XL GROUP PLC
Form 10-K
February 27, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2011

OR

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

For the transition period from _____ to _____

Commission file number 1-10804

XL GROUP

Public Limited Company

(Exact name of registrant as specified in its charter)

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

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

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

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

None

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

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

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

Documents Incorporated by Reference

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

XL GROUP PLC

TABLE OF CONTENTS

		Page
	PART I	
Item 1.	Business	1
Item 1A.	Risk Factors	27
Item 1B.	Unresolved Staff Comments	44
Item 2.	Properties	44
Item 3.	Legal Proceedings	44
Item 4.	Mine Safety Disclosures	45
	PART II	
Item 5.	Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	48
Item 6.	Selected Financial Data	50
Item 7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	52
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	106
Item 8.	Financial Statements and Supplementary Data	114
Item 9.	Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	211
Item 9A.	Controls and Procedures	211
Item 9B.	Other Information	211
	PART III	
Item 10.	Directors, Executive Officers and Corporate Governance	212
Item 11.	Executive Compensation	212
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	212
Item 13.	Certain Relationships and Related Transactions, and Director Independence	212
Item 14.	Principal Accounting Fees and Services	212
	PART IV	
Item 15.	Exhibits, Financial Statement Schedules	213

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

PART I

ITEM 1. BUSINESS

HISTORY

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

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

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

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

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

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

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

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

SEGMENTS

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

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

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

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

Insurance Segment

General

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

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

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

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

International Property and Casualty

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

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

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

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

North America Property and Casualty

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

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

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

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

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

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

Global Professional Lines

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

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

Global Specialty Lines

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

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

Marine and offshore energy coverage includes marine hull and machinery, marine war, marine excess liability, cargo and offshore energy insurance. Fine art and specie coverages include fine art and other collections, jewelers block, cash in transit and related coverages for financial institutions. Equine products specialize in providing bloodstock and livestock insurance. Product recall

coverages include product contamination for the food and beverage sector and end-product consumer goods and product guarantee aimed at component part manufacturers.

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

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

Underwriting

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

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

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

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

Engineering

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

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

Reinsurance Ceded

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

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

Premiums

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

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

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

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

Competition

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

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

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

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

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

Marketing and Distribution

The majority of Insurance segment business originates via a large number of international, national and regional producers, acting as the brokers and representatives of current and prospective policyholders. This channel is supported by the Company s Global Distribution and Network Unit, which consists of sales and marketing representatives in key markets throughout the world, representing all of the Company s products in collaboration with the four business units. A portion of Insurance segment business is

also marketed and underwritten by general agents and a portion by independent agents acting on behalf of the Company. Typically, all such producers, general agents and independent agents receive commission payments from the Company for their services, which payments are calculated as a percentage of the gross premium paid by the policyholder on an account-by-account basis. A certain portion of business originating from producers is submitted on a fee basis under which the producer is compensated by a fee paid to it by its policyholder client. From time to time, the Company also considers requests for commissions from a producer, with disclosure by the producer to the policyholder-client, where the producer receives a fee from the policyholder-client. The Company evaluates such requests on a case-by-case basis.

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

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

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

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

Claims Administration

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

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

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

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

Reinsurance Segment

General

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

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

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

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

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

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

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

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

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

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

7

Underwriting

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

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

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

Reinsurance Retroceded

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

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

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

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

Premiums

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

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

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

(2) Certain reclassifications have been made to conform to current year presentation.

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

Competition

The Company competes globally in the property and casualty markets.

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

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

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

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

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

Marketing and Distribution

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

Company s major brokers.

Claims Administration

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

Life Operations Segment

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

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

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

The portfolio has three particularly significant components:

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

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

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

Underwriting & Claims Administration

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

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

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

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

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

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

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

Reinsurance Retroceded

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

10

Premiums

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

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

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

Competition

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

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

Marketing and Distribution

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

Other Financial Lines Business

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

UNPAID LOSSES AND LOSS EXPENSES

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

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

The tables below present the development of the Company s unpaid losses and loss expense reserves on both a net and gross basis. The cumulative redundancy (deficiency) calculated on a net basis differs from that calculated on a gross basis. As different reinsurance programs cover different underwriting years, net and gross loss experience will not develop proportionately. The top lines of the tables show the estimated liability, net of reinsurance recoveries, as at the year end balance sheet date for each of the indicated years. This represents the estimated amounts of losses and loss expenses, including IBNR, arising in the current and all prior years that are unpaid at the year end balance sheet date

of the indicated year. The tables show the re-estimated amount of the previously recorded reserve liability based on experience as of the year end balance sheet date of each succeeding year. The estimate changes as more information becomes known about the frequency and severity of claims for individual years. The cumulative redundancy (deficiency) represents the aggregate change with respect to that liability originally estimated. The lower portion of the first table also reflects the cumulative paid losses relating to these reserves. Conditions and trends that have affected development of liabilities in the past may

not necessarily occur in the future. Accordingly, it may not be appropriate to extrapolate redundancies or deficiencies into the future, based on the tables below. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Cautionary Note Regarding Forward-Looking Statements.

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

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

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

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

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

Reconciliation of Unpaid Losses and Loss Expenses

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

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

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

Current year net losses incurred

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

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

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

Prior year net losses incurred

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

Gross

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

Net

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

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

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

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

The Company had net favorable prior year reserve development in property and casualty operations of $284.9 million, $372.9 million and $284.7 million for the years ended December 31, 2011, 2010 and 2009, respectively. See the Income Statement Analysis

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

Net loss reserves (disposed) acquired

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

Exchange rate effects

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

Net paid losses

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

Other loss related information

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

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

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

INVESTMENTS

Investment structure and strategy

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

Strategic Asset Allocation

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

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

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

Investment Portfolio Structure

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

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

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

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

1) P&C investment portfolio

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

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

2) Life investment portfolio

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

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

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

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

Implementation of investment strategy

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

Investment performance

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

Investment portfolio credit ratings, duration and maturity profile

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

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

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

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

17

Enterprise Risk Management

Risk Management Framework

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

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

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

Risk Governance

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

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

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

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

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

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

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

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

18

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

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

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

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

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

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

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

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

Risk Appetite Management

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

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

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

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

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

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

19

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

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

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

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

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

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

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

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

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

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

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

Inaccurate assumption of event frequency and severity;

Inaccurate or incomplete data;

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

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

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

A change in the judicial climate.

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

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

Impact of ERM Processes

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

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

REGULATION

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

Bermuda Operations

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

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

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

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

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

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

The Insurance Amendment (No. 3) Act 2010 came into force on December 31, 2010 and created five new classes of long-term insurance licenses: Class A Class E. Prior to the enactment of this amendment, a (re)insurer carrying on long-term insurance was registered simply as a long-term (re)insurer. Existing long-term insurers were required to re-register under the appropriate new classification system. Effective December 31, 2011, further amendments were made to the Act to extend enhanced solvency reporting

requirements to Class E (re)insurers. Class E insurers are now required to prepare and file with the BMA, in addition to statutory financial statements, financial statements prepared in accordance with GAAP or IFRS.

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

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

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

United States

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

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

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

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

23

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

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

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

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

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

Other International Operations

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

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

European Union

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

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

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

their respective shareholders unless the applicable entity has profits available for distribution.

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

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

Swiss Operations

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

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

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

EMPLOYEES

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

AVAILABLE INFORMATION

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

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

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

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

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

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

ITEM 1A. RISK FACTORS

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

We may develop products that insure risks we have not previously insured or contain new coverage or coverage terms.

We may refine our underwriting processes.

We may seek to expand distribution channels.

We may focus on geographic markets within or outside of the United States where we have had relatively little or no market share.

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

Demand for new products or in new markets may not meet our expectations.

To the extent we are able to market new products or expand in new markets, our risk exposures may change, and the data and models we use to manage such exposures may not be as sophisticated as those we use in existing markets or with existing products. This, in turn, could lead to losses in excess of our expectations.

Efforts to develop new products or markets have the potential to create or increase distribution channel conflict.

In connection with the conversion of existing policyholders to a new product, some policyholders pricing may increase, while the pricing for other policyholders may decrease, the net impact of which could negatively impact retention and margins.

To develop new products or markets, we may need to make substantial capital and operating expenditures, which may also negatively impact results in the near term.

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

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

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

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

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

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

We invest a portion of our investment portfolio in common stock or equity-related securities, including alternative funds and private equity funds. The value of these assets fluctuates, due to changes in the equity and credit markets along with other factors. In times of economic weakness, the market value and liquidity of these assets may decline, and may impact net income, capital and cash flows. In addition, certain of the products offered by our Life operations offer fixed guaranteed returns while debt and equity yields may continue to decline. In addition, the amount of earnings from alternative funds and private investment funds are not earned evenly across the year, or even from year to year. As a result, the amount of earnings that we record from these investments may vary

substantially from quarter to quarter. The timing of distributions from such private investment funds depends on particular events relating to the underlying investments. The ability of an alternative fund to satisfy any redemption request from its investors depends on the underlying liquidity of the alternative fund s investments. As a result, earnings, distributions and redemptions from these two asset classes may be more difficult to predict.

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

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

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

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

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

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

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

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

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

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

31

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Our reliance on brokers subjects us to credit risk.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

36

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

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

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

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

Consolidation in the insurance industry could adversely impact us.

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

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

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

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

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

When we acquire an entity, the excess of the purchase price over the net identifiable assets acquired is allocated to goodwill. We conduct impairment tests on our reported goodwill at least annually or more frequently if impairment indicators exist. In performing a goodwill impairment test, we use various methods and make various assumptions to determine the fair value of our reporting units, including the determination of expected future cash flows and/or profitability of such reporting units, and we take into account market value multiples and/or cash flows of entities that we deem to be comparable in nature, scope or size to our reporting units. However, expected future cash flows and/or profitability may be materially and negatively impacted as a result of, among other things, a decrease in renewal activity and new business

opportunities, a decrease in retention or our underwriting teams, lower-than-

expected yields and/or cash flows from our investment portfolio, higher-than-expected claims activity and magnitude of incurred losses and general economic factors that impact the reporting unit. In addition, previously determined market value multiples and/or cash flows may no longer be relevant as a result of these potential factors. As a result of these potential changes, the estimated fair value of one or more of our reporting units may decrease, causing the carrying value of the net assets assigned to the reporting unit to exceed the fair value of such net assets. If we determine an impairment exists, we adjust the carrying value of goodwill to its implied fair value. The impairment charge is recorded in our income statement in the period in which the impairment is determined. If we are required in the future to write down additional goodwill, our financial condition and results of operations would be negatively affected. In connection with fair value measurements and the accounting for goodwill, the use of generally accepted accounting principles requires management to make certain estimates and assumptions. Significant judgment is required in making these estimates and assumptions, and actual results may ultimately be materially different from such estimates and assumptions. The Company completed an interim impairment test during the fourth quarter of 2011 which resulted in a non-cash goodwill impairment charge of $429.0 million. The charge related to the Insurance segment. The remaining goodwill balance carried in our consolidated financial statements at December 31, 2011 is $391.5 million.

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

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

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

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

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

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

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

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

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

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

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

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

38

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

intended to hinder, delay or defraud its creditors; or

received less than reasonably equivalent value or fair value consideration for such release; and either:

was insolvent or rendered insolvent by reason of such occurrence; or

was engaged in a business or transaction for which its remaining assets constituted unreasonably small capital; or

intended to incur, or believed that it would incur, debts beyond its ability to pay such debts as they mature.

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

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

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

40

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Transfers of our ordinary shares effected by means of the transfer of book entry interests in DTC will not be subject to Irish stamp duty. The majority of our ordinary shares will be traded through DTC, either directly or through brokers who hold such ordinary shares on behalf of customers through DTC. However, if you hold your ordinary shares directly rather than beneficially through DTC (or through a broker that

holds your ordinary shares through DTC), any transfer of your ordinary shares could be subject

to Irish stamp duty (currently at the rate of 1% of the higher of the price paid or the market value of the ordinary shares acquired). Payment of Irish stamp duty is generally a legal obligation of the transferee. The potential for stamp duty could adversely affect the price of our ordinary shares.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

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

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

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

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

ITEM 3. LEGAL PROCEEDINGS

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

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

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

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

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

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

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

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

Executive Officers of the Registrant

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

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

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

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

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

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

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

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

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

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

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

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

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

PART II

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

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

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

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

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

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

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

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

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

Purchases of Equity Securities by the Issuer and Affiliate Purchases

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

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

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

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

Ordinary Share Performance Graph

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

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

ITEM 6. SELECTED FINANCIAL DATA

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Index

Executive Overview	53
Results of Operations and Key Financial Measures	55
Significant Items Affecting the Results of Operations	57
Other Key Focuses of Management	60
Critical Accounting Policies and Estimates	63
Segments	75
Income Statement Analysis	75
Insurance	75
Reinsurance	78
Life Operations	80
Investment Activities	81
Investment Performance	82
Net realized gains and losses on investments and other-than-temporary declines in the value of investments	82
Net realized and unrealized gains and losses on derivative instruments	83
Other Revenues and Expenses	83
Balance Sheet Analysis	85
Investments	85
Gross and net unrealized gains and losses on investments	86
Fair Value Measurements of Assets and Liabilities	90
Unpaid Losses and Loss Expenses	92
Unpaid Losses and Loss Expenses Recoverable and Reinsurance Balances Receivable	92
Liquidity and Capital Resources	94
Holding Company Liquidity	94
Sources of Liquidity for the Company	95
Capital Resources	97
Covenants	102
Cross-Default and Other Provisions in Debt Instruments	102
Long-Term Contractual Obligations	103
Variable Interest Entities and Other Off-Balance Sheet Arrangements	104
Recent Accounting Pronouncements	104
Return on Ordinary Shareholders Equity Calculation	104
Cautionary Note Regarding Forward-Looking Statements	105

EXECUTIVE OVERVIEW

Background

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

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

Impact of Recent Natural Catastrophes

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

Underwriting Environment

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

Insurance - Underwriting Environment

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

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

Reinsurance - Underwriting Environment

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

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

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

2012 Underwriting Outlook

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

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

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

Insurance - 2012 Underwriting Outlook

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

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

Reinsurance - 2012 Underwriting Outlook

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

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

Investment Environment

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

RESULTS OF OPERATIONS AND KEY FINANCIAL MEASURES

Results of Operations

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

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

Key Financial Measures

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

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

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

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

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

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

Underwriting profit property and casualty operations

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

Combined ratio property and casualty operations

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

The Company s combined ratio for the year ended December 31, 2010 is higher than for the same period in the previous year, primarily as a result of an increase in the loss and loss expense ratio, partially offset by a marginal decrease in the underwriting

expense ratio. The loss and loss expense ratio has increased as a result of higher levels of catastrophe losses and other large loss events in both the insurance and reinsurance segments. For further information on the combined ratio, see Income Statement Analysis below.

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

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

Book value per ordinary share

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

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

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

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

Return on average ordinary shareholders equity

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

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

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

SIGNIFICANT ITEMS AFFECTING THE RESULTS OF OPERATIONS

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

1) The impact of significant large natural catastrophe activity;

2) Continuing competitive factors impacting the underwriting environment;

3) Net favorable prior year loss development;

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

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

1. The impact of significant large natural catastrophe activity

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

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

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

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

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

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

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

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

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

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

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

2. Continuing competitive factors impacting the underwriting environment

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

3. Net favorable prior year loss development

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

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

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

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

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

4. Market movement impacts on the Company s investment portfolio

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

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

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

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

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

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

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

OTHER KEY FOCUSES OF MANAGEMENT

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

Capital Management

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

Buybacks of Ordinary Shares

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

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

Sale of 5.75% Senior Notes

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

Repayment of the XLCFE Notes

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

Equity Security Units

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

60

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

Series C Preference Ordinary Shares

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

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

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

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

Series D Preference Ordinary Shares

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

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

Series E Preference Ordinary Shares

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

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

Risk Management

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

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

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

(2) Probable maximum losses include secondary uncertainty which incorporates variability around the expected probable maximum loss for each event, does not represent the Company s maximum potential exposures and are pre-tax.
See Significant Items Affecting the Results of Operations - 1) The impact of significant large natural catastrophe activity above.

Regulatory Change

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

Critical Accounting Policies and Estimates

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

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

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

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

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

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

Case Reserves

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

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

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

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

63

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

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

IBNR Reserves

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

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

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

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

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

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

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

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

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

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

(1) high layer excess casualty insurance;

(2) casualty reinsurance; and

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

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

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

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

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

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

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

65

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

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

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

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

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

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

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

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

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

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

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

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

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

(1) Other specialty lines within the Insurance segment includes: environmental, programs, equine, warranty, and excess and surplus lines.

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

(3) The range for the total Insurance and Reinsurance segment reserves is narrower than the sum of the ranges for the lines of business shown in the table due to diversification benefits across the lines of business. In addition, the total for each of the Insurance and Reinsurance segments does not include reserves relating to structured indemnity business as the Company does not develop reserve ranges for this line of business.

(4) Within the Reinsurance segment, casualty-other and casualty-professional lines of business are shown in the aggregate.

There are factors that would cause reserves to increase or decrease within the context of the range provided. The magnitude of any change in ultimate losses would be determined by the magnitude of any changes to the Company s assumptions or combined impact of changes in

assumptions. Factors that would increase reserves include, but are not limited to, increases in claim severity, increases in expected level of reported claims, changes to the regulatory environment which expand the exposure insured by the Company, changes in the litigation environment that increase claim awards, filings or verdicts, unexpected increases in loss inflation, and/or new types of claims being pursued against the Company. Factors that would decrease reserves include, but are not limited to, decreases in claim severity, reductions in the expected level of reported claims, changes to the regulatory environment which contract the exposure insured by the Company, changes in the litigation environment that decrease claim awards, filings or verdicts, and/or unexpected decreases in loss inflation.

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

one year run-off period. The high and low end points of the ranges set forth in the above table are such that there is a 10% modeled probability that the reserve will develop higher than the high point and a 10% modeled probability that the reserve will develop lower than the low point.

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

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

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

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

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

Unpaid losses and loss expenses recoverable

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

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

2) Future Policy Benefit Reserves

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

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

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

68

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

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

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

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

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

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

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

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

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

69

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

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

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

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

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

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

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

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

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

Credit loss methodology structured credit

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

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

(1) Non-Agency RMBS

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

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

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

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

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

(2) Core CDOs

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

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

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

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

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

(3) Other structured credit assets classes

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

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

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

Credit loss analysis corporate sector securities

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

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

4) Income Taxes

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

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

5) Goodwill and Other Intangible Assets

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

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

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

6) Reinsurance Premium Estimates

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

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

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

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

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

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

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

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

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

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

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

Segments

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

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

Income Statement Analysis

Insurance

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

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

* NM Not Meaningful

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

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

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

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

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

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

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

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

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

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

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

Gross:

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

Net:

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

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

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

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

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

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

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

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

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

Reinsurance

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

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

* NM Not meaningful

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

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

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

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

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

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

78

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

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

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

Gross:

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

Net:

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

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

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

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

The decrease in the underwriting expense ratio during the year ended December 31, 2011 as compared to the same period of 2010 was due to a decrease in the operating expense ratio of 1.2 points (10.5% as compared to 11.7%) and a reduction in the acquisition expense ratio of 1.9

points (19.5% as compared to 21.4%). The decrease in the operating expense ratio was due to lower compensation costs in the year ended December 31, 2011 partially offset by increased information technology expenses associated with projects such as Solvency II. The decrease in the acquisition expense ratio was mainly due to the U.S. crop program where fees received were higher and profit commissions paid were lower in the year ended December 31, 2011 as compared to the same period of 2010 and profit and sliding scale commissions associated with development in Latin America.

