur from an actual catastrophe could be materially higher than the expectation of losses generated from modeled catastrophe scenarios, and our financial condition and results of operations could be adversely affected.

A modeled outcome of net loss from a single event also relies in significant part on the reinsurance and retrocessional arrangements in place, or expected to be in place at the time of the analysis, and may change during the year. Modeled outcomes assume that the reinsurance in place responds as expected with minimal reinsurance failure or dispute. Reinsurance and retrocessional coverage is purchased to protect the inwards exposure in line with our risk appetite, but it is possible for there to be a mismatch or gap in cover which could result in higher than modeled losses. In addition, many parts of our reinsurance program are purchased with limited reinstatements and, therefore, the number of claims or events which may be recovered from second or subsequent events is limited. It should also be noted that renewal dates of the reinsurance and retrocessional program do not necessarily coincide with those of the inwards business written. Where inwards business is not protected by risks attaching reinsurance and retrocessional programs, the programs could expire resulting in an increase in the possible net loss retained and as such, could have a material adverse effect on our financial condition and results of operations.

We also seek to limit loss exposure through loss limitation provisions in policies we write, such as limitations on the amount of losses that can be claimed under a policy, limitations or exclusions from coverage and provisions relating to choice of forum, which are intended to assure that our policies are legally interpreted as intended. There can be no assurance that these contractual provisions will be enforceable in the manner expected or that disputes relating to coverage will be resolved in our favor. If the loss limitation provisions in the policies are not enforceable or disputes arise concerning the application of such provisions, the losses we incur from a catastrophic event could be materially higher than expected and our financial condition and results of operations could be adversely affected.

The insurance and reinsurance business is historically cyclical and we expect to experience periods with excess underwriting capacity and unfavorable premium rates and policy terms and conditions, which could materially adversely affect our financial condition and results of operations.

The insurance and reinsurance industry has historically been cyclical. Insurers and reinsurers have experienced significant fluctuations in operating results due to competition, frequency of occurrence or severity of catastrophic events, levels of underwriting capacity, underwriting results of primary insurers, general economic conditions and other factors. The supply of insurance and reinsurance is related to prevailing prices, the level of insured losses and the level of industry surplus which, in turn, may fluctuate, including in response to changes in rates of return on investments being earned in the reinsurance industry.

The insurance and reinsurance pricing cycle has historically been a market phenomenon, driven by supply and demand rather than by the actual cost of coverage. The upward phase of a cycle is often triggered when a major event forces insurers and reinsurers to make large claim payments, thereby drawing down capital. This, combined with increased demand for insurance against the risk associated with the event, pushes prices upwards. Over time, insurers' and reinsurers' capital is replenished with the higher revenues. At the same time, new entrants flock to the industry seeking a part of the profitable business. This combination prompts a slide in prices—the downward cycle—until a major insured event potentially restarts the upward phase. As a result, the insurance and reinsurance business has been characterized by periods of intense competition on price and policy terms due to excessive underwriting capacity, which is the percentage of surplus or the dollar amount of exposure that a reinsurer is willing to place at risk, as well as periods when shortages of capacity result in favorable premium rates and policy terms and conditions.

Premium levels may be adversely affected by a number of factors which fluctuate and may contribute to price declines generally in the reinsurance industry. For example, as premium levels for many products increased subsequent to the significant natural catastrophes of 2004 and 2005, the supply of reinsurance increased, either as a result of capital provided by new entrants or by the commitment of additional capital by existing reinsurers. Increases in the supply of insurance and reinsurance may have consequences for the reinsurance industry generally and for us including fewer contracts written, lower premium rates, increased expenses for customer acquisition and retention, and less favorable policy terms and conditions. As a consequence, the Company will experience greater competition on most insurance and reinsurance lines. This could adversely affect the rates we receive for our (re)insurance and our gross premiums written. The insurance and reinsurance industry is currently experiencing a soft market whereby premiums tend to be lower, capacity is higher and competition increases.

The cyclical trends in the industry and the industry's profitability can also be affected significantly by volatile and unpredictable developments, such as natural disasters (e.g., catastrophic hurricanes, windstorms, tornadoes, earthquakes and floods), courts granting large awards for certain damages, fluctuations in interest rates, changes in the investment environment that affect market prices of investments and inflationary pressures that may tend to affect the size of losses experienced by insureds and primary insurance companies. We expect to experience the effects of cyclicality, which could materially adversely affect our financial condition and results of operations.

Competition for business in our industry is intense, and if we are unable to compete effectively, we may not be able to retain market share and our business may be materially adversely affected.

The insurance and reinsurance industries are highly competitive. We face intense competition, based upon (among other things) global capacity, product breadth, reputation and experience with respect to particular lines of business, relationships with (re)insurance intermediaries, quality of service, capital and perceived financial strength (including independent rating agencies' ratings), innovation and price. We compete with major global insurance and reinsurance companies and underwriting syndicates, many of which have extensive experience in (re)insurance and may have greater financial, marketing and employee resources available to them than us. Other financial institutions, such as banks and hedge funds, now offer products and services similar to our products and services through alternative capital markets products that are structured to provide protections similar to those provided by reinsurers. These products, such as catastrophe-linked bonds, compete with our products. In the future, underwriting capacity will continue to enter the market from these identified competitors and perhaps other sources. Increased competition could result in fewer submissions and lower rates, which could have a material adverse effect on our growth and profitability. If we are unable to compete effectively against these competitors, we may not be able to retain market share.

Insureds have been retaining a greater proportion of their risk portfolios than previously, and industrial and commercial companies have been increasingly relying upon their own subsidiary insurance companies, known as captive insurance companies, self-insurance pools, risk retention groups, mutual insurance companies and other mechanisms for funding their risks, rather than risk transferring insurance. This has also put downward pressure on (re)insurance premiums.

Consolidation in the (re)insurance industry could adversely affect our business.

We believe that several (re)insurance industry participants are seeking to consolidate. These consolidated entities may try to use their enhanced market power to negotiate price reductions for our products and services and/or obtain a larger market share through increased line sizes. If competitive pressures reduce our prices, we would expect to write less business. As the (re)insurance industry consolidates, competition for customers will become more intense and the importance of acquiring and properly servicing each customer will become greater. We could incur greater expenses relating to customer acquisition and retention, further reducing our operating margins. In addition, insurance companies that merge may be able to spread their risks across a consolidated, larger capital base so that they require less reinsurance. Reinsurance intermediaries could also continue to consolidate, potentially adversely impacting our ability to access business and distribute our products. We could also experience more robust competition from larger, better capitalized competitors. Any of the foregoing could adversely affect our business or our results of operations.

If we underestimate our reserve for losses and loss expenses, our financial condition and results of operations could be adversely affected.

Our success depends on our ability to accurately assess the risks associated with the businesses and properties that we insure/reinsure. If unpredictable catastrophic events occur, or if we fail to adequately manage our exposure to losses or fail to adequately estimate our reserve requirements, our actual losses and loss expenses may deviate, perhaps substantially, from our reserve estimates.

We estimate the risks associated with our outstanding obligations, including the risk embedded within our unearned premiums. To do this, we establish reserves for losses and loss expenses (or loss reserves), which are liabilities that we record to reflect the estimated costs of claim payment and the related expenses that we will ultimately be required to pay in respect of premiums written and include case reserves and IBNR reserves. However, under U.S. GAAP, we are not permitted to establish reserves for losses until an event which gives rise to a claim occurs. As a result, only reserves applicable to losses incurred up to the reporting date may be set aside on our financial statements, with no allowance for the provision of loss reserves to account for possible other future losses, unless we deem the unearned premium reserve to be insufficient to cover future losses on risks that have already incepted. Case reserves are reserves established with respect to specific individual reported claims. IBNR reserves are reserves for estimated losses that we have incurred but that have not yet been reported to us.

Our reserve estimates do not represent an exact calculation of liability. Rather, they are estimates of what we expect the ultimate settlement and administration of claims will cost. These estimates are based upon actuarial and statistical projections, on our assessment of currently available data, predictions of future developments and estimates of future trends and other variable factors such as inflation. Establishing an appropriate level for our loss reserve estimates is an inherently uncertain process. It is likely that the ultimate liability will be greater or less than these estimates and that, at times, this variance will be material. Our reserve estimates are regularly refined as experience develops and claims are reported and settled. In addition, as we operate largely through intermediaries, reserving for our business can involve added uncertainty arising from our dependence on information from ceding companies which, in addition to the risk of receiving inaccurate information, involves an inherent time lag between reporting information from the primary insurer to us. Additionally, ceding companies employ differing reserving practices which add further uncertainty to the establishment of our reserves. Moreover, in certain circumstances, the Company has necessitated the use of industry loss emergence patterns in deriving IBNR. Loss emergence patterns are development patterns used to project current reported or paid loss amounts to their ultimate settlement value or amount. Further, expected losses and loss ratios are typically developed using vendor and proprietary computer models and these expected loss ratios are a material component in the calculation of IBNR. Actual loss ratios will deviate from expected loss ratios and ultimate loss ratios will be greater or less than expected loss ratios. Because of these uncertainties, it is possible that our estimates for reserves at any given time could prove inadequate.

To the extent we determine that actual losses and loss adjustment expenses from events which have occurred exceed our expectations and the loss reserves reflected in our financial statements, we will be required to reflect these changes in the current reporting period. This could cause a sudden and material increase in our liabilities and a reduction in our profitability, including operating losses and reduction of capital, which could materially restrict our ability to write new business and adversely affect our financial condition and results of operations and potentially our A.M. Best rating.

The preparation of our financial statements requires us to make many estimates and judgments which, if inaccurate, could cause volatility in our results.

Our Consolidated Financial Statements have been prepared in accordance with U.S. GAAP. Management believes the item that requires the most subjective and complex estimates is the reserve for losses and loss expenses. Following a major catastrophic event, the possibility of future litigation or legislative change that may affect interpretation of policy terms further increases the degree of uncertainty in the reserving process. The uncertainties inherent in the reserving process, together with the potential for unforeseen developments, including changes in laws and the prevailing interpretation of policy terms, may result in losses and loss expenses materially different than the reserves initially established. Changes to prior year reserves will affect current underwriting results by increasing net income if the prior year reserves prove to be redundant or by decreasing net income if the prior year reserves prove to be insufficient. We expect volatility in results in periods in which significant loss events occur because U.S. GAAP does not permit insurers or reinsurers to reserve for loss events until they have occurred and are expected to give rise to a claim. As a result, we are not allowed to record contingency reserves to account for expected future losses. We anticipate that claims arising from future events will require the establishment of substantial reserves from time to time.

We rely on key personnel and the loss of their services may adversely affect us. The Bermuda location of our head office may be an impediment to attracting and retaining experienced personnel.