The decrease in the underwriting expense ratio for the year ended December 31, 2010 compared to the same period in 2009 was due to a decrease in the acquisition expense ratio of 0.4 points (21.4% as compared to 21.8% in 2009), and by a decrease in the operating expense ratio of 0.3 points (11.7% as compared to 12.0% in 2009). The decrease in the acquisition expense ratio was a result of reduced net earned premiums in relation to the credit and bond book of business in Europe following a decision to exit these lines in 2010, which carries very high acquisition costs combined with reinstatement premium adjustments. The decrease in the operating expense ratio was as a result of cost savings associated with the Company s expense reduction initiatives announced in the third quarter of 2008 and first quarter of 2009.

Net results from structured reinsurance products include certain structured indemnity contracts that are accounted for as deposit contracts. Net results from these contracts have increased during the year ended December 31, 2011 as compared to the same period of 2010 due to higher interest expense in the prior year. This higher interest expense was due to an accretion rate adjustment recorded in the third quarter of 2010 based on changes in expected cash flows and payout patterns on one of the larger structured indemnity contracts. Net results from these products for the year ended December 31, 2010 decreased compared to the same period in 2009. This decrease was mainly due to lower net investment income as a result of lower yields and a smaller investment base, which is reflective of the run off nature of this line of business, combined with the higher 2010 year interest expense already outlined above.

Fee income and other increased during the year ended December 31, 2011 as compared to same period of 2010 due in part to the amendment to the sales proceeds for the renewal rights of the European life, accident and health business, resulting in a charge for the prior year period. In addition, fees earned in Latin America increased during 2011 due to the extension in duration for some treaties. Fee income and other decreased by $3.7 million in 2010 as compared to 2009, which included the sale of underwriting year 2009 renewal rights for the European life, accident and health business.

Life Operations

During 2009, the Company completed a strategic review of its life reinsurance business. In relation to this initiative, the Company sold the renewal rights to its Continental European short-term life, accident and health business in December 2008. The Company also announced in March 2009 that it would run-off its existing book of U.K. and Irish traditional life and annuity business, and not accept new business. In addition, during July 2009, the Company entered into an agreement to sell its U.S. life reinsurance business. The transaction closed during the fourth quarter of 2009. In December 2009, the Company entered into an agreement to novate and recapture a number of U.K. and Irish term assurance and critical illness treaties. The transaction closed during the fourth quarter of 2009. During the first quarter of 2010, the Company entered into an agreement to recapture three U.K. and Irish term assurance treaties, and this transaction closed in March 2010. An agreement to recapture future premiums and liabilities on two retro pool treaties was consummated in November 2010.

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

The following table summarizes the contribution from the Life operations segment:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009
Gross premiums written	$ 394,555	(4.2)%	$ 411,938	(28.5)%	$ 576,162
Net premiums written	362,362	(5.2)%	382,075	(28.3)%	532,852
Net premiums earned	363,018	(5.2)%	382,924	(31.0)%	555,101
Claims and policy benefits	(535,074)	4.1%	(513,833)	(24.2)%	(677,562)
Acquisition costs	(40,318)	(17.9)%	(49,104)	(36.8)%	(77,689)
Operating expenses	(9,311)	(11.1)%	(10,470)	(34.6)%	(16,009)
Net investment income	318,061	1.6%	313,172	(5.8)%	332,425
Net fee income and other	219	(12.0)%	249	(14.1)%	290
Realized and unrealized (losses) on investments	(89,999)	65.3%	(54,444)	(76.6)%	(232,375)
Contribution from Life operations	$ 6,596	(90.4)%	$ 68,494	NM*	$ (115,819)

* NM Not Meaningful

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

	2011	2010	2009

(U.S. dollars in thousands)	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned	Gross Premiums Written	Net Premiums Written	Net Premiums Earned
Other Life	$ 232,754	$ 230,130	$ 230,786	$ 256,703	$ 255,056	$ 255,905	$ 413,831	$ 400,345	$ 422,594
Annuity	161,801	132,232	132,232	155,235	127,019	127,019	162,331	132,507	132,507
Total	$ 394,555	$ 362,362	$ 363,018	$ 411,938	$ 382,075	$ 382,924	$ 576,162	$ 532,852	$ 555,101

Gross premiums written decreased by 4.2% during the year ended December 31, 2011 compared to the same period of 2010, driven predominantly by the Other Life business. The decrease was in line with the run-off expectations following the recapture of a number of term assurance treaties during the first and fourth quarters of 2010, partially offset by favorable foreign exchange movements. Gross premiums written relating to annuity business increased due to favorable foreign exchange rate movements. Ceded premiums written increased due to foreign exchange movements. Gross premiums written relating to total life business decreased by

$164.2 million in the year ended December 31, 2010 as compared to the same period in 2009 mainly due to a $122.1 million decrease as a result of the novation of a long-term care treaty and the novation/recapture of a number of term assurance treaties during the second half of 2009 and during the first and fourth quarters of 2010, together with the sale of the U.S. business during the fourth quarter of 2009 Ceded premiums written decreased by $13.4 million due to run-off of the short-term life, accident and health business, and following the closure of the U.S. business in 2009.

Net premiums earned decreased by 5.2% during the year ended December 31, 2011 compared to the same period of 2010 and in the year ended December 31, 2010 decreased by 31.0% as compared to the same period in 2009. The decreases in 2011 and 2010 were consistent with the movements in total gross and net premiums written as described above.

Claims and policy benefit reserves were higher by 4.1% during the year ended December 31, 2011, compared to the same period of 2010, primarily due to adverse foreign exchange impacts and due to the prior year experiencing reserve releases on recaptured treaties that were not repeated this year. Claims and policy benefit reserves decreased by 24.2% in the year ended December 31, 2010 as compared to the same period in 2009, primarily as a result of the factors noted above affecting gross and net premiums written.

Acquisition costs decreased by 17.9% during the year ended December 31, 2011 compared to the same period of 2010, largely due to the recaptured treaties in the prior year and run-off expectations outlined above. Acquisition costs decreased by 36.8% during the year ended December 31, 2010 as compared to the same period in 2009, largely as a result of the absence of novated/recaptured treaties from the core long-term portfolio and the absence of the U.S. business; as well as decreases in line with run-off expectations.

Operating expenses decreased by 11.1% during the year ended December 31, 2011 compared to the same period of 2010 due mainly to lower compensation expenses as a result of severance costs in 2010 following the decision to place this business into run-off. Operating expenses decreased by 34.6% in the twelve months ended December 31, 2010 as compared to the same period in the prior year mainly due to lower compensation expenses resulting from lower headcount and lower costs related to acquisition of new business.

Net investment income is included in the calculation of contribution from Life operations, as it relates to income earned on portfolios of separately identified and managed life investment assets and other allocated assets. Net investment income increased by 1.6% in the year ended December 31, 2011 compared to the same period of 2010, primarily due to positive foreign exchange impact, but was broadly in line with expected returns in underlying currencies. Net investment income decreased by 5.8% in the year ended December 31, 2010, as compared to the same period in 2009, primarily as a result of negative exchange impact, as well as the absence of U.S. business in 2010.

The realized losses on investments within the Life portfolio relate primarily to the sale of European hybrids and subordinated debt in European financial institutions. See Net Realized Gains and Losses and Other-than-Temporary Declines in the Value of Investments below for an analysis of the Company s total realized losses on investments during the year ended December 31, 2011.

Investment Activities

The following table illustrates the change in net investment income from P&C operations, net income (loss) from investment fund affiliates, net realized (losses) on investments, and net realized and unrealized (losses) on investment and other derivative instruments for each of the three years ended December 31:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009 (1)
Net investment income P&C operations (2)	$ 819,708	(7.4)%	$ 884,866	(10.4)%	$ 987,398
Net income (loss) from investment fund affiliates (3)	26,253	(48.6)%	51,102	(35.2)%	78,867
Net realized (losses) on investments (4)	(188,359)	30.4%	(270,803)	NM*	(921,437)
Net realized and unrealized (losses) on investment and other derivative instruments (5)	(10,738)	(68.3)%	(33,843)	0.6%	(33,647)

(1) Certain reclassifications have been made to conform to current year presentation.
(2) Net investment income relating to P&C operations includes the net investment income related to the net results from structured products.
(3) The Company generally records the income related to alternative fund affiliates on a one-month lag and the private investment fund affiliates on a three-month lag in order for the Company to meet the filing deadlines for its periodic reports.
(4)

Results up to and including March 31, 2009 include charges for OTTI related to the non-credit impairment of unrealized losses. From April 1, 2009, the non-credit impairment is excluded from realized losses.

(5) For a summary of realized and unrealized gains and losses on all derivative instruments, see Item 8, Note 14 to the Consolidated Financial Statements, Derivative Instruments.

* NM Not meaningful

Net investment income related to P&C operations decreased in the year ended December 31, 2011 by $65.2 million as compared to the same period of 2010 due to decreasing portfolio yields and cash outflows from the investment portfolio. Overall, portfolio yields have decreased due to declining interest rates across the Company s major jurisdictions. Net investment income related to P&C operations decreased in the year ended December 31, 2010 by $102.5 million as compared to the same period in 2009 due primarily to declining portfolio yields, as a result of the impact of declines in U.S. interest rates.

Net income from investment fund affiliates includes earnings from the Company s investments in closed-end investment funds and partnerships and similar vehicles that are accounted for under the equity method. Net income from investment fund affiliates decreased in the year ended December 31, 2011 compared to the same period of 2010. However, these results reflect weaker performance from the Company s alternative and private investment portfolios for 2011 given difficult market conditions. Performance in alternative and private funds in 2011 was challenged by volatile capital markets and the generally weaker returns to risk assets during 2011 as compared to the prior year. Net income from investment fund affiliates decreased in the year ended December 31, 2010 compared to the same period of 2009. These results reflect solid results from the Company s private investment portfolio for 2010, as compared to a loss during 2009, offset by earnings from alternative funds, which were lower than the results during 2009. Performance in alternative funds in 2009 was particularly strong.

Investment Performance

The Company manages its fixed income securities in accordance with investment authorities approved by the Risk and Finance Committee of the Board of Directors. The following is a summary of the investment portfolio returns for the years ended December 31, 2011 and 2010 of the fixed income portfolio and non-fixed income portfolios:

	2011 (1)	2010 (1)
P&C - Fixed income Portfolio		
USD fixed income portfolio	4.7%	6.6%
GBP fixed income portfolio	4.4%	5.7%
EUR fixed income portfolio	3.2%	5.1%
Life - Fixed income Portfolio		
USD fixed income portfolio	11.8%	11.1%
GBP fixed income portfolio	9.5%	9.5%
EUR fixed income portfolio	7.6%	8.4%
Other Portfolios		
Alternative portfolio (2)	3.4%	6.2%
Equity portfolio (3)	(6.4)%	NM*
High-Yield fixed income portfolio	1.5%	8.4%

(1) Portfolio returns are calculated by dividing the sum of the net investment income or net income from investment fund affiliates, realized gains (losses) and unrealized gains (losses) by the average market value of each portfolio. Performance is measured in either the underlying asset currency or the functional currency.

(2) Performance on the alternative portfolio reflects the year ended November 30, 2011 and 2010, respectively.

(3) Investment returns for the equity portfolio were negligible in 2010 and, accordingly, performance returns were not presented.

* NM Not meaningful

Net Realized Gains and Losses on Investments and Other-than-Temporary Declines in the Value of Investments

Net realized losses on investments for the year ended December 31, 2011 included net realized losses of approximately $160.2 million related to the write-down of certain of the Company s fixed income investments. In addition, included in the net realized losses noted above are net realized losses of $28.2 million due primarily to losses from sales of investments, principally, on European financials and non-Agency RMBS offset partially by gains from sales of Agency MBS and Government and Government Related and Supported securities.

The significant components of the net impairment charges of $160.2 million were:

For structured credit securities, the Company recorded net impairments of $78.7 million for the year ended December 31, 2011. The Company determined that the likely recovery on these securities was below the carrying value and, accordingly, recorded an impairment of the securities to the discounted value of the cash flows of these securities.

The Company recorded impairments totaling $31.0 million for the year ended December 31, 2011 related to medium term notes backed primarily by investment grade European investment grade credit. The Company adjusted the estimated remaining holding period of certain notes resulting in a shorter reinvestment spectrum.

For corporate securities, excluding medium term notes, the Company recorded net impairments totaling $6.5 million, principally on hybrid securities, for the year ended December 31, 2011.

The Company recorded impairments of $44.0 million related primarily to foreign exchange losses arising on U.S. dollar denominated securities held in a Swiss franc functional currency entity and foreign exchange losses on U.K. sterling denominated securities held in U.S. dollar portfolios. The foreign exchange losses are recorded as part of the foreign currency revaluation process; however, because the Company s consolidated reporting currency is U.S. dollars, the foreign exchange impairment recorded on these securities is fully offset by a cumulative foreign currency translation adjustment gain recorded upon the consolidation of the foreign currency entity.

Net realized losses in the year ended December 31, 2010 included net realized losses of $205.1 million related to the write-down of certain of the Company s fixed income, equity and other investments with respect to which the Company determined that there was an other-than-temporary decline in the value of those investments as well as $65.7 million from sales of investments.

Net Realized and Unrealized Gains and Losses on Derivatives

Net realized and unrealized losses on investment derivatives for the years ended December 31, 2011, 2010 and 2009 resulted from the Company s investment strategy to manage interest rate risk, foreign exchange risk and credit risk, and to replicate permitted investments. For a further discussion see Item 8, Note 2(h) to the Consolidated Financial Statements, Significant Accounting Policies Other-Than-Temporary Impairments (OTTI) of Available for Sale and Held to Maturity Securities, and Note 14, Derivative Instruments.

Other Revenues and Expenses

The following table sets forth other revenues and expenses of the Company for each of the three years ended December 31:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009
Net income (loss) from operating affiliates (1)	$ 76,786	(36.7)%	$ 121,372	NM*	$ 60,480
Exchange gains (losses)	40,640	NM*	10,161	NM*	(84,813)
Corporate operating expenses	(159,158)	75.2%	(90,686)	(15.9)%	(107,877)
Interest expense (2)	(154,084)	3.2%	(159,118)	(7.9)%	(172,764)
Impairment of goodwill	(429,020)	NM*		NM*	
Loss on settlement of guarantee		NM*	(23,500)	NM*	
Amortization of intangible assets	(1,438)	22.6%	(1,858)	1.2%	(1,836)
Income tax expense	(59,707)	(63.3)%	(162,737)	35.3%	(120,307)

(1) The Company generally records the income related to certain operating affiliates on a three-month lag in order for the Company to meet the filing deadlines for its periodic reports.

(2) Interest expense does not include interest expense related structured products as reported within the Insurance and Reinsurance segments.

* NM Not meaningful

The following table sets forth the net income (loss) from operating affiliates for each of the three years ended December 31:

(U.S. dollars in thousands)	2011	% Change 2011 vs 2010	2010	% Change 2010 vs 2009	2009
Net income (loss) from financial operating affiliates	$ (1,018)	NM*	$ 53,031	NM*	$ 3,629
Net income from investment manager affiliates	56,913	41.6%	40,180	127.0%	17,698
Net income from other strategic operating affiliates	20,891	25.8%	28,161	(28.1)%	39,153
Total	$ 76,786	(36.7)%	$ 121,372	100.7%	$ 60,480

* NM Not meaningful

The financial operating affiliate loss in the year ended December 31, 2011 reflects a write down in value of one investment following a restructuring. Financial operating affiliate income increased during the year ended December 31, 2010 as compared to the same period of 2009 due to the sale of a significant portion of the Company s shareholding in Primus Guaranty Ltd. For further information on the sale of Primus shares, see Item 8, Note 6 to the Consolidated Financial Statements, Investments in Affiliates.

Investment manager affiliate income increased substantially in the year ended December 31, 2011 as compared to the same period of 2010, reflecting the positive impact of the sale of the Company s ownership stake in Finisterre, and strong results from certain investment manager affiliates in the current year, compared to solid broad-based results in the same period of 2010. Investment manager affiliate income increased during the year ended December 31, 2010 as compared to the same period of 2009 primarily as a result of positive capital market conditions since the fourth quarter of 2009 compared to the challenging conditions for alternative asset managers reported in the fourth quarter of 2008 and first two quarters of 2009. Finally, the Company also benefited in 2010 from a $4.4 million gain associated with the sale of its stake in one of the investment manager affiliates.

Strategic operating affiliate income decreased in the year ended December 31, 2011 as compared to the same period of 2010 due to current year losses from an insurance affiliate catastrophe bond fund and from the Company s Brazilian joint venture ITAÚ XL Seguros Corporativos S.A. (ITAU), which was sold during the second quarter of 2010. Income from other strategic operating affiliates decreased during the year ended December 31, 2010 as compared to the same period of 2009 mainly due to lower earnings in 2010 relating to an insurance affiliate which largely writes direct U.S. homeowners insurance and lower earnings due to the sale of ITAU during the second quarter of 2010.

For the full year of 2011, foreign exchange gains were produced as a result of a stronger U.S. dollar against U.K. sterling, the Brazilian real and the Swiss franc, which more than offset losses that were driven by a stronger Australian dollar. In the year ended December 31, 2010, foreign exchange gains were marginal as a result of a limited overall movement in the value of the U.S. dollar during the period.

Foreign exchange gains in the year ended December 31, 2011 were produced as a result of a stronger U.S. dollar against U.K. sterling, the Euro, the Brazilian real and the Swiss franc, which more than offset losses that were driven by a stronger Australian dollar. Foreign exchange gains in the year ended December 31, 2010 were marginal as a result of a limited overall movement in the value of the U.S. dollar during the period. The U.S. dollar was stronger against the Euro, while weakening against the Swiss franc, Canadian dollar and Brazilian real. In the year ended December 31, 2009, the U.S. dollar weakened against all of the Company s major currency exposures, particularly the Canadian dollar and U.K. sterling, generating a loss for that period.

Corporate operating expenses increased by 75.2% in the year ended December 31, 2011 as compared to the same period in 2010 primarily as a result of certain strategic corporate initiatives taking place in 2011. Corporate operating expenses decreased by 15.9% during the year ended December 31, 2010 as compared to 2009 primarily as a result of the restructuring costs incurred during 2009.

Interest expense includes costs related to the Company s debt and collateral facilities as well as certain deposit liability accretion which is not included in Net investment results structured products. Interest expense decreased in the year ended December 31, 2011 as compared to the same period in 2010 as a result of the overall reduction in the Company s debt following the purchase and retirement of the $500 million 8.25% Senior Notes in August 2011 and the sale of $400 million 5.75% Senior Notes in September 2011. In June 2010, interest rate contracts designed as fair value hedges of certain issues of the Company s notes payable and debt were settled. Interest expense for the year ended December 31, 2010 as compared to the same period in 2009 decreased as a result of the Company s debt hedging activities where the effective portion of the hedging relationship is amortizing through interest expense over the remaining term of the debt.

Due in part to continued losses in certain businesses within the Insurance segment and continued low industry market valuations, which impacts certain assumptions used in the goodwill discounted cash flow valuation test such as the selected discount rate and related risk premium, the Company performed an interim impairment test for goodwill subsequent to its annual testing date of June 30. The interim impairment test resulted in a non-cash goodwill impairment charge of $429.0 million recorded representing a write-off of all goodwill associated with the Insurance segment. For further information, see Item 8, Note 6 to the Consolidated Financial Statements, Goodwill and Other Intangible Assets, and see further discussion under Critical Accounting Policies and Estimates.

Amortization of intangible assets was flat for the year ended December 31, 2011 as compared to the same period in 2010 and 2009.

The tax charge of $59.7 million recognized in the year ended December 31, 2011 included a benefit of $11.9 million arising as a result of a change in an overseas tax rule adopted in the quarter ended June 30, 2011. The Company has incurred a tax charge in 2011 notwithstanding reporting net losses due to the distribution of operating profits across the organization and the impact of internal reinsurance. In addition, net profits were recorded in certain jurisdictions due to the distribution of prior year development. A tax benefit of $11.5 million was recognized in the fourth quarter of 2011 in respect of the non-cash goodwill impairment charge of $429.0 million. The increase in the Company s income taxes in 2010 as compared to 2009 arose principally from the increase in the profitability of the Company s U.S. and European operations in 2010. See Critical Accounting Policies and Estimates and Item 8, Note 22 to the Consolidated Financial Statements, Taxation.

BALANCE SHEET ANALYSIS

Investments

At December 31, 2011 and 2010, total investments, cash and cash equivalents, accrued investment income and net receivable for investments sold were $35.9 billion and $35.8 billion, respectively. The following table summarizes the Company s total investment and cash and cash equivalents at December 31, 2011 and 2010:

(U.S. dollars in thousands)	Carrying Value December 31, 2011 (1)	Percent of Total	Carrying Value December 31, 2010 (1)	Percent of Total
Cash and cash equivalents	$ 3,825,125	10.7%	$ 3,022,868	8.4%
Net receivable/ (payable) for investments sold/ (purchased)	1,233	0.0%	(12,599)	0.0%
Accrued investment income	331,758	0.9%	350,091	1.0%
Short-term investments	359,063	1.0%	450,681	1.3%
Fixed maturities - AFS:				
U.S. Government and Government-Related/Supported (2)	1,990,983	5.5%	2,565,444	7.2%
Corporate Financials (3) (4)	3,392,291	9.5%	3,985,889	11.1%
Corporate Non-Financials (4)	7,070,224	19.7%	6,983,082	19.5%
Residential mortgage-backed securities Agency	5,379,406	15.0%	5,203,711	14.5%
Residential mortgage-backed securities Non-Agency	641,815	1.8%	1,021,823	2.9%
Commercial mortgage-backed securities	974,835	2.7%	1,172,507	3.3%
Collateralized debt obligations	658,602	1.8%	734,138	2.1%
Other asset-backed securities	986,356	2.8%	960,532	2.7%
U.S. States and political subdivisions of the States	1,797,378	5.0%	1,360,456	3.8%
Non-U.S. Sovereign Government, Supranational and Government-Related (2)	3,298,135	9.2%	3,154,523	8.8%
Total fixed maturities - AFS	$ 26,190,025	73.0%	$ 27,142,105	75.9%
Fixed maturities - HTM:				
U.S. Government and Government-Related/Supported (2)	10,399	0.0%	10,541	0.0%
Corporate Financials (3) (4)	313,179	0.9%	319,333	0.9%
Corporate Non-Financials (4)	985,087	2.7%	1,018,464	2.8%
Residential mortgage-backed securities Non-Agency	80,955	0.2%	82,763	0.2%
Other asset-backed securities	280,684	0.8%	287,109	0.8%
Non-U.S. Sovereign Government, Supranational and Government-Related (2)	998,674	2.8%	1,010,125	2.8%
Total fixed maturities - HTM	$ 2,668,978	7.4%	$ 2,728,335	7.5%
Equity securities (5)	468,197	1.3%	84,767	0.2%
Investments in affiliates	1,052,729	2.9%	1,127,181	3.1%
Other investments	985,262	2.8%	893,570	2.6%
Total investments and cash and cash equivalents	**$ 35,882,370**	**100.0%**	**$ 35,786,999**	**100%**

(1) Carrying values represents the fair value for available for sale fixed maturities and amortized cost for held to maturity securities.

(2) U.S. Government and Government-Related/Supported and Non U.S. Sovereign Government, Provincials, Supranational and Government-Related include government-related securities with an amortized cost of $1,878.3 million and fair value of $1,915.6 million and U.S. Agencies with an amortized cost of $494.0 million and fair value of $541.2 million.

(3) Included in Corporate - Financials are gross unrealized losses of $108.8 million on Tier One and upper Tier Two securities of financial institutions (Hybrids) with fair value of $386.1 million, as well as gross unrealized losses of $70.1 million on subordinated debt (including lower Tier Two securities) with a fair value of $701.3 million.

(4) Included within Corporate are certain floating rate medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes have a fair value of $266.0 million and an amortized cost of $297.7 million. These securities have been allocated ratings of the underlying pool of securities. These notes allow the investor to participate in cash flows of the underlying bonds including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(5) Included within equity securities are investments in fixed income funds of $91.6 million and nil at December 31, 2011 and 2010, respectively.

The Company reviews on a regular basis its corporate debt investments to consider its concentration, credit quality and compliance with established guidelines. At both December 31, 2011 and 2010, the average credit quality of the Company s total fixed income portfolio (including fixed maturities, short-term investments, cash and cash equivalents and net receivable/(payable) for investment sold/(purchased)) was Aa2/AA . Included in the table below are the credit ratings of the fixed income portfolio excluding operating cash at December 31, 2011 and 2010:

	December 31, 2011		December 31, 2010	
(U.S. dollars in thousands) **Investments by Credit Rating (1)(2)**	**Carrying Value**	**Percent of Total**	**Carrying Value**	**Percent of Total**
AAA	$ 16,276	51.1%	$ 16,944	52.0%
AA	5,266	16.6%	5,058	15.5%
A	7,098	22.3%	7,288	22.3%
BBB	2,418	7.6%	2,182	6.7%
BB and below	718	2.3%	1,142	3.5%
Not rated	39	0.1%	6	0.0%
Total	**$ 31,815**	**100.0%**	**$ 32,620**	**100%**

(1) Included in the above are $266.0 million or 0.8% of the portfolio that represents medium term notes rated at the average credit rating of the underlying asset pools backing the notes.

(2) The credit rating for each asset reflected above was principally determined based on the weighted average rating of the individual securities from Standard & Poor s, Moody s Investors Service and Fitch Ratings. U.S. agencies paper, whether with implicit or explicit government support, reflect the credit quality rating of the U.S. government for the purpose of these calculations.

Gross and Net Unrealized Gains and Losses on Investments

At December 31, 2011, the Company had net unrealized gains on available for sale fixed maturities and short-term investments of $418.0 million. Gross unrealized losses on these investments were $776.6 million. The information presented below for the gross unrealized losses on the Company s investments at December 31, 2011 shows the potential effect upon future earnings and financial position should management later conclude that some of the current declines in the fair value of these investments are other-than-temporary. Realized losses or impairments, depending on their magnitude, may have a material adverse effect on the Company s operations. The decrease in net unrealized losses on investments during the year ended December 31, 2011 was primarily due to losses realized during the year and marginally favorable market movements. See Item 7A, Quantitative and Qualitative Disclosures about Market Risk Credit Risk.

The following is the maturity profile of the available for sale fixed income securities that were in a gross unrealized loss position at December 31, 2011:

Type of Securities *(U.S. dollars in thousands)*	**Length of time in a continual unrealized loss position**	**Amount of unrealized loss at December 31, 2011**	**Fair Value of Securities in an unrealized loss position at December 31, 2011**
Fixed-Maturities and Short-Term Investments	Less than six months	$ (43,802)	$ 2,084,310
	At least 6 months but less than 12 months	(44,451)	290,865
	At least 12 months but less than 2 years	(41,690)	495,270
	2 years or more	(646,619)	2,287,639
	Total	$ (776,562)	$ 5,158,084

Equities	Less than six months	$ (39,445)	$ 352,371
	At least 6 months but less than 12 months	(990)	9,214
	Total	$ (40,435)	$ 361,585

The following is the maturity profile of the AFS fixed income securities that were in a gross unrealized loss position at December 31, 2011:

Maturity profile in years of fixed income securities in a gross unrealized loss position *(U.S. dollars in thousands)*	**Amount of unrealized loss at December 31, 2011**	**Fair value of securities in an unrealized loss position at December 31, 2011**
Less than 1 year remaining	$ (16,378)	$ 525,466
At least 1 year but less than 5 years remaining (1)	(108,617)	1,439,912
At least 5 years but less than 10 years remaining (1)	(91,136)	647,381
More than 10 years but less than 20 years remaining (1)	(60,551)	269,142
At least 20 years or more remaining (1)	(37,271)	281,486
Residential mortgage-backed securities Agency	(3,849)	347,278
Residential mortgage-backed securities Non-Agency	(229,409)	555,432
Commercial mortgage-backed securities	(9,553)	108,553
Collateralized debt obligations	(191,717)	639,719
Other asset-backed securities	(28,081)	343,715
Total	$ (776,562)	$ 5,158,084

(1) Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments senior to the common and preferred equities of the financial institutions, are allocated based on the call date and medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage are allocated on contractual maturity.

The following is the maturity profile of the HTM fixed income securities that were in a gross unrealized loss position at December 31, 2011:

Maturity profile in years of held to maturity securities in a gross unrealized loss position *(U.S. dollars in thousands)*	**Amount of unrealized loss at December 31, 2011**	**Fair value of securities in an unrealized loss position at December 31, 2011**
Less than 1 year remaining	$ (30)	$ 7,021
At least 1 year but less than 5 years remaining	(565)	29,631
At least 5 years but less than 10 years remaining	(5,292)	74,229
More than 10 years but less than 20 years remaining	(14,810)	204,613
Residential mortgage-backed securities Non-Agency	(32)	9,372
Other asset-backed securities	(6)	1,106
Total	$ (20,735)	$ 325,972

Factors considered in determining that additional OTTI charges were not warranted include management s consideration of current and near term liquidity needs along with other available sources, and in certain instances an evaluation of the factors and time necessary for recovery. For further information, see Item 8, Note 5, Investments, to the Consolidated Financial Statements.

As noted in Item 8, Note 2, to the Consolidated Financial Statements Significant Accounting Policies, the determination of the amount of OTTI varies by investment type and is based upon management s periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available. Management considers a wide range of factors about the securities and uses its best judgment in evaluating the cause of the decline in the

estimated fair value of the security and in assessing the prospects for near-term recovery. Inherent in management s evaluation of the security are assumptions and estimates about the operations of the issuer and its future earnings potential. Management updates its evaluations regularly and reflects additional impairments in net income as determinations are made. Management s determination of the amount of the impairment taken on investments is highly subjective and could adversely impact the Company s results of operations. There can be no assurance that management has accurately assessed the level of OTTI taken and reflected in the Company s financial statements. Furthermore, additional impairments may need to be taken in the future. Historical trends may not be indicative of future impairments.

Levels of write down or OTTI are also impacted by the Company s assessment of the intent to sell securities that have declined in value prior to recovery. If, due to changes in circumstances, the Company determines to reposition or realign portions of the portfolio and the Company determines not to hold certain securities in an unrealized loss position to recovery, then the Company will incur OTTI charges, which could be significant.

Gross Unrealized Gains and Losses

Management, in its assessment of whether securities in a gross unrealized loss position are temporarily impaired, considers the significance of the impairments. The Company had structured credit securities with gross unrealized losses of $84.4 million, with a fair value of $39.6 million, which at December 31, 2011 had cumulative fair value declines of greater than 50% of amortized costs. All of these are mortgage and asset-backed securities. The Company has evaluated each of these securities in conjunction with its investment manager service providers and believes it is more likely than not that the issuer will be able to fund sufficient principal and interest payments to support the current amortized cost. These securities include gross unrealized losses of $61.2 million on non-Agency RMBS, $22.6 million on Core CDOs and $0.7 million on CMBS holdings.

Net Unrealized Gains and Losses Corporate Financial Sector Securities

At December 31, 2011, approximately $1.2 billion of the Company s $3.7 billion in corporate financial sector securities was held in the portfolios supporting the Company s Life operations portfolio representing 91.1% of the net unrealized losses on this asset class. The assets associated with that business are more heavily weighted towards longer term securities from financial institutions, including a significant portion of the Company s Tier 1 and Upper Tier 2 securities, representing committed term debt and hybrid instruments senior to the common and preferred equity of the financial institutions. Financials held in Life portfolios accounted for $115.8 million of the Company s net unrealized loss at December 31, 2011. At December 31, 2011, approximately 43% of the overall sensitivity to interest rate risk and 35% to credit risk was related to the Life operations portfolio, despite these portfolios accounting for only 21% of the fixed income portfolio.

Net Unrealized Gains and Losses Structured Securities

The following table details the current exposures to structured credit portfolio s excluding Agency MBS within the Company s fixed income portfolio as well as the current net unrealized (loss) gain position at December 31, 2011 and 2010:

(U.S. dollars in millions)	December 31, 2011			December 31, 2010		
	Holding at Carrying Value	Percent of Fixed Income Portfolio	Net Unrealized (Loss) Gain	Holding at Carrying Value	Percent of Fixed Income Portfolio	Net Unrealized (Loss) Gain
Non-Agency RMBS:						
Sub-prime first lien mortgages	$ 295.5	1.0%	$ (137.0)	$ 395.1	1.2%	$ (142.4)
Alt-A mortgages	114.5	0.4%	(39.7)	198.0	0.6%	(53.7)
Second lien mortgages (including sub-prime second lien mortgages)	26.5	0.1%	(6.1)	33.1	0.1%	(7.8)
Prime RMBS	158.3	0.5%	(26.3)	311.6	0.9%	(28.2)
Other assets	128.0	0.4%	5.8	169.7	0.5%	(3.3)
Total exposure to Non-Agency RMBS	722.8	2.4%	(203.3)	1,107.5	3.3%	(235.4)
Commercial Mortgage Backed Securities	974.8	3.3%	47.2	1,172.5	3.5%	37.4
Core CDOs (1)	662.9	2.3%	(185.6)	733.5	2.2%	(186.6)
Other Structured	1,266.8	4.3%	11.8	1,245.4	3.7%	(19.0)
Total Non-Agency Structured Securities	$ 3,627.3	12.3%	$ (329.9)	$ 4,258.9	12.7%	$ (403.6)

(1) The Company defines Core CDOs as investments in non-subprime collateralized debt obligations, which primarily consisted of collateralized loan obligations.

At December 31, 2011, the Company s sub-prime and Alt-A exposures had adequate underlying loan characteristics and the Company believed at such date that the current amortized cost levels were at or below the discounted cash flow value of the holdings, based on an analysis of subordination levels relative to current expectations of house price declines, loss severities and default levels. The Company had approximately $340.9 million of Non-Agency RMBS downgraded during the year ended December 31, 2011. However, 55.2% of the Company s holdings remain rated investment grade at December 31, 2011.

Refer to Significant Items Affecting the Results of Operations for further discussion surrounding the impact of credit market movements on the Company s investment portfolio.

European Sovereign Debt Crisis

The ongoing global financial crisis has led to the deterioration of economies globally, as sovereign governments have reacted to the crisis by further increasing public expenditures in order to provide stimulus and security, which has created significant budgetary shortfalls. Several key nations within the European Union particularly the GIIPS countries have suffered a high level of fiscal distress and economic vulnerability due to overreliance on external credit sources and imprudent borrowing and other monetary practices. This has raised doubts within the global financial community as to whether these sovereign nations will remain able to service their own debt obligations both at a national and local level.

The Company s primary exposure to this European sovereign debt crisis is from direct investment in fixed maturity securities issued by GIIPS national and local governments, as well as from fixed maturity securities issued by certain financial and non-financial corporate entities operating within GIIPS. The Company continues to monitor its financial exposure to this crisis, and continually assesses the impact of a potential default by any of GIIPS on their respective debt issuances, including the associated impact on non-sovereign entities in these nations in the event of such a default. With regard to non-sovereign securities, the Company considers a security to be at risk if the security issuer s main operations are physically located within GIIPS, as opposed to where the issuer is legally domiciled.

The Company currently has no unfunded investment exposures or commitments to either sovereign or non-sovereign entities within these EU nations. The Company does invest in various alternative and private investment funds that from time to time may invest in securities or investments related to these five EU nations. Currently these are not material exposures.

The following is an analysis of the Company s AFS and HTM fixed maturity investment exposures related to this GIIPS crisis at December 31, 2011 and the contractual maturities of these securities. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(U.S. dollars in thousands)	December 31, 2011 Amortized Cost	Fair Value
Fixed maturities GIIPS - AFS		
Sovereign investments National Governments	$ 6,601	$ 5,927
Non-Sovereign investments Financial Institutions	23,396	20,847
Non-Sovereign investments Non-Financial Institutions	138,834	131,890
Total fixed maturities GIIPS - AFS	$ 168,831	$ 158,664
Due less than one year	$ 13,824	$ 14,028
Due after 1 through 5 years	32,069	30,395
Due after 5 through 10 years	72,988	70,651
Due after 10 years	49,950	43,590
	$ 168,831	$ 158,664
Fixed maturities GIIPS HTM		
Sovereign investments National Governments	$ 11,738	$ 8,739
Sovereign investments Local Governments	9,360	7,649
Non-Sovereign investments Non-Financial Institutions	72,782	65,380
Total fixed maturities GIIPS - HTM	$ 93,880	$ 81,768
Due less than one year	$ 6,264	$ 6,233
Due after 1 through 5 years	4,199	4,110
Due after 5 through 10 years	20,705	18,260
Due after 10 years	62,712	53,165
	$ 93,880	$ 81,768

The following table details the gross and net unrealized (loss) gain position at December 31, 2011 relating to GIIPS:

(U.S. dollars in thousands)	December 31, 2011 Greece	Italy	Ireland	Portugal	Spain	TOTAL
Gross Unrealized (Losses) - GIIPS						
Sovereign investments National Governments	$	$ (698)	$	$	$	$ (698)
Non-Sovereign investments Financial Institutions			(2,762)		(1,317)	(4,079)
Non-Sovereign investments Non-Financial Institutions	(38)	(5,527)		(111)	(3,592)	(9,268)
Total gross unrealized gains (losses) relating to GIIPS	$ (38)	$ (6,225)	$ (2,762)	$ (111)	$ (4,909)	$ (14,045)
Net Unrealized Gains (Losses) - GIIPS						

Sovereign investments	National Governments	$	$ (698)	$	$	$ 24	$ (674)
Non-Sovereign investments	Financial Institutions			(1,233)		(1,317)	(2,550)
Non-Sovereign investments	Non-Financial Institutions	332	(4,181)		(111)	(2,984)	(6,944)
Total net unrealized gains (losses) relating to GIIPS		$ 332	$ (4,879)	$ (1,233)	$ (111)	$ (4,277)	$ (10,168)

In addition to the direct investment portfolio considerations discussed above, as an international (re)insurance company, European credit exposures may exist for the Company within unpaid losses and loss expenses recoverable and reinsurance balances receivable. For further details on these balances including the names of the Company s most significant reinsurance counterparties see Item 8, Note 9 to the Consolidated Financial Statements, Reinsurance . Other sources of potential exposure to European credit issues may exist within certain lines of insurance or reinsurance business written (including but not limited to lines such as surety, business interruption, and political risk), or within underlying investments held in securitized financial instruments or in structured transactions in which the Company has an interest. Management considers these potential exposures as part of its ongoing enterprise risk management processes.