Various aspects of our business depend on the services and skills of key personnel of the Company. We believe there are only a limited number of available qualified executives in the business lines in which we compete. We rely substantially upon the services of Edward J. Noonan, Chairman of our Board of Directors and Chief Executive Officer; Jeffrey D. Sangster, Executive Vice President and Chief Financial Officer; John J. Hendrickson, Director of Strategy, Risk Management and Corporate Development; Kean Driscoll, Executive Vice President and Chief Executive Officer of Validus Reinsurance, Ltd.; C.N. Rupert Atkin, Chief Executive Officer of the Talbot Group; Robert F. Kuzloski, Executive Vice President and General Counsel; Andrew E. Kudera, Executive Vice President and Chief Actuary; Lixin Zeng, Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd.; Romel Salam, Executive Vice President and Chief Risk Officer; Jonathan P. Ritz, Executive Vice President and Chief Operating Officer and Michael R. Moore, Executive Vice President and Chief Accounting Officer, among other key employees. The loss of any of their services or the services of other members of our management team or any difficulty in attracting and retaining other talented personnel could impede the further implementation of our business strategy, reduce our revenues and decrease our operational effectiveness. Although we have an employment agreement with each of the above named executives, there is a possibility that these employment agreements may not be enforceable in the event any of these employees leave. The employment agreements for each of the above-named executives provide that the terms of the agreement will continue for a defined period after either party giving notice of termination, and will terminate immediately upon the Company giving notice of termination for cause. We do not currently maintain key man life insurance policies with respect to these or any of our other employees. In addition, changes in employment laws, taxation and remuneration practices within our operating jurisdiction may adversely impact the retention or recruitment of key personnel.

The operating location of our head office and our primary Validus Re subsidiary may be an impediment to attracting and retaining experienced personnel. Under Bermuda law, non-Bermudians (other than spouses of Bermudians or permanent resident certificate holders) may not engage in any gainful occupation in Bermuda without an appropriate governmental work permit. Our success may depend in part on the continued services of key employees in Bermuda. A work permit may be granted or renewed upon demonstrating that, after proper public advertisement, no Bermudian (or spouse of a Bermudian or a holder of a permanent resident's certificate) is available who meets the minimum standards reasonably required by the employer. A work permit is issued with an expiry date (up to ten years for senior executives) and no assurances can be given that any work permit will be issued or, if issued, renewed upon the expiration of the relevant term. If work permits are not obtained, or are not renewed, for our principal employees, we would lose their services, which could materially affect our business. Work permits are currently required for 54 of our Bermuda employees, the majority of whom have obtained three- or five-year work permits.

Certain of our directors and officers may have conflicts of interest with us.

Entities affiliated with some of our directors have sponsored or invested in, and may in the future sponsor or invest in, other entities engaged in or intending to engage in insurance and reinsurance underwriting, some of which compete with us. They have also entered into, or may in the future enter into, agreements with companies that compete with us. We have a policy in place applicable to each of our directors and officers which provides for the resolution of potential conflicts of interest. However, we may not be in a position to influence any party's decision to engage in activities that would give rise to a conflict of interest, and they may take actions that are not in our shareholders' best interests.

We may require additional capital or credit in the future, which may not be available or only available on unfavorable terms.

We monitor our capital adequacy on a regular basis. The capital requirements of our business depend on many factors, including our premiums written, loss reserves, investment portfolio composition and risk exposures, as well as satisfying regulatory and rating agency capital requirements. Our ability to underwrite is largely dependent upon the quality of our claims paying and financial strength ratings as evaluated by independent rating agencies. To the extent that our existing capital is insufficient to fund our future operating requirements and/or cover claim losses, we may need to raise additional funds through financings or limit our growth. Any equity or debt financing, if available at all, may be on terms that are unfavorable to us. In the case of equity financings, dilution to our shareholders could result, and, in any case, such securities may have rights, preferences and privileges that are senior to those of our outstanding securities. In addition, the capital and credit markets have recently been experiencing extreme volatility and disruption. In some cases, the markets have exerted downward pressure on the availability of liquidity and credit capacity for certain issuers. If we are not able to obtain adequate capital, our business, results of operations and financial condition could be adversely affected.

In addition, for certain of our subsidiaries as an alien insurer and reinsurer (not licensed in the U.S.), we are required to post collateral security with respect to any (re)insurance liabilities that we assume from insureds or ceding insurers domiciled in the U.S. in order for U.S. ceding companies to obtain full statutory and regulatory credit for our reinsurance. Other jurisdictions may have similar collateral requirements. Under applicable statutory provisions, these security arrangements may be in the form of letters of credit, insurance or reinsurance trusts maintained by trustees or funds-withheld arrangements where assets are held by the ceding company. We intend to satisfy such statutory requirements by maintaining the trust fund requirements for Talbot's underwriting at Lloyd's and Validus Re and by providing to primary insurers letters of credit issued under our credit facilities. To the extent that we are required to post additional security in the future, we may require additional letter of credit capacity and there can be no assurance that we will be able to obtain such additional capacity or arrange for other types of security on commercially acceptable terms or on terms as favorable as under our current letter of credit facilities. Our inability to provide collateral satisfying the statutory and regulatory guidelines applicable to insureds and primary insurers would have a material adverse effect on our ability to provide (re)insurance to third parties and negatively affect our financial position and results of operations.

Security arrangements may subject our assets to security interests and/or require that a portion of our assets be pledged to, or otherwise held by, third parties. Although the investment income derived from our assets while held in trust typically accrues to our benefit, the investment of these assets is governed by the investment regulations of the state of domicile of the ceding insurer and therefore the investment returns on these assets may not be as high as they otherwise would be.

Loss of business from one or more major brokers could adversely affect us.

We market our insurance and reinsurance on a worldwide basis primarily through brokers, and we depend on a small number of brokers for a large portion of our revenues. For the year ended December 31, 2014, our business was primarily sourced from the following brokers: Aon Benfield Group Ltd. 20.1%, Marsh & McLennan 28.5% and Willis Group Holdings Ltd. 18.0%. These three brokers provided a total of 66.6% of our gross premiums written for the year ended December 31, 2014. Loss of all or a substantial portion of the business provided by one or more of these brokers could adversely affect our business.

We assume a degree of credit risk associated with substantially all of our brokers.

In accordance with industry practice, we frequently pay amounts owed on claims under our policies to brokers and the brokers, in turn, pay these amounts over to the insured and reassured that have reinsured a portion of their liabilities with us. In some jurisdictions, if a broker fails to make such a payment, we might remain liable to the insured or reassured for the deficiency notwithstanding the broker's obligation to make such payment. Conversely, in certain jurisdictions, when the insured or reassured pays premiums for these policies to the insurance and reinsurance brokers for payment to us, these premiums are considered to have been paid and the insured or reassured will no longer be liable to us for these premiums, whether or not we have actually received them. Consequently, we assume a degree of credit risk associated with substantially all of our brokers.

Our utilization of brokers, managing general agents and other third parties to support our business exposes us to operational and financial risks

Our insurance business relies upon brokers, managing general agents and other third parties to produce and service a portion of its operations. In these arrangements, we typically grant the third party the right to bind us to new and renewal policies, subject to underwriting guidelines we provide and other contractual restrictions and obligations. Should these third parties issue policies that contravene these guidelines, restrictions or obligations, we could nonetheless be deemed liable for such policies. Although we would intend to resist claims that exceed or expand on our underwriting intention, it is possible that we would not prevail in such an action, or that our managing general agent would be unable to adequately indemnify us for their contractual breach.

We also rely on managing general agents, third party administrators or other third parties we retain, to collect premiums and to pay valid claims. We could also be exposed to their or their producer's operational risk, including, but not limited to, contract wording errors, technological and staffing deficiencies and inadequate disaster recovery plans. We could also be exposed to potential liabilities relating to the claims practices of the third party administrators we have retained to manage the claims activity on this business. Although we have implemented monitoring and other oversight protocols, we cannot assure that these measures will be sufficient to mitigate all of these exposures.

Our success depends on our ability to establish and maintain effective operating procedures and internal controls. Failure to detect control issues and any instances of fraud could adversely affect us.

Our success is dependent upon our ability to establish and maintain operating procedures and internal controls (including the timely and successful implementation of information technology systems and programs) to effectively support our business and our regulatory and reporting requirements. We may not be successful in such efforts. Even when implemented, as a result of the inherent limitations in all control systems, no evaluation of controls can provide full assurance that all control issues and instances of fraud, if any, within the Company will be detected.

We may be unable to purchase reinsurance or retrocessional reinsurance in the future, and if we do successfully purchase reinsurance or retrocessional reinsurance, we may be unable to collect on claims submitted under such policies, which could adversely affect our business, financial condition and results of operations.

We purchase reinsurance and retrocessional reinsurance in order that we may offer insureds and cedants greater capacity, and to mitigate the effect of large and multiple losses on our financial condition. Reinsurance is a transaction whereby an insurer or reinsurer cedes to a reinsurer or retrocessional reinsurer all or part of the insurance it has written or reinsurance it has assumed. A reinsurer's or retrocessional reinsurer's insolvency or inability or refusal to make timely payments under the terms of its reinsurance agreement with us could have an adverse effect on us because we remain liable to our client. From time to time, market conditions have limited, and in some cases have prevented, insurers and reinsurers from obtaining the types and amounts of reinsurance or retrocessional reinsurance that they consider adequate for their business needs. Accordingly, we may not be able to obtain our desired amounts of reinsurance or retrocessional reinsurance or negotiate terms that we deem appropriate or acceptable or obtain reinsurance or retrocessional reinsurance from entities with satisfactory creditworthiness.

Our investment portfolio may suffer reduced returns or losses which could adversely affect our results of operations and financial condition. Any increase in interest rates or volatility in the fixed income markets could result in significant unrealized losses in the fair value of our investment portfolio which would reduce our net income.

Our operating results depend in part on the performance of our investment portfolio, which currently consists largely of fixed maturity securities, as well as the ability of our investment managers to effectively implement our investment strategy. Our Board of Directors, led by our Finance Committee, Chief Financial Officer and Chief Investment Officer oversees our investment strategy and has established investment guidelines. The investment guidelines dictate the portfolio's overall objective, benchmark portfolio, eligible securities, duration, limitations on the use of derivatives and inclusion of foreign securities, diversification requirements and average portfolio rating. Management and the Finance Committee periodically review these guidelines in light of our investment goals and consequently they may change at any time.

The investment return including net investment income, net realized and the change in net unrealized gains (losses) on investments, excluding assets held in trust on behalf of operating affiliates, catastrophe bonds and noncontrolling interest, on our invested assets excluding assets held in trust on behalf of operating affiliates, catastrophe bonds and noncontrolling interest was $110.2 million, or 1.8% for the year ended December 31, 2014. While we follow a conservative investment strategy designed to emphasize the preservation of invested assets and to provide sufficient liquidity for the prompt payment of claims, we will nevertheless be subject to market-wide risks including illiquidity and pricing uncertainty and fluctuations, as well as to risks inherent in particular securities. Our investment performance may vary substantially over time, and there can be no assurance that we will achieve our investment objectives. See "Business—Investment Management."