Fair Value Measurements of Assets and Liabilities

As described in Note 3 to the Consolidated Financial Statements, Fair Value Measurements, effective January 1, 2008, the Company adopted the authoritative guidance on fair value measurements and accordingly has provided required disclosures by level within the fair value hierarchy of the Company s assets and liabilities that are carried at fair value. As defined in the hierarchy, those assets and liabilities categorized as Level 3 have valuations determined using unobservable inputs. Unobservable inputs may include the entity s own assumptions about market participant assumptions, applied to a modeled valuation however, this is not the case with respect to the Company s Level 3 assets and liabilities. The vast majority of the assets and liabilities classified as Level 3 are made up of those securities for which the values were obtained from brokers where either significant inputs were utilized in determining the value that were difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilized by the broker were not obtained to support a Level 2 classification or the Company utilized internal valuation models.

During the years ended December 31, 2011 and 2010, certain collateralized debt obligations (CDOs) that were previously classified as Level 2 due to sufficient market data being available to allow a price to be determined and provided by third party pricing vendors, were transferred to Level 3 because third party vendor prices were no longer believed to be the most appropriate pricing source. Broker quotes, for which sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification, are the primary source of the valuations for these CDO securities.

Controls over Valuation of Financial Instruments

The Company performs quarterly reviews of the prices received from its third party valuation sources to assess if the prices represent a reasonable estimate of the fair value. This process is completed by investment and accounting personnel who are independent of those responsible for obtaining the valuations. The approaches taken by the Company include, but are not limited to, annual reviews of the controls of the external parties responsible for sourcing valuations which are subjected to automated tolerance checks, quarterly reviews of the valuation sources and dates, and monthly reconciliations between the valuations provided by our external parties and valuations provided by our third party investment managers at a portfolio level.

In addition, the Company relies on valuation controls performed by external parties responsible for sourcing appropriate valuations from third parties on the Company s behalf. The approaches taken by these external parties to gain comfort include, but are not limited to, comparing valuations between external sources, completing recurring reviews of third party pricing services methodologies and reviewing controls of the third party service providers to support the completeness and accuracy of the prices received.

Valuation Methodology of Level 3 Assets and Liabilities

Refer to Item 8, Notes 2 and 3 of the Consolidated Financial Statements, Significant Accounting Policies and Fair Value Measurements for a description of the valuation methodology utilized to value Level 3 assets and liabilities, how the valuation methodology is validated as well as further details associated with various assets classified as Level 3. At December 31, 2011, the Company did not have any liabilities that were carried at fair value based on Level 3 inputs other than derivative instruments in a liability position at December 31, 2011.

Fair Value of Level 3 Assets and Liabilities

At December 31, 2011, the fair value of Level 3 assets and liabilities as a percentage of the Company s total assets and liabilities that are carried at fair value was as follows:

(U.S. dollars in thousands)	**Total Assets and Liabilities Carried at Fair Value at December 31, 2011**	**Fair Value of Level 3 Assets and Liabilities**	**Level 3 Assets and Liabilities as a Percentage of Total Assets and Liabilities Carried at Fair Value, by class**
Assets			
Fixed maturities, at fair value			
U.S. Government and Government agency-Related/Supported	$ 1,990,983	$	%
Corporate	10,462,515	23,818	0.2%
Residential mortgage-backed securities Agency	5,379,406	32,041	0.6%
Residential mortgage-backed securities Non-Agency	641,815		%
Commercial mortgage-backed securities	974,835		%
Collateralized debt obligations	658,602	650,851	98.8%
Other asset-backed securities	986,356	16,552	1.7%
U.S. States and political subdivisions of the States	1,797,378		%
Non-U.S. Sovereign Government, Supranational and Government-Related	3,298,135		%
Total Fixed maturities, at fair value	26,190,025	$ 723,262	2.8%
Equity securities, at fair value	468,197		%
Short-term investments, at fair value	359,063		%
Total investments available for sale	$ 27,017,285	$ 723,262	2.7%
Cash equivalents (1)	2,754,365	%	
Other investments (2)	661,557	113,959	17.2%
Other assets (3)	65,734		%
Total assets carried at fair value	$ 30,498,941	$ 837,221	2.7%

Liabilities			
Financial instruments sold, but not yet purchased (4)	$ 20,844	$	%
Other liabilities (5)	58,706	42,644	72.6%
Total liabilities carried at fair value	$ 79,550	$ 42,644	53.6%

(1) Cash equivalents balances subject to fair value measurements include certificates of deposit and money market funds.

(2) The Other investments balance excludes certain structured transactions including certain investments in project finance transactions and a payment obligation (as described in Note 7, Other Investments), that has provided liquidity financing to a structured credit vehicle as a part of a third party medium term note facility. These Other investments are carried at amortized cost that totaled $323.7 million at December 31, 2011 and $327.7 million at December 31, 2010.
(3) Other assets include derivative instruments, reported on a gross basis.
(4) Financial instruments sold, but not yet purchased are included within Net payable for investments purchased on the balance sheet.
(5) Other liabilities include derivative instruments, reported on a gross basis.

At December 31, 2011, the Company s Level 3 assets represented approximately 2.7% of assets that are measured at fair value and less than 2% of total assets. The Company s Level 3 liabilities represented approximately 53.6% of liabilities that are measured at fair value and less than 1% of total liabilities at December 31, 2011.

Changes in the Fair Value of Level 3 Assets and Liabilities

See Item 8, Note 3 to the Consolidated Financial Statements, Fair Value Measurements, for an analysis of the change in fair value of Level 3 Assets and Liabilities.

Unpaid Losses and Loss Expenses

The Company establishes reserves to provide for estimated claims, the general expenses of administering the claims adjustment process and losses incurred but not reported. These reserves are calculated using actuarial and other reserving techniques to project the estimated ultimate net liability for losses and loss expenses. The Company s reserving practices and the establishment of any particular reserve reflects management s judgment concerning sound financial practice and do not represent any admission of liability with respect to any claims made against the Company.

Unpaid losses and loss expenses totaled $20.6 billion and $20.5 billion at December 31, 2011 and 2010, respectively. The table below represents a reconciliation of the Company s P&C unpaid losses and loss expenses for the year ended December 31, 2011:

(U.S. dollars in thousands)	Gross unpaid losses and loss expenses	Unpaid losses and loss expenses recoverable	Net unpaid losses and loss expenses
Balance at December 31, 2010	$ 20,531,607	$ (3,649,290)	$ 16,882,317
Losses and loss expenses incurred	5,172,367	(1,093,976)	4,078,391
Losses and loss expenses paid/recovered	(4,911,737)	1,065,535	(3,846,202)
Foreign exchange and other	(178,336)	47,803	(130,533)
Balance at December 31, 2011	$ 20,613,901	$ (3,629,928)	$ 16,983,973

While the Company reviews the adequacy of established reserves for unpaid losses and loss expenses regularly, no assurance can be given that actual claims made and payments related thereto will not be in excess of the amounts reserved. In the future, if such reserves develop adversely, such deficiency would have a negative impact on future results of operations. See Unpaid Losses and Loss Expenses and Critical Accounting Policies and Estimates above and Item 8, Note 10 to the Consolidated Financial Statements, Losses and Loss Expenses, for further discussion.

Unpaid Losses and Loss Expenses Recoverable and Reinsurance Balances Receivable

In the normal course of business, the Company seeks to reduce the potential amount of loss arising from claims events by reinsuring certain levels of risk assumed in various areas of exposure with other insurers or reinsurers. While reinsurance agreements are designed to limit the Company s losses from large exposures and permit recovery of a portion of direct unpaid losses, reinsurance does not relieve the Company of its ultimate liability to the Company s insureds. Accordingly, the losses and loss expense reserves on the balance sheet represent the Company s total unpaid gross losses. Unpaid losses and loss expense recoverable relates to estimated reinsurance recoveries on the unpaid loss and loss expense reserves.

92

The table below presents the Company s net paid and unpaid losses and loss expenses recoverable and reinsurance balances receivable at December 31, 2011 and 2010:

(U.S. dollars in thousands)	2011	2010
Reinsurance balances receivable	$ 263,877	$ 225,129
Reinsurance recoverable on future policy benefits	25,020	22,597
Reinsurance recoverable on unpaid losses and loss expenses	3,685,260	3,717,405
Bad debt reserve on unpaid losses and loss expenses recoverable and reinsurance balances receivable	(99,192)	(121,917)
Net paid and unpaid losses and loss expenses recoverable and reinsurance balances receivable	$ 3,874,965	$ 3,843,214

The Company has credit risk should any of its reinsurers be unable or unwilling to settle amounts due. Of the $3.9 billion total unpaid losses and loss expenses recoverable and reinsurance balances receivable at December 31, 2011, one individual reinsurer accounted for greater than 15% of the total. The Company is the beneficiary of letters of credit, trust accounts and funds withheld in the aggregate amount of $1.7 billion at December 31, 2011, collateralizing reinsurance recoverables with respect to certain reinsurers. The provision for uncollectible reinsurance is required principally due to the failure of reinsurers to indemnify the Company primarily because of disputes under reinsurance contracts and insolvencies. As at December 31, 2011 and 2010, the Company had a reserve for potential non-recoveries from reinsurers of $99.2 million and $121.9 million, respectively.

Approximately 92.2% of the total net unpaid loss and loss expense recoverable and reinsurance balances receivable (net of collateral held) outstanding at December 31, 2011, were due from reinsurers with a financial strength rating of A or better. The following is an analysis of the total recoverable and reinsurance balances receivable at December 31, 2011, by reinsurers owing more than 3% of such total:

Name of reinsurer	Reinsurer Financial Strength Rating	% of total
Munich Reinsurance Company	AA-/Stable	22.8%
Swiss Reinsurance Company	AA-/Stable	12.2%
Swiss Re Europe S.A.	AA-/Stable	5.1%
Transatlantic Reinsurance Company	A+/Stable	3.7%
Everest Reinsurance Company	A+/Stable	3.0%

The following table sets forth the ratings profile of the reinsurers that support the unpaid loss and loss expense recoverable and reinsurance balances receivable:

Reinsurer Financial Strength Rating	% of total
AAA	1.3%
AA	58.4%
A	32.3%
BBB	0.4%
BB and below	0.1%
Captives	4.8%
Not Rated	0.2%
Other	2.5%
Total	100.0%

Liquidity and Capital Resources

Liquidity is a measure of the Company s ability to generate sufficient cash flows to meet the short-and long-term cash requirements of the Company s business operations. As a global insurance and reinsurance company, one of the Company s principal responsibilities to its clients is to ensure that the Company has ready access to funds with which to settle large unforeseen claims. The Company would generally expect that positive cash flow from operations (underwriting activities and investment income) will be sufficient to cover cash outflows under most future loss scenarios. However, there is a possibility that unforeseen demands could be placed on the Company due to extraordinary events and as such the Company s liquidity needs may change. Such events include, among other things, several significant catastrophes occurring in a relatively short period of time resulting in material incurred losses; rating agency downgrades of the Company s core insurance and reinsurance subsidiaries that would require posting of collateral in connection with the Company s letter of credit and revolving credit facilities, return of unearned premium and/or the settlement of derivative transactions and large scale uncollectible reinsurance recoverables on paid losses (as a result of coverage disputes, reinsurers credit problems or decreases in the value of collateral supporting reinsurance recoverables), etc. Any one or a combination of such events may cause a liquidity strain for the Company. In addition, a liquidity strain could also occur in an illiquid market, such as that which was experienced in 2008. Investments that may be used to meet liquidity needs in the event of a liquidity strain may not be liquid, given inactive markets, or may have to be sold at a significant loss as a result of depressed prices. Because each subsidiary focuses on a more limited number of specific product lines than is collectively available from the consolidated group of companies, the mix of business tends to be less diverse at the subsidiary level. As a result, the probability of a liquidity strain, as described above, may be greater for individual subsidiaries than when liquidity is assessed on a consolidated basis. If such a liquidity strain were to occur in a subsidiary, XL-Ireland may be required to contribute capital to the particular subsidiary and/or curtail dividends from the subsidiary to support holding company operations which may be difficult given that XL-Ireland is a holding company and has limited liquidity.

A downgrade below A of the Company s principal insurance and reinsurance subsidiaries by either S&P or A.M. Best, which is two notches below the current S&P financial strength rating of A (Stable) and the A.M. Best financial strength rating of A (Stable) of these subsidiaries, may trigger cancelation provisions in a significant amount of the Company s assumed reinsurance agreements and may potentially require the Company to return unearned premiums to cedants. In addition, due to collateral posting requirements under the Company s letter of credit and revolving credit facilities, such a downgrade may require the posting of cash collateral in support of certain in use portions of these facilities. Specifically, a downgrade below A by A.M. Best would constitute an event of default under the Company s three largest credit facilities and may trigger such collateral requirements. In certain limited instances, such downgrades may require the Company to return cash or assets to counterparties or to settle derivative and/or other transactions with the respective counterparties. See Item 1A, Risk Factors A downgrade or potential downgrade in our financial strength and credit ratings by one or more rating agencies could materially and negatively impact our business, financial condition, results of operations and/or liquidity.

Holding Company Liquidity

As holding companies, XL-Ireland and XL-Cayman have no operations of their own and their assets consist primarily of investments in subsidiaries. Accordingly, XL-Ireland s and XL-Cayman s future cash flows largely depend on the availability of dividends or other statutorily permissible payments from subsidiaries. The ability to pay such dividends is limited by the applicable laws and regulations of the various countries and states in which these subsidiaries operate, including, among others, the Cayman Islands, Bermuda, the U.S., New York, Ireland, Switzerland and the U.K. See Item 8, Note 23 to the Consolidated Financial Statements, Statutory Financial Data, for further discussion and details regarding dividend capacity of the Company s major operating subsidiaries. See Risk Factors Our holding company structure and certain regulatory and other constraints affect our ability to pay dividends, make payments on our debt securities and make other payments. The ability to pay such dividends is also limited by the regulations of the Society of Lloyd s and certain contractual provisions. No assurance can be given that the Company s subsidiaries will pay dividends in the future to XL-Ireland or XL-Cayman.

Under Irish law, share premium was required to be converted to distributable reserves for the Company to have the ability to pay cash dividends and redeem and buyback shares following the Redomestication. On July 23, 2010, the Irish High Court approved XL-Ireland s conversion of share premium to $5.0 billion of distributable reserves, subject to the completion of certain formalities under Irish Company law. These formalities were completed in early August 2010. As of December 31, 2011 and 2010 XL-Ireland had $4.1 billion and $4.8 billion, respectively, in distributable reserves.

During 2009, management changed the internal ownership structure of certain of the Company s operating subsidiaries in Bermuda and Ireland in order to more efficiently utilize capital and to improve overall liquidity. In connection with these changes, certain dividends were paid to XL-Cayman by operating subsidiaries. At December 31, 2011, XL-Ireland and XL-Cayman held cash and investments, net of liabilities associated with cash sweeping arrangements, of $1.6 million and $2.0 billion, respectively, compared to $2.8 million and $1.7 billion, respectively, at December 31, 2010.

XL-Ireland s principal uses of liquidity are ordinary share related transactions including dividend payments to holders of its ordinary shareholders as well as share buybacks, capital investments in its subsidiaries and certain corporate operating expenses.

XL-Cayman s principal uses of liquidity are preference share related transactions including dividend payments to its preference shareholders as well as preference share buybacks from time to time, interest and principal payments on debt and certain corporate operating expenses.

All outstanding debt of the Company at December 31, 2011 and 2010 was issued by XL-Cayman except for the $600 million XLCFE Notes which were issued by XLCFE and were repaid at maturity on January 15, 2012. Both XL-Cayman and XLCFE are wholly-owned subsidiaries of XL-Ireland. Certain of XL-Cayman s outstanding debt is fully and unconditionally guaranteed by XL-Ireland. The Company s ability to obtain funds from its subsidiaries to satisfy any of its obligations under guarantees is subject to certain contractual restrictions, applicable laws and statutory requirements of the various countries in which the Company operates, including, among others, Bermuda, the United States, Ireland, Switzerland and the U.K. At December 31, 2011 and 2010, required statutory capital and surplus for the principal operating subsidiaries of the Company was $6.7 billion and $6.5 billion, respectively.

XL-Ireland and its subsidiaries provide no guarantees or other commitments (express or implied) of financial support to the Company s subsidiaries or affiliates, except for such guarantees or commitments that are in writing.

See Consolidated Statements of Cash Flows in Item 8, Financial Statements and Supplementary Data.

Sources of Liquidity for the Company

At December 31, 2011, the consolidated Company had cash and cash equivalents of approximately $3.8 billion as compared to approximately $3.0 billion at December 31, 2010. There are three main sources of cash flows for the Company those provided by operations, investing activities and financing activities.

Operating Cash Flows

Historically, cash receipts from operations, consisting of premiums and investment income, generally have provided sufficient funds to pay losses as well as operating expenses of the Company s subsidiaries and to fund dividends to XL-Ireland. However, as a result of the combination of current soft market conditions, the decision to put the Life operations segment and certain P&C lines into run-off and lower investment yields, operating cash flows are lower in 2011 than in the prior year. Cash receipts from operations are generally derived from the receipt of investment income on the Company s investment portfolio as well as the net receipt of premiums less claims and expenses related to the Company s underwriting activities in its P&C operations as well as its Life operations segment. The Company s operating subsidiaries provide liquidity in that premiums are generally received months or even years before losses are paid under the policies related to such premiums. Premiums and acquisition expenses are settled based on terms of trade as stipulated by an underwriting contract, and generally are received within the first year of inception of a policy when the premium is written, but can be up to three years on certain reinsurance business assumed. Operating expenses are generally paid within a year of being incurred. Claims, especially for casualty business, may take a much longer time before they are reported and ultimately settled, requiring the establishment of reserves for unpaid losses and loss expenses. Therefore, the amount of claims paid in any one year is not necessarily related to the amount of net losses incurred, as reported in the consolidated statement of income.

During the year ended December 31, 2011, net cash flows provided by operating activities were $327.2 million compared to net cash flows provided by operating activities of $594.8 million for the same period in 2010. This reduction was primarily due to P&C net loss and loss expenses paid of $3.8 billion in the year ended December 31, 2011, compared with $3.5 billion for the same period in 2010. This increase was due primarily to higher loss payments in the insurance segment in 2011 relating to the prior and current year catastrophes and other individual large property and excess casualty loss payments.

During the year ended December 31, 2010, net cash flows provided by operating activities were $594.8 million compared to net cash flows used of $42.8 million for the same period in 2009. The cash flows provided in 2010 resulted primarily from lower levels of cash payments for claims from previous underwriting years being offset by cash received as premium. In 2009, the cash flows used in operating activities were primarily as a result of cash payments for claims associated with Hurricanes Ike and Gustav losses.

Investing Cash Flows

Generally, positive cash flow from operations and financing activities is invested in the Company s investment portfolio, including affiliates or acquisition of subsidiaries.

Net cash provided by investing activities was $832.1 million in the year ended December 31, 2011 compared to net cash provided of $261.5 million for the same period in 2010. The 2011 cash inflow was mainly associated with the normal purchase and sale of portfolio investments.

Net cash provided by investing activities was $261.5 million in 2010 compared to net cash provided of $214.6 million for 2009. The 2010 cash inflow was mainly associated with normal purchase and sale of portfolio investments.

Certain of the Company s invested assets are held in trust and pledged in support of insurance and reinsurance liabilities. Such pledges are largely required by the Company s operating subsidiaries that are non-admitted under U.S. state insurance regulations, in order for the U.S. cedant to receive statutory credit for reinsurance. Also, certain deposit liabilities and annuity contracts require the use of pledged assets. As further outlined in Item 8, Note 17(f) to the Consolidated Financial Statements, Commitments and Contingencies Letters of Credit, certain assets of the investment portfolio are collateralized for the Company s letter of credit facilities. At December 31, 2011 and 2010, the Company had $17.2 billion and $16.1 billion in pledged assets, respectively.

Financing Cash Flows

Cash flows related to financing activities include ordinary and preferred share related transactions, the payment of dividends, the issue or repayment of debt and deposit liability transactions.

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

During the third quarter of 2007, the Company s Board of Directors approved a share buyback program, authorizing the Company to purchase up to $500.0 million of its ordinary shares. During 2010, the Company purchased and canceled 18.8 million ordinary shares for $375.4 million under this program which was the full amount that had been remaining at January 1, 2010 under this program.

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

On October 15, 2011, XL-Cayman issued 350,000 non-cumulative Series D Preference Ordinary Shares for $350 million of cash and liquid investments that were held in a trust account that was part of the Stoneheath facility. Holders of the Stoneheath Securities received one Series D Preference Ordinary Share in exchange for each Stoneheath Security. See Contingent Capital below.

During the year ended December 31, 2011, net cash flows used in financing activities were $358.7 million compared to net cash outflows of $1.5 billion for the same period in 2010. The 2011 net cash outflows related primarily to the buybacks of the Company s ordinary shares, as outlined above, the repurchase of all outstanding Redeemable Series C preference ordinary shares, the payment of ordinary and preferred share dividends and the repayment of deposit liabilities, partially offset by the proceeds of issuance of the 5.75% Senior Notes and the proceeds of issuance of the Series D Preference Ordinary Shares, as described above.

Net cash used in financing activities was $1.5 billion in 2010 compared to net cash used of $1.0 billion in 2009. The 2010 net cash outflows related primarily to the redemption of Redeemable Series C preference ordinary shares, purchase of the Company s ordinary shares as outlined above, settlement of $450 million of outstanding funding agreement liabilities, repayment of other deposit liabilities and the payment of ordinary and preferred dividends. For more information on the repurchase of debt, see Item 1, Note 18 to the Consolidated Financial Statements, Share Capital.

During the year ended December 31, 2009, net cash outflows related primarily to the repayment of debt and deposit liabilities and the payment of common and preferred dividends. Following the settlement of the purchase contracts associated with the 7.0% equity security units in February 2009, the Company issued 11,461,080 ordinary shares for net proceeds of approximately $743.1 million, which was used to retire the senior notes previously due February 2011, which had a fixed coupon of 5.25%.

On March 26, 2009, the Company completed a cash tender offer for a portion of its outstanding Redeemable Series C preference ordinary shares that resulted in approximately 12.7 million Redeemable Series C preference ordinary shares with a liquidation value of $317.3

million being purchased by the Company for approximately $104.7 million plus accrued and unpaid dividends, combined with professional fees totaling $0.8 million.

The Company is a Well Known Seasoned Issuer (WKSI) as defined by the rules and regulations of the SEC. The Company maintains a shelf registration statement on Form S-3 and is eligible to file automatically effective registration statements in the future for the potential offering and sale of an unlimited amount of debt and equity securities. The registration statement allows for various types of securities to be offered, including the following (i) ordinary shares, preference shares, debt securities, ordinary share warrants, ordinary share purchase contracts and ordinary share purchase units of XL-Ireland, (ii) guarantees by XL-Ireland of XL-Cayman debt securities and (iii) debt securities of XL-Cayman.

In addition the Company maintains letter of credit facilities which provide liquidity. Details of these facilities are described below in Capital Resources.

Capital Resources

At December 31, 2011 and 2010, the Company had total shareholders equity of $10.8 billion and $10.6 billion, respectively. In addition to ordinary share capital, the Company depends on external sources of financing to support its underwriting activities in the form of:

a. debt;

b. preference shares;

c. letter of credit facilities and other sources of collateral; and

d. revolving credit facilities.

In particular, the Company requires, among other things:

sufficient capital to maintain its financial strength and credit ratings, as issued by several ratings agencies, at levels considered necessary by management to enable the Company s key operating subsidiaries to compete;

sufficient capital to enable its regulated subsidiaries to meet the regulatory capital levels required in the United States, the U.K., Bermuda, Ireland, Switzerland and other key markets;

letters of credit and other forms of collateral that are required to be posted or deposited, as the case may be, by the Company s operating subsidiaries that are non-admitted under U.S. state insurance regulations in order for the U.S. cedant to receive statutory credit for reinsurance. The Company also uses letters of credit to support its operations at Lloyd s; and

revolving credit to meet short-term liquidity needs.

The following risks are associated with the Company s requirement to renew its credit facilities:

the credit available from banks may be reduced, resulting in the Company s need to pledge its investment portfolio to customers. This could result in a lower investment yield;

the Company may be downgraded by one or more rating agencies, which could materially and negatively impact the Company s business, financial condition, results of operations and/or liquidity; and

the volume of business that the Company s subsidiaries that are not admitted in the United States are able to transact could be reduced if the Company is unable to renew its letter of credit facilities at an appropriate amount.

Continued consolidation within the banking industry may result in the aggregate amount of credit provided to the Company being reduced. The Company attempts to mitigate this risk by identifying and/or selecting additional banks that can participate in the credit facilities upon renewal. See Item 1A, Risk Factors.

The following table summarizes the components of the Company s current capital resources at December 31, 2011 and 2010:

(U.S. dollars in thousands)	2011	2010
Redeemable Series C preference ordinary shares	$	$ 71,900
Series D preference ordinary shares	345,000	
Series E preference ordinary shares	999,500	1,000,000
Ordinary share capital	9,424,910	9,613,049
Total ordinary and non-controlling interests capital	$ 10,769,410	$ 10,684,949
Notes payable and debt	2,264,618	2,446,735
Total capital	$ 13,034,028	$ 13,131,684

Ordinary Share Capital

The following table reconciles the opening and closing ordinary share capital positions at December 31, 2011 and 2010:

(U.S. dollars in thousands)	2011	2010
Ordinary share equity beginning of period	$ 9,613,049	$ 8,432,417
Net income (loss) attributable to XL Group plc	(474,760)	603,550
Share buybacks	(667,022)	(521,920)
Share issues	573,015	1,109
Ordinary share dividends	(138,978)	(134,238)
Preferred share dividends		(34,694)
Gain on redemption of Series C preference ordinary shares		16,616
Change in accumulated other comprehensive income	482,269	1,243,262
Impact of adoption of new authoritative embedded derivative guidance, net of tax		(31,917)
Share based compensation and other	37,337	38,864
Ordinary share equity end of period	$ 9,424,910	$ 9,613,049

Debt

The following tables present the Company s debt under outstanding securities and lenders commitments as at December 31, 2011:

Notes Payable and Debt *(U.S. dollars in thousands)*	**Commitment/ Debt**	**In Use/ Outstanding**	**Year of Expiry**	**Payments Due by Period**			
				Less than 1 Year	**1 to 3 Years**	**3 to 5 Years**	**After 5 Years**
4-year revolver	$ 1,000,000	$	2015	$	$	$	$
6.50% XLCFE Notes (1)	600,000	599,971	2012	600,000			
5.25% Senior Notes	600,000	597,501	2014		600,000		
5.75% Senior Notes	400,000	395,963	2021				400,000
6.375% Senior Notes	350,000	348,592	2024				350,000
6.25% Senior Notes	325,000	322,591	2027				325,000
	$ 3,275,000	$ 2,264,618		$ 600,000	$ 600,000	$	$ 1,075,000
Adjustment to carrying value impact of fair value hedges		10,709					

Carrying value	$ 2,275,327

(1) The XLCFE Notes were repaid at maturity on January 15, 2012.

In Use and Outstanding data represent December 31, 2011 accreted values. Payments Due by Period data represent ultimate redemption values.

In addition, see Item 8, Note 13 to the Consolidated Financial Statements, Notes Payable and Debt Financing Arrangements, for further information.

At December 31, 2011, banks and investors provided the Company and its subsidiaries with $3.3 billion of debt capacity, of which $2.3 billion was utilized by the Company. These facilities consist of:

a revolving credit facility of $1.0 billion.

senior unsecured notes of approximately $2.3 billion. These notes require the Company to pay a fixed rate of interest during their terms. At December 31, 2011, there were five outstanding issues of senior unsecured notes:

$600 million XLCFE Notes due January 2012, with a fixed coupon of 6.5%. These notes were repaid at maturity on January 15, 2012. The notes were issued at 99.469% and gross proceeds were $596.8 million. Related expenses of the offering amounted to $7.9 million.

$600 million senior notes due September 2014, with a fixed coupon of 5.25%. The security is publicly traded. The notes were issued in two tranches of $300 million aggregate principal amount each one tranche at 99.432% and the other at 98.419%. Aggregate gross proceeds were $593.6 million. Related expenses of the offering amounted to $4 million.

$400 million senior notes due October 2021, with a fixed coupon of 5.75%. The security is publicly traded. The notes were issued at 100.0% and gross proceeds were $395.9 million. Related expenses of the offering amounted to $4.1 million.

$350 million senior notes due November 2024, with a fixed coupon of 6.375%. The security is publicly traded. The notes were issued at 100.0% and gross proceeds were $350 million. Related expenses of the offering amounted to $2 million.

$325 million of senior notes due May 2027, with a fixed coupon of 6.25%. The security is publicly traded. The notes were issued at 99.805% and gross proceeds were $324.4 million. Related expenses of the offering amounted to $2.5 million.

Preferred Shares and Non-controlling Interest in Equity of Consolidated Subsidiaries

Neither the Redeemable Series C preference ordinary shares nor the Series E preference ordinary shares were transferred from XL-Cayman to XL-Ireland in the Redomestication. Accordingly, subsequent to July 1, 2010, these instruments represent non-controlling interests in the consolidated financial statements of the Company and have been reclassified to non-controlling interest in equity of consolidated subsidiaries. See Item 8, Note 1, General to Consolidated Financial Statements for further information. During the third quarter of 2011, all Redeemable Series C preference ordinary shares were purchased and canceled. See Key Focuses of Management Capital Management herein. At December 31, 2011, the face value of the outstanding Series E preference ordinary shares was $999.5 million.

On October 15, 2011, XL-Cayman issued 350,000 non-cumulative Series D Preference Ordinary Shares for $350 million of cash and liquid investments that were held in a trust account that was part of the Stoneheath facility. Holders of the Stoneheath Securities received one Series D Preference Ordinary Share in exchange for each Stoneheath Security. See Contingent Capital below.

On December 5, 2011, the Company repurchased 5,000 of the outstanding Series D Preference Ordinary Shares with a liquidation preference value of $5.0 million for $3.7 million, including accrued dividends. As a result of these repurchases, the Company recorded a gain of approximately $1.3 million through Non-controlling interests in the Consolidated Statement of Income in the fourth quarter of 2011. At December 31, 2011, the face value of the outstanding Series D Preference Ordinary Shares was $345.0 million.

In August 2011, in accordance with the terms of the 10.75% Units, XL-Cayman purchased and retired all of the 8.25% Senior Notes for $575 million in a remarketing. These notes comprised a part of the 10.75% Units. The proceeds from the remarketing were used to satisfy the purchase price for XL-Ireland s ordinary shares issued to holders of the 10.75% Units pursuant to the forward purchase contracts comprising a part of the 10.75% Units. Each forward purchase contract provided for the issuance of 1.3242 ordinary shares of XL-Ireland at a price of $25 per share. The settlement of the forward purchase contracts resulted in XL-Ireland s issuance of an aggregate of 30,456,600 ordinary shares for an aggregate purchase price of $575 million. As a result of the settlement of the forward purchase contracts, the 10.75% Units ceased to exist and are no longer traded on the NYSE.

In August 2011, XL-Cayman completed a cash tender offer for its outstanding Redeemable Series C preference ordinary shares that resulted in 2,811,000 Redeemable Series C preference ordinary shares with a liquidation value of $25.00 being repurchased and canceled by XL-Cayman for approximately $71.0 million including accrued and unpaid dividends and professional fees. Subsequent to the expiration of the tender offer, and on the same terms as the offer, XL-Cayman repurchased and canceled the remaining outstanding Redeemable Series C preference ordinary shares with a liquidation value of $25.00 for approximately $0.9 million plus accrued and unpaid dividends. Therefore, no Redeemable Series C preference ordinary shares were outstanding at December 31, 2011.

On February 16, 2011, the Company repurchased 30,000 of the outstanding Redeemable Series C preference ordinary shares with a liquidation preference value of $0.75 million for $0.65 million. In addition, the Company repurchased 500 of the outstanding Series E preference ordinary shares with a liquidation preference value of $0.50 million for $0.47 million. As a result of these

repurchases, the Company recorded a reduction in Non-controlling interests of approximately $0.13 million in the first quarter of 2011.

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

On March 26, 2009, the Company completed a cash tender offer for its outstanding Redeemable Series C preference ordinary shares that resulted in approximately 12.7 million Redeemable Series C preference ordinary shares with a liquidation value of $317.3 million being purchased by the Company for approximately $104.7 million plus accrued and unpaid dividends, combined with professional fees totaling $0.8 million. As a result, a book value gain of approximately $211.8 million was recorded in the first quarter of 2009 to ordinary shareholders. In addition, see Item 8, Note 18 to the Consolidated Financial Statements, Share Capital, for further information.

Contingent Capital

At December 31, 2011, the Company did not have any contingent capital transactions. At December 31, 2010, the Company had one contingent capital transaction where the outstanding put option had not been exercised, as discussed below.

On December 5, 2006, the Company and certain operating subsidiaries (Ceding Insurers) entered into a securities issuance agreement (the Securities Issuance Agreement), and certain of the Company s foreign insurance and reinsurance subsidiaries (Ceding Insurers) entered into an excess of loss reinsurance agreement (the Reinsurance Agreement), with Stoneheath. The net effect of these agreements to the Company was the creation of a contingent put option to issue $350.0 million of preference ordinary shares in the aggregate of XL-Cayman. The agreements provided the Company with a Reinsurance Collateral Account in support of certain covered perils named in the Reinsurance Agreement. The covered perils included United States wind, European wind, California earthquake and terrorism worldwide. After an initial three-month period, the covered perils as well as the attachment points and aggregate retention amounts could be changed by the Ceding Insurers in their sole discretion, which could have resulted in a material increase or decrease in the likelihood of payment under the Reinsurance Agreement. On each date on which a Ceding Insurer withdrew funds from the Reinsurance Collateral Account, the Company would have been required to issue and deliver to Stoneheath an amount of Series D Preference Ordinary Shares having an aggregate liquidation preference that is equal to the amount of funds so withdrawn from the Collateral Account. The Company was obligated to reimburse Stoneheath for certain fees and ordinary expenses. The initial term of the Reinsurance Agreement was for the period from the December 5, 2006 through June 30, 2007, with four annual mandatory extensions through June 30, 2011 (unless coverage is exhausted thereunder prior to such date). At the Ceding Insurers option, the Reinsurance Agreement was extended to December 31, 2011.

On October 15, 2011, the Company announced that the Stoneheath facility would be terminated and, as a result, XL-Cayman would issue Series D Preference Ordinary Shares. Under the terms of the Securities Issuance Agreement, XL-Cayman was required upon the occurrence of certain conditions to issue and deliver to Stoneheath for distribution to the holders of the Stoneheath Securities, Series D Preference Ordinary Shares having an aggregate liquidation preference equal to the remaining assets in the Reinsurance Collateral Account in exchange for a distribution of such assets from the Reinsurance Collateral Account to XL-Cayman. One such condition, the termination of an asset swap agreement covering the assets held under the Reinsurance Collateral Account, occurred in accordance with the terms of the swap agreement because Stoneheath did not seek to extend or replace it prior to its termination date. As a result, on November 16, 2011, Stoneheath redeemed the Stoneheath Securities and distributed the Series D Preference Ordinary Shares it received from XL-Cayman in exchange for the $350 million in assets from the Reinsurance Collateral Account.

Letter of Credit Facilities and other sources of collateral

At December 31, 2011, the Company had five letter of credit facilities in place with total availability of $4.0 billion, of which $1.9 billion was utilized.

Other Commercial Commitments *(U.S. dollars in thousands)*	**Commitment**	**In Use**	**Year of Expiry**	**Amount of Commitment Expiration per period**			
				Less than 1 Year	**1 to 3 Years**	**3 to 5 Years**	**After 5 Years**
Letter of Credit Facility (1)	$ 1,000,000	$ 805,770	2014		1,000,000		
Letter of Credit Facility (2) (3)	1,350,000	116,664	2015			1,350,000	
Letter of Credit Facility (3)	650,000	487,851	2015			650,000	

Letter of Credit Facility	750,000	344,659	Continuous				
Letter of Credit Facility	250,000	116,248	Continuous				
Five letter of credit facilities	$ 4,000,000	$ 1,871,192		$	$ 1,000,000	$ 2,000,000	$

(1) The Company has the option to increase the size of the March 2011 Credit Agreement by an additional $500 million.

(2) This letter of credit facility includes $1.0 billion that is also included in the 4-year revolver listed under Notes Payable and Debt.
(3) The Company has the option to increase the size of the facilities under the December 2011 Credit Agreements by an additional $500 million across both such facilities.

In 2011, the Company and certain of its subsidiaries (i) entered into three new credit agreements, which provided for an aggregate amount of outstanding letters of credit and revolving credit loans up to $3 billion, subject to certain options to increase the size of the facilities, and (ii) terminated the five-year credit agreement dated June 21, 2007 (the 2007 Credit Agreement), which had provided for an aggregate amount of outstanding letters of credit and revolving credit loans up to $4 billion.

On March 25, 2011, the Company and certain of its subsidiaries entered into a secured credit agreement (the March 2011 Credit Agreement) that currently provides for issuance of letters of credit up to $1 billion with the option to increase the size of the facility by an additional $500 million. Concurrent with the effectiveness of the 2011 Credit Agreement, the commitments of the lenders under the 2007 Credit Agreement were reduced from $4 billion to $3 billion. The commitments under the March 2011 Credit Agreement will expire on, and the credit facility is available on a continuous basis until, the earlier of (i) March 25, 2014 and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon an event of default.

On December 9, 2011, the Company and certain of its subsidiaries entered into (i) a new secured credit agreement (the December 2011 Secured Credit Agreement) and (ii) a new unsecured credit agreement (the December 2011 Unsecured Credit Agreement and together with the December 2011 Secured Credit Agreement, the December 2011 Credit Agreements). In connection with the December 2011 Credit Agreements, the 2007 Credit Agreement was terminated. The March 2011 Credit Agreement continues in force, but was amended to conform certain of its terms to those of the December 2011 Secured Credit Agreement.