Investment results will also be affected by general economic conditions, market volatility, interest rate fluctuations, liquidity and credit risks beyond our control. In addition, our need for liquidity may result in investment returns below our expectations. Also, with respect to certain of our investments, we are subject to prepayment or reinvestment risk. In particular, our fixed income portfolio is subject to reinvestment risk, and as at December 31, 2014, 26.3% of our fixed maturity portfolio is comprised of mortgage-backed and asset-backed securities which are subject to prepayment risk. Although we attempt to manage the risks of investing in a changing interest rate environment, a significant increase in interest rates could result in significant losses, realized or unrealized, in the fair value of our investment portfolio and, consequently, could have an adverse effect on our results of operations.

Investment methodologies and assumptions are subject to differing interpretations and unrealized losses taken on our investments are subjective which could adversely affect our results of operations and financial condition.

The valuation of our investments may include methodologies, estimations and assumptions that are subject to differing interpretations and could result in changes to our investment valuations. During periods of market disruptions, it may be difficult to value certain securities if trading becomes less frequent or market data less observable. There may also be certain asset classes that become illiquid due to the financial environment. As a result, valuation of securities in our investment portfolio may require more subjectivity and management judgment. Valuation methods that require greater estimation may result in values which may be greater or less than the value at which the investments may be ultimately sold. In addition, rapidly changing and unpredictable credit and equity market conditions could materially affect the valuation of securities as reported in our Consolidated Financial Statements.

The determination of the unrealized losses taken on our investments are also partially subjective and could materially impact our financial position. Unrealized losses vary by investment type and are based upon our periodic evaluations and assessments of known and inherent risks associated with the respective asset class. Evaluations are revised as conditions change, and management reflects unrealized losses in operations on a quarterly basis. Furthermore, additional unrealized losses may need to be taken in the future. Subjective unrealized losses could adversely affect our financial condition and our results of operations.

Certain of our investments are illiquid and may be difficult to sell, or to sell in significant amounts at acceptable prices, to generate cash to meet our needs.

Investments in certain securities in funds attributed to utilizing the equity method, may be illiquid due to contractual provisions or investment market conditions. If we require significant amounts of cash on short notice in excess of anticipated cash obligations, then we may have difficulty selling these investments in a timely manner or we may be forced to sell or terminate them at unfavorable values. The foregoing could adversely affect our financial condition and results of operations.

Our operating results may be adversely affected by currency fluctuations.

Our reporting currency is the U.S. dollar and the majority of our operating companies have a functional currency of the U.S. dollar. Many of our companies maintain both assets and liabilities in local currencies. Therefore, we are exposed to foreign exchange risk on the assets and liabilities denominated in those foreign currencies. Foreign exchange risk is reviewed as part of our risk management process. Locally required capital levels may be invested in home currencies in order to satisfy regulatory requirements and to support local insurance operations. The principal currencies potentially creating unhedged foreign exchange risk are the Australian dollar, New Zealand dollar, Japanese yen, British pound sterling and the Euro. As a result of the accounting treatment for non-monetary items, we may experience volatility in our income statement during a period when movement in foreign exchange rates fluctuate significantly. In accordance with U.S. GAAP, non-monetary items are not re-measured at the reporting date and are therefore translated at historic exchange rates. Non-monetary items include unearned premiums and deferred acquisition costs. Therefore, a mismatch arises in the income statement between the amount of premium recognized at historical exchange rates and the related claims which are re-measured using currency rates at the reporting date which can cause volatility in the income statement. We look to manage our foreign currency exposure through matching our major foreign-denominated assets and liabilities, as well as through the use of currency derivatives. However, there is no guarantee that we will effectively mitigate our exposure to foreign exchange losses. Please refer to Part II, Item 7A “Quantitative and Qualitative Disclosures About Market Risk” for further discussion of foreign currency risk.

Heightened European sovereign debt risk could adversely affect our results of operations and financial condition.

Our fixed maturity portfolio contains certain Eurozone government and government agency securities and Eurozone corporate securities which are subject to increased liquidity risk, interest rate risk and default risk as a result of heightened European sovereign debt risk. As of December 31, 2014, our fixed maturity portfolio contains $115.3 million or 2.1% of Eurozone government and government agency securities and $197.1 million or 3.6% of Eurozone corporate securities. Increased defaults, and/or a significant increase in interest rates could result in losses, realized or unrealized, in the fair value of our investment portfolio and, consequently, could have an adverse effect on our results of operations.

We are subject to cyber security risks and may incur increasing costs in an effort to minimize those risks.

We depend on the proper functioning and availability of our information technology platform, including communications and data processing systems, in operating our business. These systems consist of proprietary software programs that are integral to the efficient operation of our business, including our proprietary pricing and exposure management system. We are also required to effect electronic transmissions with third parties including brokers, client's vendors and others with whom we do business, and to facilitate the oversight conducted by our Board of Directors. Security breaches could expose us to a risk of loss or misuse of our information, litigation and potential liability. In addition, cyber incidents that impact the availability, reliability, speed, accuracy or other proper functioning of these systems could have a significant impact on our operations, and potentially on our results. We may not have the resources or technical sophistication to anticipate or prevent rapidly evolving types of cyber attacks. A significant cyber incident, including system failure, security breach, disruption by malware or other damage could interrupt or delay our operations, result in a violation of applicable privacy and other laws, damage our reputation, cause a loss of customers or give rise to monetary fines and other penalties, which could be significant.

We may be exposed to risk in connection with our management of third party capital.

Our operating subsidiaries may owe certain legal duties and obligations to third party investors (including reporting obligations) and are subject to a variety of often complex laws and regulations relating to the management of third party capital. Compliance with some of these laws and regulations requires significant management time and attention. Although we seek to continually monitor our policies and procedures to attempt to ensure compliance, there could be faulty judgments, simple errors or mistakes, or the failure of our personnel to adhere to established policies and procedures that could result in our failure to comply with applicable laws or regulations which could result in significant liabilities, penalties or other losses to the Company, and seriously harm our business and results of operations. In addition to the forgoing, our third party capital providers may redeem their interests in our managed funds, which could materially impact the financial condition of such funds, and could in turn materially impact our financial condition and results of operations. Moreover, we can provide no assurance that we will be able to attract and raise additional third party capital for our existing funds or for potential new funds and therefore we may forego existing and/or potential fee income and other income generating opportunities.

The ongoing development of our U.S. excess and surplus lines insurance operations is subject to increased risk from changing market conditions.

Excess and surplus lines insurance is a substantial portion of the business written by our newly acquired U.S. operating subsidiary, Western World. Excess and surplus lines insurance covers risks that are typically more complex and unusual than standard risks and require a high degree of specialized underwriting. As a result, excess and surplus lines risks do not often fit the underwriting criteria of standard insurance carriers. Our excess and surplus lines insurance business fills the insurance needs of businesses with unique characteristics and is generally considered higher risk than those in the standard market. If our underwriting staff inadequately judges and prices the risks associated with the business underwritten in the excess and surplus lines market, our financial results could be adversely impacted.

Further, the excess and surplus lines market is significantly affected by the conditions of the property and casualty insurance market in general. The impact of this cyclicality can be more pronounced in the excess and surplus market than in the standard insurance market. During times of hard market conditions (when market conditions are more favorable to insurers), as rates increase and coverage terms become more restrictive, business tends to move from the admitted market to the excess and surplus lines market and growth in the excess and surplus market can be significantly more rapid than growth in the standard insurance market. When soft market conditions are prevalent (when market conditions are less favorable to insurers), standard insurance carriers tend to loosen underwriting standards and expand market share by moving into business lines traditionally characterized as excess and surplus lines, exacerbating the effect of rate decreases. If we fail to manage the cyclical nature and volatility of the revenues and profit we generate in the excess and surplus lines market, our financial results could be adversely impacted.

A decrease in the fair value of Talbot, Western World and/or our intangible assets may result in future impairments.

Goodwill and intangible assets are tested for impairment on an annual basis or more frequently if events or changes in circumstances indicate that the carrying amount may not be recoverable. These tests require us to use significant judgment in making various estimates and assumptions, such as the determination of expected future cash flows and/or earnings, and actual results may ultimately be materially different from such estimates and assumptions. For example, expected future cash flows and/or earnings may be materially and negatively impacted as a result of, among other things, a decrease in renewals and new business, loss of key personnel, lower-than-expected yields and/or cash flows from our investment portfolio or higher-than-expected claims activity and incurred losses as well as other general economic factors. As a result of these potential changes, the estimated fair value of Talbot, Western World and/or our intangible assets may decrease, causing the carrying value to exceed the fair value and the goodwill and/or intangible assets to be impaired. If an impairment is determined to exist, the carrying value of the goodwill and/or intangible asset is adjusted to its implied fair value with the corresponding expense recorded in our income statement in the period in which the impairment is determined. If we are required to record goodwill impairments in the future, our financial condition and results of operations would be negatively affected.

Risks Related to Acquisitions and New Ventures

Any future acquisitions or new ventures may expose us to operational risks.

We may in the future make strategic acquisitions, either of other companies or selected books of business, or grow our business organically. Any future acquisitions or new ventures may expose us to operational challenges and risks, including:

- integrating financial and operational reporting systems;
- integration into new geographical regions;
- establishing satisfactory budgetary and other financial controls;
- funding increased capital needs and overhead expenses;
- retaining management personnel required for existing operations;
- obtaining management personnel required for expanded operations;
- obtaining necessary regulatory permissions;
- funding cash flow shortages that may occur if anticipated revenues are not realized or are delayed, whether by general economic or market conditions or unforeseen internal difficulties;
- the value of assets related to acquisitions or new ventures may be lower than expected or may diminish due to credit defaults or changes in interest rates and liabilities assumed may be greater than expected;

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- the assets and liabilities related to acquisitions or new ventures may be subject to foreign currency exchange rate fluctuation; and
- financial exposures in the event that the sellers of the entities we acquire are unable or unwilling to meet their indemnification, reinsurance and other obligations to us.

Our failure to manage successfully these operational challenges and risks may adversely impact our results of operations.

Risks Related to Lloyd’s and Other U.K. Regulatory Matters

The regulation of Lloyd’s members and of Lloyd’s by the U.K. Financial Conduct Authority (“FCA”) and Prudential Regulation Authority (“PRA”) and under European Directives and other local laws may result in intervention that could have a significant negative impact on Talbot.

Talbot operates in a regulated jurisdiction. Its underwriting activities are regulated by the FCA and PRA and franchised by Lloyd’s. The FCA and PRA have substantial powers of intervention in relation to the Lloyd’s managing agents (such as Talbot Underwriting Ltd.) which it regulates, including the power to remove their authorization to manage Lloyd’s syndicates. In addition, the Lloyd’s Franchise Board requires annual approval of Syndicate 1183’s business plan, including a maximum underwriting capacity, and may require changes to any business plan presented to it or additional capital to be provided to support underwriting (known as Funds at Lloyd’s or “FAL”). An adverse determination in any of these cases could lead to a change in business strategy which may have an adverse effect on Talbot’s financial condition and results of operations.