The 2007 Credit Agreement had provided for letters of credit and for revolving credit loans of up to $750 million with the aggregate amount of outstanding letters of credit and revolving credit loans thereunder not to exceed $3 billion. At the time at which it was terminated and the December 2011 Credit Agreements became effective, there were no outstanding revolving credit loans under the 2007 Credit Agreement. A portion of the letters of credit outstanding under the 2007 Credit Agreement at the time of its termination were continued under the March 2011 Credit Agreement and the remainder were continued under the December 2011 Credit Agreements.

The December 2011 Secured Credit Agreement provides for issuance of letters of credit up to $650 million. The December 2011 Unsecured Credit Agreement is a $1.35 billion facility that provides for issuance of letters of credit and up to $1 billion of revolving credit loans. The Company has the option to increase the maximum amount of letters of credit available by an additional $500 million across the facilities under the December 2011 Credit Agreements.

The commitments under each December 2011 Credit Agreement expire on, and such credit facilities are available until, the earlier of (i) December 9, 2015 and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon an event of default.

The availability of letters of credit under the December 2011 Secured Credit Agreement and the March 2011 Credit Agreements is subject to a borrowing base requirement, determined on the basis of specified percentages of the face value of eligible categories of assets varying by type of collateral. In the event that such credit support is insufficient, the Company could be required to provide alternative security to cedants. This could take the form of insurance trusts supported by the Company s investment portfolio or funds withheld (amounts retained by ceding companies to collateralize loss or premium reserves) using the Company s cash resources or combinations thereof. The face amount of letters of credit required is driven by, among other things, loss development of existing reserves, the payment pattern of such reserves, the expansion of business written by the Company and the loss experience of such business. In addition to letters of credit, the Company has established insurance trusts in the United States that provide cedants with statutory credit for reinsurance under state insurance regulation in the United States.

The Company reviews current and projected collateral requirements on a regular basis, as well as new sources of collateral. Management s objective is to maintain an excess amount of collateral sources over expected uses. The Company also reviews its liquidity needs on a regular basis.

In October 2011, the $75,000 letter of credit facility that was supporting a subsidiary of the Company terminated.

On June 22, 2010, a $2.3 billion five-year letter of credit facility expired and was not replaced.

Covenants

The Company s Credit Facilities contains a number of financial covenants that must be met and maintained, and that among other things, could restrict, subject to certain exceptions, our financial flexibility including the ability to:

engage in mergers or consolidations;

dispose of assets outside of the ordinary course of business;

create liens on assets; and

engage in certain transactions with affiliates.

The following outlines the covenant requirements and actual amounts as of December 31, 2011:

	Covenant Requirement	Actual Ratio or Balance at December 31, 2011	Margin of Adverse Development from December 31, 2011 Levels
Ratio of Total Funded Debt to Total Capitalization (1)	Less than 0.35:1.00	0:18:1.00	$2.1 billion
Maximum Secured Indebtedness (2)	Less than 15% of consolidated net worth	$345 million	$1.2 billion
Consolidated Net Worth (3)	$6.5 billion	$10.3 billion	$3.8 billion
Financial Strength Ratings (4)	A- or better from A.M. Best	A(Stable)	Two notches

(1) The ratio of total funded debt to total capitalization not to be greater than 0.35:1.00. This ratio is defined as total funded debt to the sum of total funded debt plus consolidated net worth.

(2) Secured indebtedness excludes secured letter of credit facilities as permitted under the schedules to the credit facilities. At December 31, 2011, such secured letter of credit facilities amounted to $1.75 billion.

(3) Consolidated net worth means, at any time, the consolidated stockholders equity of the Company excluding (a) the effect of any adjustments required under the authoritative accounting guidance for accounting for certain investments in debt and equity securities; and (b) any exempt indebtedness (and the assets relating thereto) in the event such exempt indebtedness is consolidated on the consolidated balance sheet the Company.

(4) Covenants require that none of XL Insurance (Bermuda) Ltd, XL Re Ltd or XL Re Europe Ltd has a financial strength ratings of less than A from A.M. Best. At December 31, 2011, the Company was in compliance with such covenants.

As noted in the table above, at December 31, 2011, the Company was in compliance with all covenants by significant margins, and the Company currently remains in compliance.

CROSS-DEFAULT AND OTHER PROVISIONS IN DEBT INSTRUMENTS

The following describes certain terms of the documents referred to below. All documents referred to below have been filed with the SEC and should be referred to for an assessment of the complete contractual obligations of the Company.

In general, all of the Company s bank facilities, indentures and other documents relating to the Company s outstanding indebtedness, including the credit facilities discussed above (collectively, the Company s Debt Documents), contain cross default provisions to each other and the Company s Debt Documents contain affirmative covenants. These covenants provide for, among other things, minimum required ratings of the Company s insurance and reinsurance operating subsidiaries and minimum required levels of secured indebtedness in the future. In addition, generally each of the Company s Debt Documents provide for an event of default in the event of a change of control of the Company or certain events involving bankruptcy, insolvency or reorganization of the Company.

A downgrade below A of the Company s principal insurance and reinsurance subsidiaries by either S&P or A.M. Best, which is two notches below the current S&P financial strength rating of A (Stable) and the A.M. Best financial strength rating of A (Stable) of these subsidiaries, may trigger cancelation provisions in a significant amount of the Company s assumed reinsurance agreements and may potentially require the Company to return unearned premiums to cedants. In addition, due to collateral posting requirements under the Company s letter of credit and revolving credit facilities, such a downgrade may require the posting of cash collateral in support of certain in use portions of these facilities (see Liquidity and Capital Resources). In certain limited instances, such downgrades may require the Company to return cash or assets to counterparties or to settle derivative and/or other transactions with the respective counterparties. See Item 1A, Risk Factors, A downgrade or potential downgrade in our financial strength and credit ratings by one or more rating agencies could materially and negatively impact our business, financial condition, results of operations and/or liquidity.

Under the March 2011 Credit Agreement and December 2011 Credit Agreements, in the event that XL Insurance (Bermuda) Ltd, XL Re Ltd or XL Re Europe Ltd fail to maintain a financial strength rating of at least A from A.M. Best, an event of default would occur.

Given that all of the Company s Debt Documents contain cross default provisions, this may result in all holders declaring such debt due and payable and an acceleration of all debt due under those documents. If this were to occur, the Company may not have funds sufficient at that time to repay any or all of such indebtedness.

LONG-TERM CONTRACTUAL OBLIGATIONS

The following table presents the Company s long term contractual obligations and related payments as at December 31, 2011, due by period. This table excludes further commitments of $135.2 million to the Company s related investment funds and certain limited partnerships, and letter of credit facilities of $1.9 billion. See Item 8, Note 14 to the Consolidated Financial Statements, Derivative Instruments, and Note 17 to the Consolidated Financial Statements, Commitments and Contingencies. See Item 8, Note 13 to the Consolidated Financial Statements, Notes Payable and Debt and Financing Arrangements, for further information.

Contractual Obligations *(U.S. dollars in thousands)*	**Total**	**Less than 1 year**	**1 to 3 years**	**3 to 5 years**	**More than 5 years**
Long-term debt obligations	$ 2,275,000	$ 600,000	$ 600,000	$	$ 1,075,000
Interest on long-term debt	944,910	100,294	263,453	198,607	382,556
Operating lease obligations	180,936	34,867	56,877	33,413	55,779
Capital lease obligations	224,645	11,169	23,183	24,356	165,937
Deposit liabilities (1)	2,419,629	165,270	245,552	314,663	1,694,144
Future policy benefits (2)	7,806,322	387,336	754,256	743,967	5,920,763
Unpaid losses and loss expenses property and casualty operations (3)	20,960,825	4,810,155	5,775,328	3,401,607	6,973,735
Total	$ 34,812,267	$ 6,109,091	$ 7,718,649	$ 4,716,613	$ 16,267,914

(1) Deposit liabilities on the Company s Consolidated Balance Sheet at December 31, 2011 were $1,608,108. The difference from the amount included above relates to the discount on payments due in the future. The payment related to these liabilities varies primarily based on interest rates. The ultimate payments associated with these liabilities could differ from the Company s estimate. See Item 8, Note 11 to the Consolidated Financial Statements, Deposit Liabilities, for further information.

(2) Future policy benefit reserves related to Life operations were $4,845,394 on the Company s Consolidated Balance Sheet at December 31, 2011. Amounts reflected above include an allowance for future premiums in respect of contracts under which premiums are payable throughout the life of the underlying policy. The value of the discount is also included for those lines of business that have reserves where future claim payments and future premium receipts can be estimated using actuarial principles. The timing and amounts of actual claims payments and premium receipts related to these reserves vary based on the underlying experience of the portfolio. Typical elements of the experience include mortality, morbidity and persistency. The ultimate amount of the claims payments and premium receipts could differ materially from the Company s estimated amounts.

(3) The unpaid loss and loss expenses were $20,613,901 on the Company s Consolidated Balance Sheet at December 31, 2011. The difference from the amount included above relates to the discount on payments due in the future for certain workers compensation lines. The timing and amounts of actual claims payments related to these P&C reserves vary based on many factors including large individual losses, changes in the legal environment, as well as general market conditions. The ultimate amount of the claims payments could differ materially from the Company s estimated amounts. For information regarding the estimates for unpaid loss and loss expenses as well as factors effecting potential payment patterns of reserves for actual and potential claims related the Company s different lines of business see Critical Accounting Policies and Estimates above. Certain lines of business written by the Company, such as excess casualty, have loss experience characterized as low frequency and high severity. This may result in significant variability in loss payment patterns and, therefore, may impact the related asset/liability investment management process. In order to be in a position, if necessary, to make these payments, the Company s liquidity requirements are supported by having revolving lines of credit facilities available to the Company and significant reinsurance programs, in addition to the Company s general high grade fixed income investment portfolio.

Variable Interest Entities (VIEs) and Other Off-Balance Sheet Arrangements

At times, the Company has utilized VIEs both indirectly and directly in the ordinary course of the Company s business.

The Company invests in CDOs, and other investment vehicles that are issued through variable interest entities as part of the Company s investment portfolio. The activities of these VIEs are generally limited to holding the underlying collateral used to service investments therein. Our involvement in these entities is passive in nature and we are not the arranger of these entities. The Company has not been involved in establishing these entities. The Company is not the primary beneficiary of these variable interest entities as contemplated in current authoritative accounting guidance.

The Company has a limited number of remaining outstanding credit enhancement exposures including written financial guarantee and credit default swap contracts. The obligations related to these transactions are often securitized through variable interest entities. The Company is not the primary beneficiary of these variable interest entities as contemplated in current authoritative accounting guidance. For further details on the nature of the obligations and the size of the Company s maximum exposure see Item 8, Note 14, Derivative Instruments, and Note 17(h), Commitments and Contingencies Financial and Other Guarantee Exposures, and to the Consolidated Financial Statements.

The Company has utilized variable interest entities in certain instances as a means of accessing contingent capital. The Company has utilized unconsolidated entities in the formation of contingent capital facilities.

At December 31, 2011, the Company did not have any contingent capital facilities. The following description is of the contingent capital facility that was terminated in the fourth quarter of 2011.

On December 5, 2006, the Company and ceding insurers entered into a securities issuance agreement, and certain of the Company s ceding insurers entered into a reinsurance agreement, with Stoneheath. The net effect of these agreements to the Company was the creation of a contingent put option in the amount of $350.0 million in the aggregate. The Company s interests in Stoneheath represented an interest in a variable interest entity under current authoritative accounting guidance, however, the Company was not the primary beneficiary as contemplated in that guidance.

The agreements provided the Company with a Reinsurance Collateral Account in support of certain covered perils named in the Reinsurance Agreement. The covered perils include U.S. wind, European wind, California earthquake and terrorism worldwide. The contingent put option was recorded at fair value with changes in fair value recognized in earnings.

Recent Accounting Pronouncements

See Item 8, Note 2 to the Consolidated Financial Statements, Significant Accounting Policies, for a discussion of recent accounting pronouncements.

Return on Ordinary Shareholders Equity Calculation

The following is a reconciliation of the Company s annualized return on ordinary shareholders equity for the years ended December 31:

(U.S. dollars in thousands)	2011	2010	2009
Opening shareholders equity	$ 10,613,049	$ 9,432,417	$ 6,116,831
Less: Non-controlling interest in equity of consolidated subsidiaries	(1,002,296)	(2,305)	(1,598)
Less: Series E preference ordinary shares		(1,000,000)	(1,000,000)
Opening ordinary shareholders equity	$ 9,610,753	$ 8,430,112	$ 5,115,233
Closing shareholders equity	10,769,410	10,613,049	9,432,417
Less: Non-controlling interest in equity of consolidated subsidiaries	(1,344,472)	(1,002,296)	(1,002,305)
Closing ordinary shareholders equity	$ 9,424,938	$ 9,610,753	$ 8,430,112
Average ordinary shareholders equity	9,517,845	9,020,432	6,772,673
Net income (loss) attributable to ordinary shareholders	(474,760)	585,472	206,607
	(5.0)%	6.5%	3.1%

Return on ordinary shareholders equity	Net income (loss) attributable to ordinary shareholders	

Cautionary Note Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 (PSLRA) provides a safe harbor for forward-looking statements. Any prospectus, prospectus supplement, the Company s Annual Report to ordinary shareholders, any proxy statement, any other Form 10-K, Form 10-Q or Form 8-K of the Company or any other written or oral statements made by or on behalf of the Company may include forward-looking statements that reflect the Company s current views with respect to future events and financial performance. Such statements include forward-looking statements both with respect to the Company in general, and to the insurance and reinsurance sectors in particular (both as to underwriting and investment matters). Statements that include the words expect, intend, plan, believe, project, anticipate, will, may and similar statements of a fu forward-looking nature identify forward-looking statements for purposes of the PSLRA or otherwise.

All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in such statements. The Company believes that these factors include, but are not limited to, the following: (i) changes in the size of the Company s claims relating to natural or man-made catastrophe losses due to the preliminary nature of some reports and estimates of loss and damage to date; (ii) trends in rates for property and casualty insurance and reinsurance; (iii) the timely and full recoverability of reinsurance placed by the Company with third parties, or other amounts due to the Company; (iv) changes in ratings, rating agency policies or practices; (v) changes in the projected amount of ceded reinsurance recoverables and the ratings and creditworthiness of reinsurers; (vi) the timing of claims payments being faster or the receipt of reinsurance recoverables being slower than anticipated by the Company; (vii) the Company s ability to successfully implement its business strategy especially during a soft market cycle; (viii) increased competition on the basis of pricing, capacity, coverage terms or other factors, which could harm the Company s ability to maintain or increase its business volumes or profitability; (ix) greater frequency or severity of claims and loss activity than the Company s underwriting, reserving or investment practices anticipate based on historical experience or industry data; (x) changes in general economic conditions, including the effects of inflation on the Company s business, including on pricing and reserving, and changes in interest rates, credit spreads, foreign currency exchange rates and future volatility in the worlds credit, financial and capital markets that adversely affect the performance and valuation of the Company s investments or access to such markets; (xi) developments, including uncertainties related to the ability of Euro-zone countries to service existing debt obligations and the strength of the Euro as a currency and to the financial condition of counterparties, reinsurers and other companies that are at risk of bankruptcy to affect the Company s business; (xii) the potential impact on the Company from government-mandated insurance coverage for acts of terrorism; (xiii) the potential for changes to methodologies, estimations and assumptions that underlie the valuation of the Company s financial instruments that could result in changes to investment valuations; (xiv) changes to the Company s assessment as to whether it is more likely than not that the Company will be required to sell, or has the intent to sell, available for sale debt securities before their anticipated recovery; (xv) availability of borrowings and letters of credit under the Company s credit facilities; (xvi) the ability of the Company s subsidiaries to pay dividends to XL Group plc and XLIT Ltd.; (xvii) the potential effect of regulatory developments in the jurisdictions in which the Company operates, including those which could impact the financial markets or increase the Company s business costs and required capital levels; (xviii) changes in regulation or laws applicable to XL Group plc or its subsidiaries, brokers or customers; (xix) acceptance of the Company s products and services, including new products and services; (xx) changes in the availability, cost or quality of reinsurance; (xxi) changes in the distribution or placement of risks due to increased consolidation of insurance and reinsurance brokers; (xxii) loss of key personnel; (xxiii) changes in accounting policies or practices or the application thereof; (xxiv) legislative or regulatory developments including, but not limited to, changes in regulatory capital balances that must be maintained by the Company s operating subsidiaries and governmental actions for the purpose of stabilizing the financial markets; (xxv) the effects of mergers, acquisitions and divestitures; (xvi) developments related to bankruptcies of companies insofar as they affect property and casualty insurance and reinsurance coverages or claims that the Company may have as a counterparty; (xxvii) changes in applicable tax laws, tax treaties or tax regulations or the interpretation or enforcement thereof; (xxviii) the effects of business disruption or economic contraction due to war, terrorism or other hostilities; (xxix) the Company s ability to realize the expected benefits from the redomestication; and (xxx) the other factors set forth in Item 1A, Risk Factors, and the Company s other documents on file with the SEC. The foregoing review of important factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included herein or elsewhere. The Company undertakes no obligation to update publicly or revise any forward-looking statement, whether as a result of new information, future developments or otherwise, except as required by the federal securities laws.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following risk management discussion and the estimated amounts generated from the sensitivity and value-at-risk (VaR) analyses presented in this document are forward-looking statements of market risk assuming certain adverse market conditions occur. Actual results in the future may differ materially from these estimated results due to, among other things, actual developments in the global financial markets and changes in the composition of the Company s investment portfolio. The results of analysis used by the Company to assess and mitigate risk should not be considered projections of future events of losses. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Cautionary Note Regarding Forward-Looking Statements.

Market risk represents the potential for loss due to adverse changes in the fair value of financial and other instruments. The Company is principally exposed to the following market risks: interest rate risk, foreign currency exchange rate risk, equity price risk, and credit risk. For a discussion of related risks, see the risk factor titled We are exposed to significant capital markets risk related to changes in interest rates, credit spreads, equity prices and foreign exchange rates as well as other investment risks, which may adversely affect our results of operations, financial condition or cash flows in Item 1A, Risk Factors , above.

The majority of the Company s market risk arises from its investment portfolio which consists of fixed income securities, alternative investments, public equities, private investments, derivatives, other investments, and cash, denominated in both U.S. and foreign currencies, which are sensitive to changes in interest rates, credit spreads, equity prices, foreign currency exchange rates and other related market risks. The Company s fixed income and equity securities are primarily classified as available for sale; accordingly market related changes will have an immediate effect on comprehensive income and shareholders equity but will not ordinarily have an immediate effect on net income. Nevertheless, market related changes affect consolidated net income when, and if, a security is sold or is impaired.

On a limited basis the Company may enter into derivatives and other financial instruments primarily for risk management purposes. For example, the Company may use derivatives to hedge foreign exchange and interest rate risk related to its consolidated net exposures. From time to time, the Company may also use instruments such as futures, options, interest rate swaps, credit default swaps and foreign currency forward contracts to manage the risk of interest rate changes, credit deterioration, foreign currency exposures, and other market related exposures and also to obtain exposure to a particular financial market. Historically, the Company entered into credit derivatives outside of the investment portfolio in conjunction with the legacy financial guarantee and financial products operations. The Company attempts to manage the risks associated with derivative use with guidelines established by senior management. Derivative instruments are carried at fair value with the resulting changes in fair value recognized in income in the period in which they occur. See Item 8, Note 14 to the Consolidated Financial Statements, Derivative Instruments, for further information.

This risk management discussion and the estimated amounts generated from the sensitivity and VaR analyses presented in this document are forward-looking statements of market risk assuming certain adverse market conditions occur. Actual results in the future may differ materially from these estimated results due to, among other things, actual developments in the global financial markets and changes in the composition of the Company s investment portfolio. The results of analysis used by the Company to assess and mitigate risk should not be considered projections of future events of losses. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Cautionary Note Regarding Forward-Looking Statements.

Interest Rate Risk

Interest rate risk is the price sensitivity of a fixed income security to changes in interest rates. The Company s fixed income portfolio is exposed to interest rate risk. The Company s liabilities are accrued at a static rate from an accounting standpoint. However, management considers the liabilities to have an economic exposure to interest rate risk and manages the net economic exposure to interest rate risk considering both assets and liabilities. Interest rate risk is managed within the context of its SAA process by specifying SAA Benchmarks relative to the estimated duration of its liabilities and managing the fixed income portfolio relative to the Benchmarks such that the overall economic effect of interest rate risk is within management s risk tolerance. Nevertheless, the Company remains exposed to interest rate risk with respect to the Company s overall net asset position and more generally from an accounting standpoint since the assets are marked to market, while liabilities are accrued at a static rate.

In addition, while the Company s debt is not carried at fair value and not adjusted for market changes, changes in market interest rates could have an impact on debt values at the time of any refinancing.

Foreign Currency Exchange Rate Risk

Many of the Company s non-U.S. subsidiaries maintain both assets and liabilities in local currencies, therefore, foreign exchange risk is generally limited to net assets denominated in foreign currencies.

Foreign currency exchange rate gains and losses in the Company s Statement of Income arise for accounting purposes when net assets or liabilities are denominated in foreign currencies that differ from the functional currency of those subsidiaries. While unrealized foreign exchange gains and losses on underwriting balances are reported in earnings, the offsetting unrealized gains and losses on invested assets are recorded as a separate component of shareholders equity, to the extent that the asset currency does not match that entity s functional currency. This results in an accounting mismatch that will result in foreign exchange gains or losses in the consolidated statements of income depending on the movement in certain currencies. The Company has formed several branches with Euro and U.K. sterling functional currencies and continues to focus on attempting to limit exposure to foreign exchange risk.

Foreign currency exchange rate risk in general is reviewed as part of the Company s risk management framework. Within its asset liability framework for the investment portfolio, the Company pursues a general policy of holding the assets and liabilities in the same currency and as such the Company is not generally exposed to the risks associated with foreign exchange movements within its investment portfolio as currency impacts on the assets are generally matched by corresponding impacts on the related liabilities. However, locally-required capital levels are invested in local currencies in order to satisfy regulatory requirements and to support local insurance operations and are not matched by related liabilities. Foreign exchange contracts within the investment portfolio may be utilized to manage individual portfolio foreign exchange exposures, subject to investment management service providers guidelines established by management. These contracts are generally not designated as specific hedges for financial reporting purposes and, therefore, realized and unrealized gains and losses on these contracts are recorded in income in the period in which they occur. These contracts generally have maturities of three months or less. The Company may also attempt to manage the foreign exchange volatility arising on certain transactions denominated in foreign currencies. These include, but are not limited to, premium receivable, reinsurance contracts, claims payable and investments in subsidiaries.

The principal currencies creating foreign exchange risk for the Company are the U.K. sterling, the Euro, the Swiss franc and the Canadian dollar. The following table provides more information on the Company s net exposures to its principal foreign currencies at December 31, 2011 and December 31, 2010:

(Foreign Currency in Millions)	**2011**	**2010**
Euro	52.0	90.3
U.K. Sterling	35.1	2.1
Swiss Franc	153.7	268.4
Canadian Dollar	222.5	247.8

Credit Risk

Credit risk relates to the uncertainty of an obligor s continued ability to make timely payments in accordance with the contractual terms of the instrument or contract. The Company is exposed to direct credit risk within its investment portfolio as well as through general counterparties, including customers and reinsurers. The Company manages credit risk within its investment portfolio through its Strategic Asset Allocation framework and its established investment credit policies, which address quality of obligors and counterparties, industry limits, and diversification requirements. The Company s exposure to market credit spreads primarily relates to market price and cash flow variability associated with changes in credit spreads.

Certain of the Company s underwriting activities expose it to indirect credit risk in that profitability of certain strategies can correlate with credit events at the issuer level, industry level or country level. The Company manages these risks through established underwriting policies which operate in accordance with established limit and escalation frameworks.

The Company has an established credit risk governance process delegated to the Credit Sub-Committee of the Enterprise Risk Management Committee. The governance process is designed to ensure that transactions and activities, individually and in the aggregate, are carried out within management s risk tolerances.

Credit Risk Investment Portfolio

Credit risk in the investment portfolio is the exposure to adverse changes in the creditworthiness of individual investment holdings, issuers, groups of issuers, industries and countries. A widening of credit spreads will increase the net unrealized loss position, will increase losses associated with credit based non-qualifying derivatives where the Company assumes credit exposure, and, if issuer credit spreads increase significantly for an extended period of time and in a period of increasing defaults, would also likely result in higher other-than-temporary

impairments. All else held equal, credit spread tightening will reduce net investment income associated with new purchases of fixed maturities. In addition, market volatility can make it difficult to value certain of the Company s securities if trading becomes less frequent. As such, valuations may include assumptions or estimates that may have significant period to period changes that could have a material adverse effect on the Company s consolidated results of operations or

financial condition. The credit spread duration in the Company s fixed income portfolio, excluding the impact of the HTM election, was 3.7 years at December 31, 2011.

The Company manages credit risk in the investment portfolio, including fixed income, alternative and short-term investment through the credit research performed primarily by the investment management service providers. The management of credit risk in the investment portfolio is also fully integrated in the Company s credit risk management governance framework and the management of credit exposures and concentrations within the investment portfolio are carried out in accordance with the Company s risk policies, philosophies, appetites, limits and risk concentrations delegated to the investment portfolio. In the investment portfolio, the Company reviews on a regular basis its asset concentration, credit quality and adherence to the Company s credit limit guidelines. Any issuer over its credit limits, experiencing financial difficulties, material credit quality deterioration or potentially subject to forthcoming credit quality deterioration is placed on a watch list for closer monitoring. Where appropriate, exposures are reduced or prevented from increasing.

The table below shows the Company s aggregate fixed income portfolio by credit rating in percentage terms of the Company s aggregate fixed income exposure (including fixed maturities, short-term investments, cash and cash equivalents and net payable for investments purchased) as at December 31, 2011:

	Percentage of Aggregate Fixed Income Portfolio (1) (2)
AAA	51.1%
AA	16.6%
A	22.3%
BBB	7.6%
BB & below	2.3%
Not rated	0.1%
Total (1)	100.0%

(1) Included in the above are $266.0 million or 0.8% of the portfolio that represents medium term notes rated at the average credit rating of the underlying asset pools backing the notes.

(2) The credit rating for each asset reflected above was principally determined based on the weighted average rating of the individual securities from Standard & Poor s, Moody s Investors Service and Fitch Ratings. U.S. agencies paper, whether with implicit or explicit government support, reflect the credit quality rating of the U.S. government for the purpose of these calculations.

At December 31, 2011 and 2010, the average credit quality of the Company s aggregate fixed income investment portfolio was Aa2/AA, excluding operating cash. The Company s $10.7 billion portfolio of government and government related, agency, sovereign and cash holdings were rated AAA at December 31, 2011. The Company s $11.8 billion portfolio of corporates is rated A. The Company s $9.0 billion structured credit portfolio is AA+ rated.

The Company is closely monitoring its corporate financial bond holdings given the events of the past four years. The table below summarizes the Company s significant exposures (defined as bonds issued by financial institutions with an amortized cost in excess of $50.0 million) to corporate bonds of financial issuers held within its available for sale and HTM investment portfolio at December 31, 2011, representing both amortized cost and net unrealized gains (losses):

(U.S. dollars in millions)

Issuer (by Global Ultimate Parent)	Weighted Average Credit Quality (1)	Amortized Cost December 31, 2011 (2)	Unrealized Gain/ (Loss) December 31, 2011
Rabobank Nederland NV	AA+	$ 169.8	$ (2.3)
The Goldman Sachs Group, Inc.	A-	153.8	(8.7)
Lloyds Banking Group plc	AA	146.4	(0.4)
Bank Of America Corporation	A-	128.0	(12.8)
JPMorgan Chase & Co.	A	125.6	(6.6)
National Australia Bank Limited	AA-	118.5	(3.9)
HSBC Holdings plc	A+	117.3	(9.3)
Citigroup Inc.	BBB+	108.4	(6.1)
The Bank Of Nova Scotia	AA	101.6	3.0
Morgan Stanley	A	97.4	(3.1)
Wells Fargo & Company	A+	93.5	2.3
Australia And New Zealand Banking Group Limited	AA-	89.9	(0.5)
H M Government Cabinet Office (RBS Group plc)	AA	85.5	4.1
Westpac Banking Corporation	AA-	83.1	1.3
Canadian Imperial Bank Of Commerce	AA	80.9	2.0
Standard Chartered plc	A	72.7	(3.5)
Nordea Bank AB	AA-	70.9	(1.7)
Credit Suisse Group AG	A+	70.4	(1.8)
UBS AG	A+	70.4	(2.4)
The Bank Of New York Mellon Corporation	AA-	68.7	1.5
BNP Paribas	AA-	68.4	(3.5)
Nationwide Building Society	AA-	67.3	(8.5)
Barclays plc	BBB	64.8	(18.5)
Commonwealth Bank Of Australia	AA-	63.9	(0.8)
Royal Bank Of Canada	AA	61.7	1.5
U.S. Bancorp	A+	60.3	1.1
Bank Of Montreal	AA	58.4	2.0
Svenska Handelsbanken AB	A+	57.7	(2.1)
BPCE	AAA	55.4	0.1
Legal & General Group plc	BBB+	55.2	(7.6)

(1) The credit rating for each asset reflected above was principally determined based on the weighted average rating of the individual securities from Standard & Poor s, Moody s Investors Service and Fitch Ratings. U.S. agencies paper, whether with implicit or explicit government support, reflect the credit quality rating of the U.S. government for the purpose of these calculations.

(2) Government-guaranteed paper has been excluded from the above figures. Included within all financial bond exposures are covered bonds with a fair value of $368.7 million and amortized cost of $360.2 million.

Within the Company s corporate financial bond holdings, the Company is further monitoring its exposures to hybrid securities, representing Tier One and Upper Tier Two securities of various financial institutions. The following table summarizes the top ten exposures to hybrid securities, listed by amortized cost representing both amortized cost and unrealized (losses):

(U.S. dollars in millions)

Issuer (by Global Ultimate Parent)	Tier One Amortized Cost at December 31, 2011	Upper Tier Two Amortized Cost at December 31, 2011	Total Amortized Cost at December 31, 2011	Net Unrealized (Loss) at December 31, 2011
Barclays, Plc	$	$ 50.6	$ 50.6	$ (13.2)
Zurich Financial Services.		25.6	25.6	(4.7)

Aviva PLC	5.4	19.7	25.1	(8.4)
Nationwide Building Society	24.6		24.6	(8.5)
Legal & General Group PLC		24.6	24.6	(5.7)
Standard Life PLC		21.3	21.3	(5.0)
RSA Insurance Group PLC		20.5	20.5	(3.2)
Mitsubishi UFJ Financial Group, Inc.	20.5		20.5	(1.1)
The British United Provident Association Limited		20.1	20.1	(5.7)
Danske Bank A/S	8.9	11.1	20.0	(3.2)
Total	$ 59.4	$ 193.5	$ 252.9	$ (58.7)

At December 31, 2011, the top 10 corporate holdings, which exclude government guaranteed and government sponsored enterprises, represented approximately 5.0% of the aggregate fixed income portfolio and approximately 13.2% of all corporate holdings. The top 10 corporate bond holdings listed below represent the direct exposure to the corporations listed below, including their subsidiaries, and excludes any securitized, credit enhanced and collateralized asset or mortgage-backed securities, cash and cash equivalents, pooled notes and any over-the-counter (OTC) derivative counterparty exposures, if applicable but does include covered bonds.

Top 10 Corporate Holdings (1)	Percentage of Aggregate Fixed Income Portfolio
Wal-Mart Stores, Inc.	0.6%
Pfizer Inc.	0.6%
General Electric Company	0.5%
Rabobank Nederland NV	0.5%
The Proctor & Gamble Company	0.5%
AT&T Inc.	0.5%
Lloyds Banking Group PLC	0.5%
The Goldman Sachs Group, Inc.	0.5%
BP PLC	0.4%
Glaxosmithkline PLC	0.4%

(1) Corporate issuers exclude government related/government guaranteed and supported enterprises and cash and cash equivalents.

As at December 31, 2011, the top 5 corporate sector exposures listed below represented 28.2% of the aggregate fixed income investment portfolio and 78.4% of all corporate holdings.

(U.S. dollars in millions)

Top 5 Sector Exposures	Fair Value	Percentage of Aggregate Fixed Income Portfolio
Financials (1)	$ 3,737.3	11.2%
Consumer, Non-Cyclical	2,273.4	7.1%
Utilities	1,473.8	4.6%
Communications	985.2	3.0%
Industrial	938.7	2.9%
Total	$ 9,408.4	28.8%

(1) Government-guaranteed paper has been excluded from the above figures.

Within the Company s fixed income portfolios, the Company is further monitoring its exposures to holdings representing risk in certain Euro-zone countries (Greece, Italy, Ireland, Portugal and Spain). In particular, the Company has government holdings of $27.0 million, corporate holdings of $225.5 million (financials $20.8 million, non-financials $204.7 million) and structured credit holdings totaling $3.2 million in GIIPS. The non-financial corporate holdings primarily consist of securities issued by multinational companies with low reliance on local economics and systemically important industries such as utilities and telecoms. For further detail on the Company s exposure to the Euro-zone sovereign debt crisis please refer to Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Balance Sheet Analysis.

The Company also has exposure to credit risk associated with its mortgage-backed and asset-backed securities. The table below shows the breakdown of the $9.0 billion structured credit portfolio, of which 78.2% is AAA rated:

(U.S. dollars in millions)	Fair Value	Percentage of Structured Portfolio
CMBS	$ 974.8	10.8%
Non-Agency RMBS	722.8	8.0%
Core CDO (non-ABS CDOs and CLOs)	662.9	7.4%
Other ABS	1,266.8	14.1%
Agency RMBS	5,381.3	59.7%
Total	$ 9,008.6	100.0%

Credit Risk Other

Credit derivatives are purchased within the Company s investment portfolio, have been sold through a limited number of contracts written as part of the Company s previous financial lines business, and were previously entered into through the Company s prior reinsurance agreements with Syncora. From time to time, the Company may purchase credit default swaps to hedge an existing position or concentration of holdings. The credit derivatives are recorded at fair value. See Item 8, Note 14 to the Consolidated Financial Statements, Derivative Instruments, for further information.

The Company has exposure to many different industries and counterparties, and routinely executes transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, alternatives and other investment funds and other institutions. Many of these transactions expose the Company to credit risk in the event of default of the Company s counterparty. In addition, with respect to secured transactions, the Company s credit risk may be exacerbated when the collateral held by the Company cannot be sold or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure that is due. The Company also has exposure to financial institutions in the form of unsecured debt instruments, derivative transactions, revolving credit facility and letter of credit commitments and equity investments. There can be no assurance that any such losses or impairments to the carrying value of these assets would not materially and adversely affect the Company s business and results of operations.

With regards to unpaid losses and loss expenses recoverable and reinsurance balances receivable, the Company has credit risk should any of its reinsurers be unable or unwilling to settle amounts due to the Company; however, these exposures are not marked to market. For further information relating to reinsurer credit risk, see Management s Discussion and Analysis of Financial Condition and Results of Operations Unpaid Losses and Loss Expenses Recoverable and Reinsurance Balances Receivable.

The Company is exposed to credit risk in the event of non-performance by the other parties to its derivative instruments in general; however, the Company does not anticipate non-performance. The difference between the notional principal amounts and the associated market value is the Company s maximum credit exposure.

Equity Price Risk

Equity price risk is the potential loss arising from changes in the market value of equities. The Company s equity investment portfolio is exposed to equity price risk. At December 31, 2011, the Company s equity portfolio was approximately $376.6 million as compared to $84.8 million at December 31, 2010. This excludes fixed income fund investments of $91.6 million that generally do not have the risk characteristics of equity investments but are treated as equity investments under GAAP. At December 31, 2011 and 2010, the Company s direct allocation to equity securities was 1.1% and a negligible percentage, respectively, of the total investment portfolio (including cash and cash equivalents, accrued investment income and net payable for investments purchased). The Company also estimates the equity risk embedded in certain alternative and private investments. Such estimates are derived from market exposures provided to the Company by certain individual fund investments and/or internal statistical analyses.

Other Market Risks

The Company s private investment portfolio is invested in limited partnerships and other entities which are not publicly traded. In addition to normal market risks, these positions may also be exposed to liquidity risk, risks related to distressed investments, and risks specific to startup or small companies. As at December 31, 2011, the Company s exposure to private investments, excluding unfunded commitments, was $288.4 million representing 0.9% of the fixed income portfolio compared to $331.7 million as at December 31, 2010.

The Company s alternative investment portfolio, which is exposed to equity and credit risk as well as certain other market risks, had a total exposure of $1,027.2 million, representing approximately 3.1% of the investment portfolio (including cash and cash equivalents, accrued investment income and net payable for investments purchased) at December 31, 2011, as compared to December 31, 2010, where the Company had a total exposure of $933.5 million representing approximately 2.8% of the investment portfolio.

At December 31, 2011, bond and stock index futures outstanding had a net long position of $12.6 million as compared to a net long position of $14.1 million at December 31, 2010. The Company may reduce its exposure to these futures through offsetting transactions, including options and forwards.

As noted above, the Company also invests in certain derivative positions that can be impacted by market value movements. For further details on derivative instruments see Item 8, Note 14, Derivative Instruments, to the Consolidated Financial Statements.

Sensitivity and Value-at-Risk Analysis

Value-at-Risk (VaR) is central to the Company s market risk management framework for its investment portfolio. VaR is a statistical risk measure representing a specific percentile of estimated potential mark-to-market portfolio returns in normal market conditions over a specific time horizon.

The Company estimates the VaR of the investment portfolio, the P&C investment portfolio and the Life investment portfolio, using a one year holding period and a 95% level of confidence. This means that, on average, the Company could expect mark-to-market losses greater than predicted by the VaR results 5% of the time, or once every 20 years.

The calculation of VaR is performed monthly using an analytical, or variance-covariance approach, based on the linear sensitivity of the investment portfolio and individual securities to a broad set of systematic market risk factors and idiosyncratic risk factors. The Company estimates the parametric sensitivity of every security in the investment portfolio to changes in key interest rates, spreads, implied volatility and equities. The parametric exposures are summed using the appropriate investment portfolio weights to compute the investment portfolio s exposure to these systematic and idiosyncratic market risk factors.

The modeling of risk, as measured by VaR, involves a number of assumptions and approximations. While the Company believes that its assumptions and approximations are appropriate, there is no uniform industry methodology for calculating VaR. The Company notes that different VaR results can be produced for the same portfolio dependent not only on the approach used but also on the assumptions employed when implementing the approach.