An EU directive covering the capital adequacy, risk management and regulatory reporting for insurers, known as Solvency II was adopted by the European Parliament in April 2009. The proposed implementation date has been changed more than once, but is it now intended to come into force on January 1, 2016. Insurers and reinsurers have been and continue to undertake a significant amount of work to ensure that they meet the new requirements and this may divert resources from other operational roles. Talbot's implementation plans are materially complete, as Lloyd's requires that businesses in the Lloyd's market must be materially Solvency II compliant by January 1, 2015 and fully compliant with the tests and standards for internal model approval by February 28, 2015. Talbot is currently engaged in the review process with Lloyd's and expects to achieve compliance with the agreed time line. If the review process results in noncompliance, there is a risk that it may result in prudential measures being taken by Lloyd's in respect of Talbot.

Additionally, Lloyd’s worldwide insurance and reinsurance business is subject to local regulation. Changes in such regulation may have an adverse effect on Lloyd’s generally and on Talbot in particular.

Should Lloyd’s Council decide additional levies are required to support the central fund, this could adversely affect Talbot.

The central fund, which is funded by annual contributions and loans from Lloyd’s members, acts as a policyholders’ protection fund to make payments where any Lloyd’s member has failed to pay, or is unable to pay, valid claims. The Lloyd’s Council may resolve to make payments from the central fund for the advancement and protection of policyholders, which could lead to additional or special contributions being payable by Lloyd’s members, including Talbot. This, in turn, could adversely affect Talbot and the Company.

The failure of Lloyd’s to satisfy the PRA’s annual solvency test could result in limitations on managing agents’ ability, including Talbot’s ability to underwrite or the commencement of legal proceedings against Lloyd’s.

The PRA requires Lloyd’s to satisfy an annual solvency test. The solvency requirement in essence measures whether Lloyd’s has sufficient assets in the aggregate to meet all outstanding liabilities of its members, both current and in run-off. If Lloyd’s fails to satisfy the test in any year, the PRA may require Lloyd’s to cease trading and/or its members to cease or reduce underwriting. In the event of Lloyd’s failing to meet any solvency requirement, either the Society of Lloyd’s or the PRA may apply to the court for a Lloyd’s Market Reorganization Order (“LMRO”). On the making of an order a “reorganization controller” is appointed, and for its duration, a moratorium is imposed preventing any proceedings or legal process from being commenced or continued against any party that is the subject of such an order, which, if made, would apply to the market as a whole, including members, former members, managing agents, members’ agents, Lloyd’s brokers, approved run-off companies and managing general agents unless individual parties are specifically excluded.

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A downgrade in Lloyd’s ratings would have an adverse effect on Syndicate 1183’s rating as well its standing among brokers and customers and cause its premiums and earnings to decrease.

The ability of Lloyd’s syndicates to trade in certain classes of business at current levels is dependent on the maintenance of a satisfactory credit rating issued by an accredited rating agency. The financial security of the Lloyd’s market is regularly assessed by three independent rating agencies, A.M. Best, Standard & Poor’s and Fitch Ratings. Lloyd's current ratings are: A.M. Best: A, Positive Outlook; Standard & Poor's: A+, Stable Outlook; Fitch Ratings: AA-, Stable Outlook. Syndicate 1183 is also rated A, Positive Outlook, by A.M. Best. Syndicate 1183 benefits from Lloyd’s current ratings and would be adversely affected if the current ratings were downgraded from their present levels.

An increase in the charges paid by Talbot to participate in the Lloyd’s market could adversely affect Talbot’s financial and operating results.

Lloyd’s imposes a number of charges on businesses operating in the Lloyd’s market, including, for example, annual subscriptions and central fund contributions for members and policy signing charges. The basis and amounts of charges may be varied by Lloyd’s and could adversely affect Talbot and the Company.

An increase in the level or type of deposits required by U.S. Situs Trust Deeds to be maintained by Lloyd’s syndicates could result in Syndicate 1183 being required to make a cash call which could adversely affect Talbot’s financial performance.

The U.S. Situs Trust Deeds require syndicates transacting certain types of business in the United States to maintain minimum deposits as protection for U.S. policyholders. These deposits represent the syndicates' estimates of unpaid claims liabilities (less premiums receivable) relating to this business, adjusted for provisions for potential bad debt on premiums earned but not received and for any anticipated profit on unearned premiums. No credit is generally allowed for potential reinsurance recoveries. The New York Insurance Department and the U.S. National Association of Insurance Commissioners ("NAIC") currently require funding of 30% of gross liabilities in relation to insurance business classified as “Surplus Lines.” The “Credit for Reinsurance” trust fund is usually required to be funded at 100% of gross liabilities. The funds contained within the deposits are not ordinarily available to meet trading expenses. U.S. regulators may increase the level of funding required or change the requirements as to the nature of funding. Accordingly, in the event of a major claim arising in the United States, for example from a major catastrophe, syndicates participating in such U.S. business may be required to make cash calls on their members to meet claims payments and deposit funding obligations. This could adversely affect Talbot.

Risks Related to Taxation

Our non U.S companies may be subject to U.S. tax.

We intend to operate in such a manner that none of our non-U.S. companies would be considered engaged in a U.S. trade or business. No definitive standards, however, are provided by the Internal Revenue Code of 1986, as amended (the “Code”), U.S. Treasury regulations or court decisions regarding activities that constitute the conduct of a U.S. trade or business. Because that determination is essentially factual, there can be no assurance that the Internal Revenue Service (the “IRS”) will not contend that we are engaged in a U.S. trade or business. If we were found to be so engaged, we could be subject to U.S. corporate income and branch profits tax on our earnings that are effectively connected to such U.S. trade or business.

If the group company involved is entitled to the benefits of a U.S. income tax treaty (the “Treaty”), it would not be subject to U.S. income tax on any income protected by the Treaty unless that income is attributable to a permanent establishment in the U.S. The income tax treaty between the U.S. and Bermuda (the “Bermuda Treaty”) clearly applies to premium income, but may be construed as not protecting other income such as investment income. If any of the Company's Bermuda-based subsidiaries were found to be engaged in a trade or business in the U.S. and were entitled to the benefits of the Bermuda Treaty in general, but the Bermuda Treaty was found not to protect investment income, a portion of the relevant subsidiary's investment income could be subject to U.S. tax.

U.S. persons who hold common shares may be subject to U.S. income taxation at ordinary income rates on our undistributed earnings and profits.

Controlled Foreign Corporation Status: The Company should not be a controlled foreign corporation (“CFC”) because its organizational documents provide that if the common shares owned, directly, indirectly or by attribution, by any person would otherwise represent more than 9.09% of the aggregate voting power of all the Company’s common shares, the voting rights attached to those common shares will be reduced so that such person may not exercise and is not attributed more than 9.09% of the total voting power of the common shares. There can be no assurance, however, that the provisions of the Organizational Documents will operate as intended and that the Company will not be considered a CFC. If the Company were considered a CFC, any shareholder that is a U.S. person that owns directly, indirectly or by attribution, 10% or more of the voting power of the Company may be subject to current U.S. income taxation at ordinary income tax rates on all or a portion of the Company’s undistributed earnings and profits attributable to the Company's insurance and reinsurance income, including underwriting and investment income. Any gain realized on sale of common shares by such shareholder may also be taxed as a dividend to the extent of the Company’s earnings and profits attributed to such shares during the period that the shareholder held the shares and while the Company was a CFC (with certain adjustments).

Related Person Insurance Income: If the related person insurance income (“RPII”) of any of the Company’s non-U.S. insurance subsidiaries were to equal or exceed 20% of that subsidiary’s gross insurance income in any taxable year, and U.S. persons were treated as owning 25% or more of the subsidiary’s stock, by vote or value, a U.S. person who directly or indirectly owns any common shares on the last day of such taxable year on which the 25% threshold is met would be required to include in income for U.S. federal income tax purposes that person’s ratable share of that subsidiary’s RPII for the taxable year. The amount to be included in income is determined as if the RPII were distributed proportionately to U.S. shareholders on that date, regardless of whether that income is distributed. The amount of RPII to be included in income is limited by such shareholder’s share of the subsidiary’s current-year earnings and profits, and possibly reduced by the shareholder’s share of prior year deficits in earnings and profits. The amount of RPII earned by a subsidiary will depend on several factors, including the identity of persons directly or indirectly insured or reinsured by that subsidiary. Although we do not believe that the 20% threshold will be met for our non-U.S. insurance subsidiaries, some of the factors that might affect that determination in any period may be beyond our control. Consequently, we cannot assure that we will not exceed the RPII threshold in any taxable year.

If a U.S. person disposes of shares in a non-U.S. insurance corporation that had RPII (even if the 20% threshold was not met) and the 25% threshold is met at any time during the five-year period ending on the date of disposition, and the U.S. person owned any shares at such time, any gain from the disposition will generally be treated as a dividend to the extent of the holder’s share of the corporation’s undistributed earnings and profits that were accumulated during the period that the holder owned the shares (possibly whether or not those earnings and profits are attributable to RPII). In addition, the shareholder will be required to comply with specified reporting requirements, regardless of the amount of shares owned. We believe that those rules should not apply to a disposition of common shares because the Company is not itself directly engaged in the insurance business. We cannot assure, however, that the IRS will not successfully assert that those rules apply to a disposition of common shares.

U.S. persons who hold common shares will be subject to adverse tax consequences if the Company is considered a passive foreign investment company for U.S. federal income tax purposes.

If the Company is considered a passive foreign investment company (“PFIC”) for U.S. federal income tax purposes, a U.S. holder who owns common shares will be subject to adverse tax consequences, including a greater tax liability than might otherwise apply and an interest charge on certain taxes that are deferred as a result of the Company’s non-U.S. status. We currently do not expect that the Company will be a PFIC for U.S. federal income tax purposes in the current taxable year or the foreseeable future because, through Validus Reinsurance, Ltd., Talbot 2002 Underwriting Capital Ltd., Validus Reinsurance (Switzerland) Ltd and Talbot Underwriting Ltd., it intends to be predominantly engaged in the active conduct of a global insurance and reinsurance business. We cannot assure you, however, that the Company will not be deemed to be a PFIC by the IRS. No regulations currently exist regarding the application of the PFIC provisions to an insurance company.

Changes in U.S. tax laws may be retroactive and could subject a U.S. holder of our common shares to other adverse tax consequences.

The tax treatment of non-U.S. companies and their U.S. and non-U.S. insurance and reinsurance subsidiaries has been the subject of Congressional discussion and legislative proposals in the U.S. We cannot assure you that future legislative action will not increase the amount of U.S. tax payable by us.

In addition, the U.S. federal income tax laws and interpretations, including those regarding whether a company is engaged in a U.S. trade or business or is a PFIC, or whether U.S. holders would be required to include “subpart F income” or RPII in their gross income, are subject to change, possibly on a retroactive basis. No regulations regarding the application of the PFIC rules to insurance companies are currently in effect, and the regulations regarding RPII are still in proposed form. New regulations or pronouncements interpreting or clarifying such rules may be forthcoming. We cannot be certain if, when, or in what form, such regulations or pronouncements may be provided, and whether such guidance will have a retroactive effect.

The Obama administration’s proposed budget for Fiscal Year 2016 could disallow a deduction for premiums paid for reinsurance.

Insurance companies are generally allowed a deduction for premiums paid for reinsurance. The proposed U.S. budget for fiscal year 2016 contains a proposal that denies an insurance company a deduction for premiums and other amounts paid to affiliated foreign companies with respect to reinsurance of property and casualty risks to the extent that the foreign reinsurer (or its parent company) is not subject to U.S. income tax with respect to the premiums received. Furthermore, the proposed law would exclude from the insurance company’s income (in the same proportion in which the premium deduction was denied) any return premiums, ceding commissions, reinsurance recovered, or other amounts received with respect to reinsurance policies for which a premium deduction is wholly or partially denied. Based on the information currently available to us, it is uncertain to what extent this legislation will adversely impact us.

We may become subject to taxes in Bermuda after March 31, 2035, which may have a material adverse effect on our results of operations.

Under current Bermuda law, we are not subject to tax on income or capital gains. We have received from the Minister of Finance under The Exempted Undertaking Tax Protection Act 1966, as amended, an assurance that, in the event that Bermuda enacts legislation imposing tax computed on profits, income, any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance, then the imposition of any such tax shall not be applicable to us or to any of our operations or shares, debentures or other obligations, until March 31, 2035. We could be subject to taxes in Bermuda after that date. This assurance is subject to the provision that it is not to be construed to prevent the application of any tax or duty to such persons as are ordinarily resident in Bermuda or to prevent the application of any tax payable in accordance with the provisions of the Land Tax Act 1967 or otherwise payable in relation to any property leased to us. The Company's Bermuda-domiciled subsidiaries each pay annual Bermuda government fees and each Bermuda subsidiary licensed insurer and reinsurer pays an annual insurance license fee. In addition, all entities employing individuals in Bermuda are required to pay a payroll tax and there are other sundry taxes payable, directly or indirectly, to the Bermuda government.

The impact of Bermuda's letter of commitment to the Organization for Economic Cooperation and Development ("OECD") to eliminate harmful tax practices is uncertain and could adversely affect our tax status in Bermuda.

The OECD has published reports and launched a global initiative among member and non-member countries on measures to limit harmful tax competition. These measures are largely directed at counteracting the effects of tax havens and preferential tax regimes in countries around the world. Bermuda was not listed in the most recent report as an uncooperative tax haven jurisdiction because it had previously committed to eliminate harmful tax practices, to embrace international tax standards for transparency, to exchange information and to eliminate an environment that attracts business with no substantial domestic activity. We are not able to predict what changes will arise from the commitment or whether such changes will subject us to additional taxes.

Our non-U.K. companies may be subject to U.K. tax.

We intend to operate in such a manner that none of our non-U.K. companies would be resident in the U.K. for tax purposes. A company incorporated outside the U.K. will be deemed resident if its business is centrally managed and controlled from the U.K. The concept of central management and control is not defined in statute but derives from case law and the determination of residence is subjective, therefore Her Majesty's Revenue and Customs ("HMRC") might contend successfully that one or more of our companies are resident in the U.K.

Furthermore, we intend to operate in such a manner that none of our non-U.K. companies carry on a trade wholly or partly in the U.K. Case law has held that whether or not a trade is being carried on is a matter of fact and emphasis is placed on where operations take place from which the profits in substance arise. This judgment is subjective. The HRMC might contend successfully that one or more of our non-U.K. companies, is conducting business in the U.K. For tax purposes, a non-U.K. tax resident company will only be subject to corporation tax if it carries on a trade in the U.K. through a permanent establishment. However, that company will still have an income tax liability if it carries on a trade in the U.K., even absent a permanent establishment, unless that company is treaty-protected.

We may become subject to taxation on profits generated in Bermuda as a result of the OECD's plan on "Base erosion and profit shifting"

In 2013, the OECD published an ‘Action Plan on Base Erosion and Profit Shifting.’ The plan proposes the development of rules to prevent Base Erosion and Profit Shifting which may drive fundamental changes in the perception of tax structuring and transfer pricing by tax authorities. The action plan includes adopting transfer pricing rules or special measures to ensure that returns will not accrue to an entity solely because it has contractually assumed risks or has provided capital. The action plan will likely put a much greater emphasis on the location of individuals and their contributions towards profit generation. This would notably result in a significant change to the existing transfer pricing rules and could potentially have a significant impact on the allocation of taxable profits throughout the Company. As a consequence, profits currently generated in Bermuda may become subject to taxation outside Bermuda.

Our non-Swiss companies may be subject to taxation in Switzerland.

We intend to operate in such a manner that none of our non-Swiss companies would be resident in Switzerland for tax purposes. A company incorporated outside Switzerland will be deemed resident if its business is centrally managed and controlled from Switzerland. However, the analysis is factual and the Swiss tax authorities might contend successfully that one or more of our non-Swiss group companies are resident in Switzerland.

Furthermore, a group company incorporated and managed outside of Switzerland should not be liable for Swiss corporation taxation unless it carries on business through a permanent establishment in Switzerland. From a Swiss tax perspective, a permanent establishment is a fixed place of business through which a company performs business activities that are considered as being quantitatively and qualitatively significant by the tax authorities, and may include a branch, office, agency or place of management. As of the date of this Annual Report, the Validus group intends to operate in such a manner so that none of our non-Swiss companies will carry on business through a permanent establishment in Switzerland. If any of our companies were to be treated as carrying on business in Switzerland through a branch or agency or of having a permanent establishment in Switzerland, our results of operations could be adversely affected.

Diverted Profit Tax in the U.K.

The U.K. Authorities announced in 2014 that they would introduce a new Diverted Profits Tax. This tax will apply as of April 1, 2015 to profits of multinationals artificially diverted from the U.K. The Lloyd's accounting practices delay the recognition of underwriting results by three years ("reinsurance to close") and this might give the Diverted Profits Tax a retroactive effect. The tax rate will be 25%. Diverted Profits Tax will apply in two situations; (a) where a foreign company has artificially avoided having a taxable presence in the U.K, or (b) where a group has entered into a tax advantageous structure or transaction that lacks economic substance. On December 10, 2014, draft legislation and guidance and a Technical Note were published by HMRC.

Although the intentions of the legislation are to address aggressive tax planning which is artificial or lacks economic substance, the draft legislation may have a wider reach. The Validus group has significant U.K. operations and several intragroup reinsurance agreements. We believe that these transactions have economic substance and should fall outside the intended reach of the Diverted Profit Tax. However, given that the legislation is still in draft and the many uncertainties related to its application, we are not able to predict the financial impact of the new Diverted Profits Tax and such impact may be adverse.

Risks Related to Laws and Regulations Applicable to Us

If we become subject to insurance statutes and regulations in addition to the statutes and regulations that currently apply to us, there could be a significant and negative impact on our business.

We currently conduct our business in a manner such that we expect the Company will not be subject to insurance and/or reinsurance licensing requirements or regulations in any jurisdiction other than Bermuda, Switzerland, the United States, and, with respect to Talbot, the U.K. and jurisdictions to which Lloyd’s is subject. See “Business—Regulation.” Although we do not currently intend to engage in activities which would require us to comply with insurance and reinsurance licensing requirements of other jurisdictions, should we choose to engage in activities that would require us to become licensed in such jurisdictions, we cannot assure you that we will be able to do so or that we will be able to do so in a timely manner.

The insurance and reinsurance regulatory framework has recently become subject to increased scrutiny in many jurisdictions. Governmental authorities in both the U.S. and worldwide have become increasingly interested in the potential risks posed by the insurance industry as a whole, and to commercial and financial systems in general. For example, the U.S. Congress and the current administration have made, or called for consideration of, several additional proposals relating to a variety of issues with respect to financial regulation reform, including the Dodd-Frank Act that was signed into law by President Obama on July 21, 2010. The Dodd-Frank Act represented a comprehensive overhaul of the regulation of the financial services industry within the United States and established a Federal Insurance Office under the U.S. Treasury Department to monitor all aspects of the insurance industry and of lines of business other than certain health insurance, certain long-term care insurance and crop insurance. The director of the Federal Insurance Office has the ability to recommend that an insurance company or an insurance holding company be subject to heightened prudential standards under the supervision of the Federal Reserve. In addition, some state legislators have considered or enacted laws that will alter and likely increase state regulation of insurance and reinsurance companies and holding companies. Furthermore, the NAIC, which is an association of the insurance commissioners of all 50 states and the District of Columbia, regularly reexamines existing laws and regulations.

Government regulators are generally concerned with the protection of policyholders rather than other constituencies, such as our shareholders. We are not able to predict the exact nature, timing or scope of changes in laws and regulations to which we are or may become subject; however, compliance with such laws and regulations may result in additional costs which may adversely impact our results of operations.

Our international business is subject to applicable laws and regulations relating to sanctions and foreign corrupt practices, the violation of which could adversely affect our operations.

We must comply with all applicable economic sanctions and anti-bribery laws and regulations of the United States and other foreign jurisdictions where we operate, including the United Kingdom and the European Community. United States laws and regulations applicable to us include the economic trade sanctions laws and regulations administered by the United States Department of the Treasury's Office of Foreign Assets Control ("OFAC") as well as certain laws administered by the United States Department of State. In addition, we are subject to the Foreign Corrupt Practices Act ("FCPA") and other anti-bribery laws such as the UK Bribery Act that generally bar corrupt payments or unreasonable gifts to foreign governments or officials. Although we have policies and controls in place that are designed to ensure compliance with these laws and regulations, it is possible that an employee or intermediary could fail to comply with applicable laws and regulations. In such event, we could be exposed to civil penalties, criminal penalties and other sanctions, including fines or other punitive actions. In addition, such violations could damage our business and/or our reputation. Such criminal or civil sanctions, penalties, other sanctions, and damage to our business and/or reputation could have a material adverse effect on our financial condition and results of operations.

Risks Related to Ownership of Our Common Shares

Because Validus Holdings, Ltd. is a holding company and substantially all of our operations are conducted by our main operating subsidiaries our ability to meet any ongoing cash requirements and to pay dividends will depend on our ability to obtain cash dividends or other cash payments or obtain loans from these subsidiaries.

We conduct substantially all of our operations through subsidiaries. Our ability to meet our ongoing cash requirements, including any debt service payments or other expenses, and pay dividends on our common shares in the future, will depend on our ability to obtain cash dividends or other cash payments or obtain loans from these subsidiaries and as a result will depend on the financial condition of these subsidiaries. The inability of these subsidiaries to pay dividends in an amount sufficient to enable us to meet our cash requirements could have a material adverse effect on us and the value of our common shares. Each of these subsidiaries is a separate and distinct legal entity that has no obligation to pay any dividends or to lend or advance us funds and may be restricted from doing so by contract, including other financing arrangements, charter provisions or applicable legal and regulatory requirements or rating agency constraints. The payment of dividends by these subsidiaries to us is limited under Bermuda, U.K. and U.S. laws and regulations. The Insurance Act provides that our Bermuda Class 3B and 4 insurance subsidiaries may not declare or pay in any financial year dividends of more than 25% of their total statutory capital and surplus (as shown on their statutory balance sheets in relation to the previous financial year) unless they file an affidavit with the BMA at least seven days prior to the payment signed by at least two directors and such subsidiary's principal representative, stating that in their opinion such subsidiaries will continue to satisfy the required margins following declaration of those dividends, though there is no additional requirement for BMA approval. In addition, before reducing its total statutory capital by 15% or more (as set out in its previous years' statutory financial statements) each of our Class 3A and Class 4 insurance subsidiaries must make application to the BMA for permission to do so, such application to consist of an affidavit signed by at least two directors and such subsidiary's principal representative stating that in their opinion the proposed reduction in capital will not cause such subsidiaries to fail to meet its relevant margins, and such other information as the BMA may require. Each of our Class 3 insurance subsidiaries must make application to the BMA before reducing its total statutory capital by 15% or more and should provide such information as the BMA may require. During 2015, the Bermuda regulated subsidiaries have the ability to distribute up to $968.2 million of unrestricted net assets as dividend payments and/or return of capital to Validus Holdings, Ltd. without prior regulatory approval.

Talbot manages Syndicate 1183 (the "Syndicate") at Lloyd's. Lloyd's requires Talbot to hold cash and investments in trust for the benefit of policyholders either as Syndicate trust funds or as Funds at Lloyd's ("FAL"). Talbot may not distribute funds from the Syndicate into its corporate member's trust accounts unless, firstly, they are represented by audited profits and, secondly, the Syndicate has adequate future cash flow to service its policyholders. Talbot's corporate member may not distribute funds to Talbot’s unregulated bank or investment accounts unless they are represented by a surplus of cash and investments over the FAL requirement. Additionally, U.K. company law prohibits Talbot’s corporate name from declaring a dividend to the Company unless it has profits available for distribution. The determination of whether a company has profits available for distribution is based on its accumulated realized profits less its accumulated realized losses. While the U.K. insurance regulatory laws do not impose statutory restrictions on a corporate name’s ability to declare a dividend, the FCA and PRA rules require maintenance of each insurance company’s solvency margin within its jurisdiction.

Western World's operating subsidiaries are domiciled in the state of New Hampshire. New Hampshire insurance laws limit the amount of dividends Western World may pay to the Company in any 12 month period without prior approval of the New Hampshire State Insurance Department. These limitations are based on the lesser of: a maximum of 10% of prior year end statutory surplus as determined under statutory accounting practices or the net income, not including realized capital gains, for the 12-month period ending December 31, next preceding, but shall not include pro rata distributions of any class of the insurer's own securities. In determining whether a dividend or distribution is extraordinary, an insurer may carry forward net income from the previous two calendar years that has not already been paid out as dividends. This carry-forward shall be computed by taking the net income from the second and third preceding calendar years, not including realized capital gains, less dividends paid in the second and immediate preceding calendar years. During 2015, the maximum dividend that may be paid to the Company by Western World without obtaining prior approval is $45.2 million.

The timing and amount of any cash dividends on our common shares are at the discretion of our Board of Directors and will depend upon our results of operations and cash flows, our financial position and capital requirements, general business conditions, legal, tax, regulatory, rating agency and contractual constraints or restrictions and any other factors that our Board of Directors deems relevant. In addition, the indentures governing our Junior Subordinated Deferrable Debentures would restrict us from declaring or paying dividends on our common shares if we are downgraded by A.M. Best to a financial strength rating of “B” (Fair) or below or if A.M. Best withdraws its financial strength rating on any of our material insurance subsidiaries.

Future sales of our common shares and grants of restricted shares may affect the market price of our common shares and the future exercise of options and warrants may result in immediate and substantial dilution of the common shares.

As of December 31, 2014 (but without giving effect to unvested restricted shares), we had 83,869,845 common shares outstanding and 5,174,114 shares issuable upon exercise of outstanding warrants. Approximately 2,449,543 of these outstanding shares were subject to the volume limitations and other conditions of Rule 144 under the Securities Act of 1933, as amended, which we refer to as the “Securities Act.” Furthermore, certain of our sponsoring shareholders and their transferee's have the right to require us to register these common shares under the Securities Act for sale to the public, either in an independent offering pursuant to a demand registration or in conjunction with a public offering, subject to a “lock-up” agreement of no more than 90 days. Following any registration of this type, the common shares to which the registration relates will be freely transferable. In addition, we have filed one or more registration statements on Form S-8 under the Securities Act to register common shares issued or reserved for issuance under our 2005 Long Term Incentive Plan (the “Plan”). The number of common shares that have been reserved for issuance under the Plan is equal to 13,126,896 of which 903,292 shares remain available as of December 31, 2014. We cannot predict what effect, if any, future sales of our common shares, or the availability of common shares for future sale, will have on the market price of our common shares. Sales of substantial amounts of our common shares in the public market, or the perception that sales of this type could occur, could depress the market price of our common shares and may make it more difficult for our shareholders to sell their common shares at a time and price that they deem appropriate.

Our Bye-laws authorize our Board of Directors to issue one or more series of common shares and preferred shares without shareholder approval. Specifically, we have an authorized share capital of 571,428,571 shares ($0.175 par value per share), which can consist of common shares and/or preference shares, as determined by our Board of Directors. The Board of Directors has the right to issue the remaining shares without obtaining any approval from our shareholders and to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, conversion rights, voting rights, terms of redemption, liquidation preferences and the number of shares constituting any series or designation of such series. Any issuance of our preferred stock could adversely affect the voting power of the holders of our common shares and could have the effect of delaying, deferring, or preventing the payment of any dividends (including any liquidating dividends) and any change in control of us. If a significant number of either common or preferred shares are issued, it may cause the market price of our common shares to decline.

Our classified board structure may prevent a change in our control.

Our Board of Directors is divided into three classes of directors. Each year one class of directors is elected by the shareholders for a three year term. The staggered terms of our directors may reduce the possibility of a tender offer or an attempt at a change in control, even though a tender offer or change in control might be in the best interest of our

shareholders.
There are provisions in our Bye-laws that reduce the voting rights of voting common shares that are held by a person or group to the extent that such person or group holds more than 9.09% of the aggregate voting power of all common shares entitled to vote on a matter.
In general, and except as provided below, shareholders have one vote for each common share held by them and are entitled to vote at all meetings of shareholders. However, if, and for so long as, the common shares of a shareholder, including any votes conferred by “controlled shares” (as defined below), would otherwise represent more than 9.09% of the aggregate voting power of all common shares entitled to vote on a matter, including an election of directors, the votes conferred by such shares will be reduced by whatever amount is necessary such that, after giving effect to any such reduction (and any other reductions in voting

power required by our Bye-laws), the votes conferred by such shares represent 9.09% of the aggregate voting power of all common shares entitled to vote on such matter. “Controlled shares” include, among other things, all shares that a person is deemed to own directly, indirectly or constructively (within the meaning of Section 958 of the Code, or Section 13(d) (3) of the Securities and Exchange Act of 1934, as amended (the “Exchange Act”)). At December 31, 2014, there were 86,728,556 common shares, of which 7,883,625 common shares would confer votes that represent 9.09% of the aggregate voting power of all common shares entitled to vote generally at an election of directors. An investor who does not hold, and is not deemed under the provisions of our Bye-laws to own, any of our common shares may therefore purchase up to such amount without being subject to voting cutback provisions in our Bye-laws. In addition, we have the authority under our Bye-laws to request information from any shareholder for the purpose of determining ownership of controlled shares by such shareholder.

There are regulatory limitations on the ownership and transfer of our common shares which could result in the delay or denial of any transfers shareholders might seek to make.

The BMA must approve all issuances and transfers of securities of a Bermuda exempt company except where a general permission applies under the Exchange Control Act 1972 and related regulations. We have received permission from the BMA to issue our common shares and securities, and for the free transferability of our common shares and securities, as long as the common shares are listed on the New York Stock Exchange or other appointed exchange, to and among persons who are residents and non-residents of Bermuda for exchange control purposes. Any other transfers remain subject to approval by the BMA and such approval may be denied or delayed. Additionally issuances and transfers of voting or controlling shares of Bermuda registered insurance subsidiaries requires application to, or notification to, the BMA Insurance Division (depending on the circumstances) pursuant to the Insurance Act.

A shareholder of our Company may have greater difficulties in protecting its interests than as a shareholder of a U.S. corporation.

The Companies Act 1981 (the “Companies Act”), which applies to us, differs in material respects from laws generally applicable to U.S. corporations and their shareholders. Taken together with the provisions of our Bye-laws, some of these differences may result in a shareholder having greater difficulties in protecting its interests as a shareholder of our company than it would have as a shareholder of a U.S. corporation. This affects, among other things, the circumstances under which transactions involving an interested director are voidable, whether an interested director can be held accountable for any benefit realized in a transaction with our Company, what approvals are required for business combinations by our Company with a large shareholder or a wholly owned subsidiary, what rights a shareholder may have as a shareholder to enforce specified provisions of the Companies Act or our Bye-laws, and the circumstances under which we may indemnify our directors and officers.

We are a Bermuda company and it may be difficult for our shareholders to enforce judgments against us or against our directors and executive officers.

We were incorporated under the laws of Bermuda and our business is based in Bermuda. In addition, certain of our directors and officers reside outside the United States, and a portion of our assets and the assets of such persons may be located in jurisdictions outside the United States. As such, it may be difficult or impossible to effect service of process within the United States upon us or those persons, or to recover against us or them on judgments of U.S. courts, including judgments predicated upon the civil liability provisions of the U.S. federal securities laws. Further, no claim may be brought in Bermuda against us or our directors and officers in the first instance for violation of U.S. federal securities laws because these laws have no extraterritorial application under Bermuda law and do not have force of law in Bermuda; however, a Bermuda court may impose civil liability, including the possibility of monetary damages, on us or our directors and officers if the facts alleged in a complaint constitute or give rise to a cause of action under Bermuda law. Currently, of our executive officers, Kean Driscoll, Jeffrey Sangster, Robert Kuzloski, Michael Moore and Lixin Zeng reside in Bermuda, Edward Noonan, John Hendrickson, Romel Salam, Andrew Kudera and Jonathan Ritz maintain residences in both Bermuda and the United States and Rupert Atkin resides in the United Kingdom. Of our directors, Edward Noonan and John Hendrickson maintain residences in both Bermuda and the United States, Jean-Marie Nessi resides in France, Michael Carpenter resides in the United Kingdom and the remainder reside in the United States.

We have been advised by Bermuda counsel that there is doubt as to whether the courts of Bermuda would enforce judgments of U.S. courts obtained in actions against us or our directors and officers, predicated upon the civil liability provisions of the U.S. federal securities laws, or original actions brought in Bermuda against us or such persons predicated solely upon U.S. federal securities laws. Further, we have been advised by Bermuda counsel that there is no treaty in effect between the United States and Bermuda providing for the enforcement of judgments of U.S. courts in civil and commercial matters, and there are grounds upon which Bermuda courts may decline to enforce the judgments of U.S. courts. Some remedies available under the laws of U.S. jurisdictions, including some remedies available under the U.S. federal securities laws, may not be allowed in Bermuda courts as contrary to public policy in Bermuda. Because judgments of U.S. courts are not automatically enforceable in Bermuda, it may be difficult for our shareholders to recover against us based upon such judgments.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Company and its subsidiaries currently occupy office space as described below. As a result of the Flagstone acquisition, we own office space and buildings in Hyderabad, India and Luxembourg. We believe our current facilities and the leaseholds with respect thereto are sufficient for us to conduct our operations.

Legal entity	Location	Expiration date
Validus Holdings, Ltd.	Pembroke, Bermuda	December 31, 2021
Validus Research Inc.	Waterloo, Canada	March 31, 2020
Validus Research Inc.	Toronto, Canada	February 29, 2024
Validus Reaseguros, Inc.	Miami, Florida, USA	April 1, 2018
Validus Services, Inc.	New York, New York, USA	November 8, 2015
Talbot Underwriting Services (U.S.) Ltd.	New York, New York, USA	November 8, 2015
Talbot Holdings Ltd. and Talbot Underwriting Services Ltd.	London, England	June 22, 2024
Validus Reinsurance, Ltd.	Republic of Singapore	August 31, 2016
Talbot Risk Services Pte, Ltd.	Republic of Singapore	December 31, 2015
Talbot Underwriting (MENA) Ltd.	Dubai, United Arab Emirates	January 31, 2017
Validus Reinsurance (Switzerland) Ltd	Zurich, Switzerland	January 31, 2019
Western World Insurance Group, Inc.	Franklin Lakes, New Jersey, USA	May 31, 2016

Item 3. Legal Proceedings

During the normal course of business, the Company and its subsidiaries are subject to litigation and arbitration. Legal proceedings such as claims litigation are common in the insurance and reinsurance industry in general. The Company and its subsidiaries may be subject to lawsuits and regulatory actions in the normal course of business that do not arise from or directly relate to claims on reinsurance treaties or contracts or insurance policies.

Litigation typically can include, but is not limited to, allegations of underwriting errors or misconduct, employment claims, regulatory activity, shareholder disputes or disputes arising from business ventures. These events are difficult, if not impossible, to predict with certainty. It is Company policy to dispute all allegations against the Company and/or its subsidiaries that management believes are without merit.

As at December 31, 2014, the Company was not a party to, or involved in any litigation or arbitration that it believes could have a material adverse effect on the financial condition, results of operations or liquidity of the Company.

Executive Officers of the Company

The following table provides information regarding our executive officers and key employees as of February 24, 2015:

Name	Age	Position
Edward J. Noonan	56	Chairman of the Board of Directors and Chief Executive Officer of the Validus Group
Jeffrey D. Sangster	42	Executive Vice President and Chief Financial Officer
C.N. Rupert Atkin	56	Chief Executive Officer of the Talbot Group
Kean D. Driscoll	41	Executive Vice President and Chief Executive Officer of Validus Reinsurance, Ltd.
John J. Hendrickson	54	Director of Strategy, Risk Management and Corporate Development
Andrew E. Kudera	55	Executive Vice President and Chief Actuary
Robert F. Kuzloski	51	Executive Vice President and General Counsel
Michael R. Moore	45	Executive Vice President and Chief Accounting Officer
Romel Salam	48	Executive Vice President and Chief Risk Officer
Jonathan P. Ritz	47	Executive Vice President and Chief Operating Officer
Lixin Zeng	46	Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd.

Edward J. Noonan has been Chairman of our Board and the Chief Executive Officer of the Company since its formation. Mr. Noonan has over 30 years of experience in the insurance and reinsurance industry, serving most recently as the acting Chief Executive Officer of Global Indemnity plc (NASDAQ: GBLI) from February 2005 through October 2005 and as a member of the Board of Directors from December 2003 to May 2007. Mr. Noonan served as President and Chief Executive Officer of American Re-Insurance Company from 1997 to 2002, having joined American Re in 1983. Mr. Noonan also served as Chairman of Inter-Ocean Reinsurance Holdings of Hamilton, Bermuda from 1997 to 2002. Mr. Noonan is also a Director of Central Mutual Insurance Company and All American Insurance Company, both of which are property and casualty companies based in Ohio.

Jeffrey D. Sangster has served as Executive Vice President and Chief Financial Officer of the Company since February 2013. Mr. Sangster joined the Company in October 2006 and has served in various finance positions during that time, including Chief Accounting Officer and Chief Financial Officer of Validus Reinsurance, Ltd. Mr. Sangster has 17 years of experience in the reinsurance industry and was previously with Endurance, Centre Group and Ernst & Young. Mr. Sangster is a member of the Institute of Chartered Accountants in Bermuda and the Institute of Chartered Accountants in Manitoba.

C. N. Rupert Atkin began his career at the Alexander Howden Group in 1980 before moving to Catlin Underwriting Agencies in 1984. After six years at Catlin he left to join Talbot, then Venton Underwriting Ltd to start Syndicate 1183 as Active Underwriter. In November 2001, Mr. Atkin was made Director of Underwriting. Following the sale of Talbot to Validus in the summer of 2007 Mr. Atkin was appointed as Chief Executive Officer of Talbot. Mr. Atkin has served or is still serving on a variety of market bodies including chairing the Lloyd's Underwriters' Association and Joint War Risk Committee and being a member of the Lloyd's Insurance Services Board, Lloyd's Regulatory Board, Lloyd's Professional Standards Committee and Lloyd's Charities Trust Committee. Mr. Atkin was appointed to the Council of Lloyd's in 2007, Chairman of the Lloyd's Market Association in 2012 and Deputy Chairman of Lloyd's in 2014.

Kean D. Driscoll is the Chief Executive Officer of Validus Reinsurance, Ltd., the reinsurance segment for the Validus Group. He was a founding member of the Company, and previously served as Chief Underwriting Officer. Mr. Driscoll has 19 years of experience as a reinsurance underwriter, and was previously with Quanta Re, and Zurich Re N.A. (Converium). Mr. Driscoll holds a B.A. in Literature from Colgate University and an M.B.A. from Columbia University, where he graduated with Honors.

John J. Hendrickson has been a director of the Company since its formation. In February 2013, Mr. Hendrickson joined Validus Group as Director of Strategy, Risk Management and Corporate Development. Prior to this, Mr. Hendrickson was the Founder and Managing Partner of SFRi LLC, an independent investment and advisory firm specializing in the insurance industry. From 1995 to 2004, Mr. Hendrickson held various positions with Swiss Re, including as Member of the Executive Board, Head of Capital Partners (Swiss Re's Merchant Banking Division) and

Managing Partner of Securitas Capital. From 1985 to 1995, Mr. Hendrickson was with Smith Barney, the U.S. investment banking firm. Mr. Hendrickson has also served as a director of insurance and reinsurance companies, including serving as audit committee chair.

Andrew E. Kudera has served as Chief Actuary of the Company since January 2010. Previously, Mr. Kudera operated an independent actuarial consulting firm which served as corporate actuary and loss reserve specialist for Validus Reinsurance, Ltd. from its inception through to the end of 2008. Prior to establishing his own consulting firm, Mr. Kudera was the Chief Reserving Actuary for Endurance Specialty Holdings Ltd., a large international insurance and reinsurance company. Mr. Kudera has over 30 years of actuarial and financial management experience in the insurance industry, primarily in a consulting capacity. Mr. Kudera is a Fellow of the Casualty Actuarial Society, a Member of the American Academy of Actuaries, an Associate of the Society of Actuaries, and a Fellow of the Canadian Institute of Actuaries.

Robert F. Kuzloski joined the company in January 2009 and served as Executive Vice President and Chief Corporate Legal Officer of the Company until August of 2012 when he was appointed Executive Vice President and General Counsel of the Company. Prior to joining the Company in January of 2009, Mr. Kuzloski served as Senior Vice President and Assistant General Counsel of XL Capital Ltd. Prior to that, Mr. Kuzloski worked as an attorney at the law firm of Cahill Gordon & Reindel LLP where he specialized in general corporate and securities law, mergers and acquisitions and corporate finance.

Michael R. Moore serves as Executive Vice President and Chief Accounting Officer of the Company, a position he has held since June 2013. Mr. Moore has 20 years of experience, including 15 years in the insurance and reinsurance industry. Prior to this role, Mr. Moore served as a Senior Vice President, Corporate Operations at Axis Capital, Chief Accounting Officer at Endurance Specialty Holdings Ltd. and as a Senior Manager with Ernst & Young. Mr. Moore received a Bachelor of Commerce, with distinction, from the University of Alberta in 1993 and he is a Chartered Accountant and member of the Canadian Institute of Chartered Accountants.

Romel Salam serves as Executive Vice President and Chief Risk Officer of the Company, a position he has held since April 2013. He was promoted to his current role after serving for three years as Chief Actuary and Chief Risk Officer of Validus Reinsurance, Ltd, the reinsurance arm of Validus Group. Prior to joining the Company in 2010, Romel was a Senior Vice President at Transatlantic Reinsurance where he spent 20 years in positions of increasing responsibility. Romel is a Fellow of the Casualty of Actuarial Society and a Member of the American Academy of Actuaries.

Jonathan P. Ritz joined the Company in October 2010 and currently serves as Executive Vice President and Chief Operating Officer of the Company. Mr. Ritz has over 20 years of experience in the (re)insurance and brokerage industries. Most recently, Mr. Ritz served as Chief Operating Officer of IFG Companies-Burlington Insurance Group. Prior to IFG, Mr. Ritz served as Chief Operating Officer of the specialty lines division of ICAT Holdings LLC. From 2007 to 2008, Mr. Ritz was a Managing Director at Guy Carpenter and from 1997 to 2007 he held various positions with United America Insurance Group including Chief Operating Officer and Senior Vice President of ceded reinsurance.

Lixin Zeng, Ph.D., CFA serves as Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd. and has played a key role in AlphaCat since its formation in 2008. Prior to this role, he was Executive Risk Officer of Validus Reinsurance, Ltd., responsible for developing and executing the catastrophe risk strategy of the entire Validus Group. Mr. Zeng was one of the original employees at the founding of the Company in 2005. His prior positions include: Chief Catastrophe Risk Officer at the ACE Group from 2004 to 2005, Head of Development at Willis Re Inc. from 2001 to 2004, Analyst at EW Blanch Co. from 1998 to 2001 and Research Scientist at Arkwright Mutual Insurance Co from 1996 to 1998. Mr. Zeng has expertise in insurance portfolio optimization and risk management and has published multiple articles in professional journals on related topics. He has a Ph.D. in atmospheric sciences from the University of Washington where he graduated in 1996. He received a B.S. in Meteorology from Beijing University, graduating in 1990 and is a CFA charter holder.

Item 4. Mine Safety Disclosure—Not Applicable

PART II

All amounts presented in this part are in U.S. dollars except as otherwise noted.

Item 5. Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

The Company’s common shares, $0.175 par value per share, are listed on the New York Stock Exchange under the symbol “VR.”

The following tables set forth the high and low sales prices per share, as reported on the New York Stock Exchange Composite Tape, of the Company’s common shares per fiscal quarter for the two most recent fiscal years.

	High	Low
2014:		
1st Quarter	$40.20	$34.68
2nd Quarter	$38.43	$36.01
3rd Quarter	$39.72	$36.16
4th Quarter	$42.35	$37.45

	High	Low
2013:		
1st Quarter	$37.80	$34.20
2nd Quarter	$40.06	$33.40
3rd Quarter	$37.18	$34.10
4th Quarter	$40.71	$36.82

There were approximately 43 record holders of our common shares as of December 31, 2014. This figure does not represent the actual number of beneficial owners of our common shares because such shares are frequently held in “street name” by securities dealers and others for the benefit of individual owners.

Performance Graph

Set forth below is a line graph comparing the percentage change in the cumulative total shareholder return, assuming the reinvestment of dividends, over the five year period through December 31, 2014 as compared to the cumulative total return of the S&P 500 Stock Index and the cumulative total return of an index of the Company’s peer group. The peer group index is comprised of the following companies: Alleghany Corporation, Allied World Assurance Company Holdings, Ltd., Arch Capital Group, Ltd., Argo Group International Holdings, Ltd., Aspen Insurance Holdings Limited, AXIS Capital Holdings Limited, Endurance Specialty Holdings Ltd., Everest Re Group, Ltd., Montpelier Re Holdings Ltd., PartnerRe Ltd., Platinum Underwriters Holdings Ltd., and RenaissanceRe Holdings Ltd.

Dividend Policy

On February 3, 2015, the Company approved an increase in its regular quarterly dividend to $0.32 from $0.30 per common share and common share equivalent for which each outstanding warrant is exercisable.

We are a holding company and have no direct operations. Our ability to pay dividends depends, in part, on the ability of our principal operating subsidiaries to pay dividends to us. As a holding company, Validus Holdings, Ltd.'s principal source of income is dividends or other sources of permitted payments from its subsidiaries. These funds provide the cash flow required for dividend payments to the Company's shareholders. During 2015, the Bermuda regulated subsidiaries have the ability to distribute up to $968.2 million of unrestricted net assets as dividend payments and/or return of capital to Validus Holdings, Ltd. without prior regulatory approval. The Companies Act limits the Company’s ability to pay dividends and distributions to shareholders. Total statutory capital and surplus and total statutory capital of our subsidiaries are relevant to the calculation of net assets that are free of restriction for the payment of dividends and/or return of capital to Validus Holdings Ltd. In addition, the maximum dividend that may be paid to the Company by Western World without obtaining prior approval is $45.2 million. See “Risk Factors, Risks Related to Ownership of Our Common Shares." Because Validus Holdings, Ltd. is a holding company and substantially all of our operations are conducted by our main operating subsidiaries our ability to meet any ongoing cash requirements and to pay dividends will depend on our ability to obtain cash dividends or other cash payments or obtain loans from these subsidiaries.

Share Repurchase Program

The Company has repurchased approximately 71.4 million common shares for an aggregate purchase price of $2.3 billion from the inception of the share repurchase program to February 20, 2015.

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

On February 3, 2015, the Board of Directors of the Company approved an increase to the Company's common share repurchase authorization to $750.0 million. This amount is in addition to the $2.3 billion of common shares repurchased by the Company through February 3, 2015 under its previously authorized share repurchase programs. The repurchase program may be modified, extended or terminated by the Board of Directors at any time. The remaining amount available under the current share repurchase authorization is $739.6 million as of February 20, 2015.

Share repurchases include repurchases by the Company of shares, from time to time, from employees in order to facilitate the payment of withholding taxes on restricted shares which have vested. We repurchase these shares at their fair market value, as determined by reference to the closing price of our common shares on the day the restricted shares vested.

		Share Repurchase Activity by Quarter		
Effect of share repurchases:	As at December 31, 2013 (cumulative)	Quarter ended March 31, 2014	Quarter ended June 30, 2014	Quarter ended September 30, 2014
	(Dollars in thousands, except share and per share amounts)			
Aggregate purchase price (a)	$1,720,349	$197,339	$—	$89,187
Shares repurchased	56,805,310	5,366,672	—	2,330,428
Average price (a)	$30.29	$36.77	$—	$38.27
Estimated net cumulative accretive (dilutive) impact on:				
BV per diluted common share (b)		$2.58	$2.93	$3.00
Diluted EPS—Quarter (c)		$0.60	$0.61	$0.12
Estimated quarterly net accretive (dilutive) impact on:				
BV per diluted common share		$0.04	$—	$0.01

		Fourth Quarter Share Repurchase Activity			
Effect of share repurchases:	As at September 30, 2014 (cumulative)	October	November	December	Quarter ended December 31, 2014
	(Dollars in thousands, except share and per share amounts)				
Aggregate purchase price (a)	$2,006,875	$65,633	$73,454	$85,339	$224,426
Shares repurchased	64,502,410	1,663,577	1,815,805	2,063,712	5,543,094
Average price (a)	$31.11	$39.45	$40.45	$41.35	$40.49
Maximum number of shares that may yet be purchased under the program (d)		5,171,341	3,085,374	1,034,415	1,034,415
Estimated net cumulative accretive (dilutive) impact on:					
BV per diluted common share (b)					$3.35
Diluted EPS—Quarter (c)					$0.53
Estimated quarterly net accretive (dilutive) impact on:					
BV per diluted common share					$(0.05)

	Share Repurchase Activity Post Year End				
Effect of share repurchases:	As at December 31, 2014 (cumulative)	January	February	As at February 20, 2015	Cumulative to Date Effect
	(Dollars in thousands, except share and per share amounts)				
Aggregate purchase price(a)	$2,231,301	$43,100	$10,382	$53,482	$2,284,783
Shares repurchased	70,045,504	1,072,462	247,438	1,319,900	71,365,404
Average price(a)	$31.86	$40.19	$41.96	$40.52	$32.02

(a) Share transactions are on a trade date basis through February 20, 2015 and are inclusive of commissions. Average share price is rounded to two decimal places.

(b) As the average price per share repurchased during the periods from 2009 at the inception of the share repurchase program through to 2014 was lower than the book value per common share, the repurchase of shares increased the ending book value per share.

(c) The estimated impact on earnings per diluted share was calculated by comparing reported results versus i) net income per share plus an estimate of lost net investment income on the cumulative share repurchases divided by ii) weighted average diluted shares outstanding excluding the weighted average impact of cumulative share repurchases. The impact of cumulative share repurchases was accretive to earnings per diluted share.

(d) The maximum number of shares that may yet be purchased under the program is calculated using the month end closing price.

Item 6. Selected Financial Data

The summary Consolidated Statements of Comprehensive Income data for the years ended December 31, 2014, December 31, 2013, December 31, 2012, December 31, 2011 and December 31, 2010 and the summary Consolidated Balance Sheet data as of December 31, 2014, December 31, 2013, December 31, 2012, December 31, 2011 and December 31, 2010 are derived from our audited Consolidated Financial Statements. The Company was formed on October 19, 2005 and completed the acquisitions of Talbot, IPC, Flagstone and Western World on July 2, 2007, September 4, 2009, November 30, 2012 and October 2, 2014, respectively. Flagstone is included in the Company's consolidated results for the one month ended December 31, 2012 and for subsequent fiscal year ends. Western World is included in the Company's consolidated results from the October 2, 2014 date of acquisition.

(Dollars in thousands, except share and per share amounts)	Years Ended December 31,				
	2014	2013	2012	2011	2010
Revenues					
Gross premiums written	$2,363,286	$2,401,106	$2,166,440	$2,124,691	$1,990,566
Reinsurance premiums ceded	(309,233)	(372,585)	(307,506)	(289,241)	(229,482)
Net premiums written	2,054,053	2,028,521	1,858,934	1,835,450	1,761,084
Change in unearned premiums	(51,649)	73,524	14,282	(33,307)	39
Net premiums earned	2,002,404	2,102,045	1,873,216	1,802,143	1,761,123
Gain on bargain purchase, net of expenses (a)	—	—	17,701	—	—
Net investment income	100,076	96,072	107,936	112,296	134,103
Net realized gains on investments	23,095	3,258	18,233	28,532	32,498
Net unrealized (losses) gains on investments	(57,973)	(58,481)	17,585	(19,991)	45,952
Income (loss) from investment affiliate	8,411	4,790	(964)	—	—
Other insurance related income and other income	19,739	8,343	22,396	5,718	5,219
Foreign exchange (losses) gains	(10,630)	2,505	4,798	(22,124)	1,351
Total revenues	2,085,122	2,158,532	2,060,901	1,906,574	1,980,246
Expenses					

Losses and loss expenses	772,049	793,932	999,446	1,244,401	987,586
Policy acquisition costs	340,556	360,310	334,698	314,184	292,899
General and administrative expenses	329,792	315,265	263,652	197,497	209,290
Share compensation expenses	33,073	27,630	26,709	34,296	28,911
Finance expenses	63,854	64,177	53,857	54,817	55,870
Transaction expenses (b)	8,096	—	—	17,433	—
Total expenses	1,547,420	1,561,314	1,678,362	1,862,628	1,574,556
Income before taxes, income from operating affiliates and (income) attributable to operating affiliate investors	537,702	597,218	382,539	43,946	405,690

Tax expense	(155)	(383)	(2,501)	(824)	(3,126)
Income from operating affiliates	17,723	14,289	12,580	—	—
(Income) attributable to operating affiliate investors	(109,399)	(68,763)	—	—	—
Net income	445,871	542,361	392,618	43,122	402,564
Net loss (income) attributable to noncontrolling interest	35,464	(9,695)	15,820	(21,793)	—
Net income available to Validus	481,335	532,666	408,438	21,329	402,564
Other comprehensive (loss) income					
Change in foreign currency translation adjustments	(7,501)				