The VaR approach uses historical data to determine the sensitivity of each of the underlying securities to the risk factors incorporated into the pricing models employed in the VaR estimates. In calculating these sensitivities, greater importance is placed on the more recent data points and information. Since the VaR approach is based on historical positions and market data, VaR results should not be viewed as an absolute and predictive gauge of future financial performance or as a way for the Company to predict risk. There is no assurance that the Company s actual future losses will not exceed its VaR and the Company expects that 5% of the time the VaR will be exceeded.

Additionally, the Company acknowledges the fact that risks associated with abnormal market events can be significantly different from the VaR results and these are by definition not reflected or assessed in the VaR analysis, rather this is evaluated using the Company s stress testing framework.

The table below summarizes the Company s assessment of the estimated impact on the value of the Company s investment portfolio at December 31, 2011 associated with an immediate and hypothetical: +100bps increase in interest rates, a -10% decline in equity markets, a +100bps widening in spreads and a +10% widening in spreads. The table also reports the 95%, 1-year VaRs for the Company s investment portfolios at December 31, 2011, excluding foreign exchange.

The interest rate, spread risk, and VaR referenced in the table below include the impact of market movements on the Company s held to maturity fixed maturities from the Company s Life investment portfolios. While the market value of these holdings is sensitive to prevailing interest rates and credit spreads, the Company s book value is not impacted as these holdings are carried at amortized cost. At December 31, 2011, if the Company were to exclude these impacts in order to present the impact of these risks to the Company s book value, the interest rate

risk would be reduced by approximately $302.4 million, absolute spread risk would be

reduced by approximately $202.1 million, relative spread risk would be reduced by approximately $31.7 million, and VaR would be reduced by approximately $327.1 million.

The table below excludes the impact of foreign exchange rate risk on the Company s investment portfolio. The Company s investment portfolio is managed on an asset-liability matched basis, and, accordingly, any foreign exchange movements impact the assets and liabilities equally. See foreign exchange rate risk for further details. The Company considers that the investment portfolio VaR estimated results as well as the P&C and Life investment portfolios VaR estimated results excluding foreign exchange rate risk are the more relevant and appropriate metrics to consider when assessing the actual risk of the investment portfolio.

The estimated results below also do not include any risk contributions from our various operating affiliates (strategic, investment manager or financial operating affiliates) or certain other investments that are carried at amortized cost.

(U.S. dollars in thousands)	Interest Rate Risk(1)	Equity Risk (2)	Absolute Spread Risk (3)	Relative Spread Risk (4)	VaR (5)(6)
Total Investment Portfolio (7)	**$ (1,263.9)**	**$ (87.9)**	**$ (1,220.3)**	**$ (241.7)**	**$ 1,380.3**
A. P&C Investment Portfolio	**$ (725.8)**	**$ (87.9)**	**$ (766.7)**	**$ (125.3)**	**$ 783.6**
(I) P&C Fixed Income Portfolio	(725.8)		(766.7)	(125.3)	824.6
(a) Cash & Short Term Investments	(7.5)				10.5
(b) Total Government-Related	(255.8)		(174.6)	(8.6)	249.2
(c) Total Corporate Credit	(301.7)		(335.4)	(61.4)	399.6
(d) Total Structured Credit	(160.9)		(257.5)	(55.4)	247.1
(II) P&C Non-Fixed Income Portfolio		(87.9)			211.4
(e) Equity Portfolio		(38.7)			141.7
(f) Alternative Portfolio		(19.9)			61.9
(g) Private Investments		(29.3)			95.3
B. Life Investment Portfolio	$ (526.2)	$	$ (416.4)	$ (113.5)	$ 694.3
(III) Life Fixed Income Portfolio	(526.2)		(416.4)	(113.5)	694.3
(i) Cash & Short Term Investments	(0.0)				0.2
(j) Total Government-Related	(217.1)		(77.1)	(5.9)	318.8
(k) Total Corporate Credit	(257.3)		(279.4)	(85.8)	359.7
(l) Total Structured Credit	(51.8)		(59.9)	(21.8)	68.4
(IV) Life Non-Fixed Income Portfolio					

(1) The estimated impact on the fair value of the Company s fixed income portfolio of an immediate hypothetical +100 bps adverse parallel shift in global bond curves.

(2) The estimated impact on the fair value of the Company s investment portfolio of an immediate hypothetical -10% change in the value of equity exposures in the Company s equity portfolio, certain equity-sensitive alternative investments and private equity investments. This includes the Company s estimate of equity risk embedded in the alternatives and private investment portfolio with such estimates utilizing market exposures provided to the Company by certain individual fund investments, internal statistical analyses, and/or various assumptions regarding illiquidity and concentrations.

(3) The estimated impact on the fair value of the Company s fixed income portfolio of an immediate hypothetical +100 basis point increase in all global government-related corporate and structured credit spreads to which the Company s fixed income portfolio is exposed. This excludes exposure to credit spreads in the Company s alternative investments, private investments and counterparty exposure.

(4) The estimated impact on the fair value of the Company s fixed income portfolio of an immediate hypothetical +10% increase in all global government-related corporate and structured credit spreads to which the Company s fixed income portfolio is exposed. This excludes exposure to credit spreads in the Company s alternative investments, private investments and counterparty exposure.

(5) The VaR results are based on a 95% confidence interval, with a one year holding period, excluding foreign exchange rate risk. The Company s investment portfolio VaR at December 31, 2011 is not necessarily indicative of future VaR levels.

(6) The VaR results are the standalone VaRs, based on the prescribed methodology, for each component of the Company s Total Investment Portfolio. The standalone VaRs of the individual components are non-additive, with the difference between the summation of the individual component VaRs and their respective aggregations being due to diversification benefits across the individual components. In the case of the VaR results for the Company s Total Investment Portfolio, the results also include the impact associated with the Company s Business and Other Investments.

(7) The Company s Total Investment Portfolio comprises the Company s P&C Investment Portfolio and Life Investment Portfolio as well as the Company s Business and Other Investments that do not form part of the Company s P&C Investment Portfolio or Life Investment Portfolio. The individual results reported in the above table for the Company s Total Investment Portfolio therefore represent the aggregate impact on

the Company s P&C Investment Portfolio, Life Investment Portfolio and the majority of the Company s Other Investments.

Stress Testing

VaR does not provide the means to estimate the magnitude of the loss in the 5% of occurrences when the Company expects the VaR level to be exceeded. To complement the VaR analysis based on normal market environments, the Company considers the impact on the investment portfolio in several different stress scenarios to analyze the effect of unusual market conditions. The Company establishes certain stress scenarios which are applied to the actual investment portfolio. As these stress scenarios and estimated gains and losses are based on scenarios established by the Company, they will not necessarily reflect future stress events or gains and losses from such events. The results of the stress scenarios are reviewed on a regular basis to ensure they are appropriate, based on current shareholders equity, market conditions and the Company s total risk tolerance. It is important to note that when assessing the risk of the Company s investment portfolio, the Company does not take into account either the value or risk associated with the liabilities arising from the Company s operations.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements **Page**

Consolidated Balance Sheets as at December 31, 2011 and 2010	115
Consolidated Statements of Income for the years ended December 31, 2011, 2010 and 2009	116
Consolidated Statements of Comprehensive Income for the years ended December 31, 2011, 2010 and 2009	117
Consolidated Statements of Shareholders Equity for the years ended December 31, 2011, 2010 and 2009	118
Consolidated Statements of Cash Flows for the years ended December 31, 2011, 2010 and 2009	119
Notes to Consolidated Financial Statements for the years ended December 31, 2011, 2010 and 2009	121

XL GROUP PLC

CONSOLIDATED BALANCE SHEETS AS AT DECEMBER 31, 2011 AND 2010

(U.S. dollars in thousands, except share data)	2011	2010
ASSETS		
Investments:		
Fixed maturities, at fair value (amortized cost: 2011, $25,771,715; 2010, $27,322,842)	$ 26,190,025	$ 27,142,105
Equity securities, at fair value (cost: 2011, $480,685; 2010, $56,737)	468,197	84,767
Short-term investments, at fair value (amortized cost: 2011, $359,378; 2010, $450,491)	359,063	450,681
Total investments available for sale	27,017,285	27,677,553
Fixed maturities, held to maturity at amortized cost (fair value: 2011, $2,895,688; 2010, $2,742,626)	$ 2,668,978	$ 2,728,335
Investments in affiliates	1,052,729	1,127,181
Other investments	985,262	893,570
Total investments	31,724,254	32,426,639
Cash and cash equivalents	3,825,125	3,022,868
Accrued investment income	331,758	350,091
Deferred acquisition costs	668,017	633,035
Ceded unearned premiums	596,895	625,654
Premiums receivable	2,411,611	2,414,912
Reinsurance balances receivable	220,017	171,327
Unpaid losses and loss expenses recoverable	3,654,948	3,671,887
Receivable from investments sold	59,727	21,716
Goodwill and other intangible assets	407,321	839,508
Deferred tax asset	115,601	143,525
Other assets	610,803	694,782
Total assets	$ 44,626,077	$ 45,015,944
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Unpaid losses and loss expenses	$ 20,613,901	$ 20,531,607
Deposit liabilities	1,608,108	1,684,606
Future policy benefit reserves	4,845,394	5,075,127
Unearned premiums	3,555,310	3,484,830
Notes payable and debt	2,275,327	2,457,003
Reinsurance balances payable	90,552	122,250
Payable for investments purchased	58,494	34,315
Deferred tax liability	98,420	105,667
Other liabilities	711,161	835,590
Total liabilities	$ 33,856,667	$ 34,330,995
Commitments and Contingencies		
Non-controlling interest - Redeemable Series C preference ordinary shares, 20,000,000 authorized, par value $0.01; Issued and outstanding: (2011, nil; 2010, 2,876,000)	$	$ 71,900
Shareholders Equity:		
Ordinary shares, 999,990,000 authorized, par value $0.01; Issued and outstanding: (2011, 315,645,796; 2010, 316,396,289)	3,157	3,165
Additional paid in capital	8,938,678	8,993,016
Accumulated other comprehensive income	583,064	100,795
Retained earnings (deficit)	(99,961)	513,777
Shareholders equity attributable to XL Group plc	$ 9,424,938	$ 9,610,753

Non-controlling interest in equity of consolidated subsidiaries	1,344,472	1,002,296
Total shareholders equity	$ 10,769,410	$ 10,613,049
Total liabilities, redeemable preference ordinary shares and shareholders equity	$ 44,626,077	$ 45,015,944

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

(U.S. dollars in thousands, except per share amounts)	2011	2010	2009
Revenues:			
Net premiums earned	$ 5,690,130	$ 5,414,061	$ 5,706,840
Net investment income	1,137,769	1,198,038	1,319,823
Realized investment gains (losses):			
Net realized gains (losses) on investments sold	(28,187)	(65,670)	(108,979)
Other-than-temporary impairments on investments	(174,102)	(170,643)	(992,202)
Other-than-temporary impairments on investments transferred to (from) other comprehensive income	13,930	(34,490)	179,744
Total net realized (losses) on investments	(188,359)	(270,803)	(921,437)
Net realized and unrealized (losses) on derivative instruments	(10,738)	(33,843)	(33,647)
Income (loss) from investment fund affiliates	26,253	51,102	78,867
Fee income and other	41,748	40,027	43,201
Total revenues	$ 6,696,803	$ 6,398,582	$ 6,193,647
Expenses:			
Net losses and loss expenses incurred	$ 4,078,391	$ 3,211,800	$ 3,168,837
Claims and policy benefits	535,074	513,833	677,562
Acquisition costs	826,411	788,258	853,558
Operating expenses	1,082,479	971,105	1,055,823
Exchange (gains) losses	(40,640)	(10,161)	84,813
Interest expense	205,592	213,643	216,504
Loss on termination of guarantee		23,500	
Impairment of goodwill	429,020		
Amortization of intangible assets	1,438	1,858	1,836
Total expenses	$ 7,117,765	$ 5,713,836	$ 6,058,933
Income (loss) before income tax and income (loss) from operating affiliates	$ (420,962)	$ 684,746	$ 134,714
Provision for income tax	59,707	162,737	120,307
Income (loss) from operating affiliates	76,786	121,372	60,480
Net income (loss)	$ (403,883)	$ 643,381	$ 74,887
Non-controlling interests	(70,877)	(39,831)	104
Net income (loss) attributable to XL Group plc	$ (474,760)	$ 603,550	$ 74,991
Preference share dividends		(34,694)	(80,200)
Gain on redemption of Redeemable Series C preference ordinary shares		16,616	211,816
Net income (loss) attributable to ordinary shareholders	$ (474,760)	$ 585,472	$ 206,607
Weighted average ordinary shares and ordinary share equivalents outstanding basic	312,896	336,283	340,612
Weighted average ordinary shares and ordinary share equivalents outstanding diluted	312,896	337,709	340,966
Earnings (loss) per ordinary share and ordinary share equivalent basic	$ (1.52)	$ 1.74	$ 0.61

Earnings (loss) per ordinary share and ordinary share equivalent	diluted	$ (1.52)	$ 1.73	$ 0.61

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

(U.S. dollars in thousands)	2011	2010	2009
Net income (loss) attributable to XL Group plc	$ (474,760)	$ 603,550	$ 74,991
Impact of adoption of new authoritative OTTI guidance, net of taxes			(229,670)
Impact of adoption of new authoritative embedded derivative guidance, net of taxes		31,917	
Change in net unrealized gains (losses) on investments, net of tax	446,427	997,066	2,376,556
Change in net unrealized gains (losses) on affiliate and other investments, net of tax	25,269	44,314	14,464
Change in OTTI losses recognized in other comprehensive income, net of tax	39,456	124,906	(123,343)
Change in underfunded pension liability	(2,622)	(2,619)	(3,427)
Change in value of cash flow hedge	439	439	438
Change in net unrealized gains (losses) on future policy benefit reserves		(3,714)	6,554
Foreign currency translation adjustments	(26,700)	50,953	180,888
Comprehensive income (loss)	$ 7,509	$ 1,846,812	$ 2,297,451

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

(U.S. dollars in thousands)	2011	2010	2009
Non-controlling Interest in Equity of Consolidated Subsidiaries:			
Balance beginning of year	$ 1,002,296	$ 2,305	$ 1,598
Non-controlling interests	(83)	4	(104)
Non-controlling interest share in change in AOCI	(2,241)	(13)	811
Transfer from Series E preference ordinary shares and additional paid in capital		1,000,000	
Issuance of Series D preference ordinary shares	350,000		
Purchase of Series D preference ordinary shares	(5,000)		
Purchase of Series E preference ordinary shares	(500)		
Balance end of year	$ 1,344,472	$ 1,002,296	$ 2,305
Series E preference ordinary shares:			
Balance beginning of year	$	$ 10	$ 10
Transfer to non-controlling interest in equity of consolidated subsidiaries		(10)	
Balance end of year	$	$	$ 10
Ordinary Shares:			
Balance beginning of year	$ 3,165	$ 3,421	$ 3,308
Issuance of ordinary shares	308		114
Exercise of stock options	1		
Buybacks of ordinary shares	(317)	(256)	(1)
Balance end of year	$ 3,157	$ 3,165	$ 3,421
Additional paid in capital:			
Balance beginning of year	$ 8,993,016	$ 10,474,688	$ 9,792,371
Issuance of ordinary shares	572,707	1,109	741,177
Buybacks of ordinary shares	(666,705)	(521,664)	(625)
Transfer to non-controlling interest in equity of consolidated subsidiaries		(999,990)	
Dividends on Series E preference ordinary shares			(42,126)
Dividends on ordinary shares			(68,389)
Exercise of stock options, net of tax	1,333	1,182	
Share based compensation expense	38,327	37,691	52,280
Balance end of year	$ 8,938,678	$ 8,993,016	$ 10,474,688
Accumulated Other Comprehensive Income:			
Balance beginning of year	$ 100,795	$ (1,142,467)	$ (3,364,927)
Impact of adoption of new authoritative OTTI guidance, net of taxes			(229,670)
Impact of adoption of new authoritative embedded derivative guidance, net of taxes		31,917	
Change in net unrealized gains (losses) on investments, net of tax	446,427	997,066	2,376,556
Change in net unrealized gains (losses) on affiliate and other investments, net of tax	25,269	44,314	14,464
Change in OTTI losses recognized in other comprehensive income, net of tax	39,456	124,906	(123,343)
Change in underfunded pension liability	(2,622)	(2,619)	(3,427)
Change in value of cash flow hedge	439	439	438
Change in net unrealized gain (loss) on future policy benefit reserves		(3,714)	6,554
Foreign currency translation adjustments	(26,700)	50,953	180,888

Balance end of year	$ 583,064	$ 100,795	$ (1,142,467)
Retained (Deficit) Earnings:			
Balance beginning of year	$ 513,777	$ 94,460	$ (315,529)
Impact of adoption of new authoritative OTTI guidance, net of tax			229,670
Impact of adoption of new authoritative embedded derivative guidance, net of taxes		(31,917)	
Net income (loss) attributable to XL Group plc	(474,760)	603,550	74,991
Dividends on ordinary shares	(138,978)	(134,238)	(68,415)
Dividends on Redeemable Series C and Series E preference ordinary shares		(34,694)	(38,073)
Gain on redemption of Redeemable Series C preference ordinary shares		16,616	211,816
Balance end of year	$ (99,961)	$ 513,777	$ 94,460
Total shareholders equity	$ 10,769,410	$ 10,613,049	$ 9,432,417

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

(U.S. dollars in thousands)	2011	2010	2009
Cash Flows Provided by (used in) Operating Activities:			
Net income (loss)	$ (403,883)	$ 643,381	$ 74,887
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Net realized losses on investments	188,359	270,803	921,437
Net realized and unrealized losses on derivative instruments	10,738	33,843	33,647
Amortization of premiums (discounts) on fixed maturities	120,130	60,869	(8,183)
(Income) loss from investment and operating affiliates	(103,039)	(172,474)	(139,347)
Impairment of goodwill	429,020		
Share based compensation	29,377	31,291	32,231
Depreciation	49,800	40,423	56,078
Accretion of deposit liabilities	82,799	104,311	88,752
Unpaid losses and loss expenses	243,040	(207,526)	(1,120,074)
Future policy benefit reserves	(171,618)	(197,570)	(340,690)
Unearned premiums	95,393	(133,955)	(675,946)
Premiums receivable	(31,286)	94,649	634,893
Unpaid losses and loss expenses recoverable	(2,168)	(74,242)	443,510
Ceded unearned premiums	21,532	83,246	204,442
Reinsurance balances receivable	(49,286)	201,479	191,462
Deferred acquisition costs	(41,881)	12,235	64,736
Reinsurance balances payable	(31,846)	(253,213)	(368,928)
Deferred tax asset - net	(43,583)	104,111	(3,959)
Derivatives	93,796	123,027	(202,162)
Other assets	(10,685)	(22,483)	70,331
Other liabilities	(107,385)	(78,176)	(132,951)
Other	(40,122)	(69,273)	133,074
Total adjustments	$ 731,085	$ (48,625)	$ (117,647)
Net cash provided by (used in) operating activities	$ 327,202	$ 594,756	$ (42,760)
Cash flows provided by (used in) investing activities:			
Proceeds from sale of fixed maturities and short-term investments	$ 5,091,375	$ 5,206,690	$ 12,049,552
Proceeds from redemption of fixed maturities and short-term investments	3,595,922	2,851,815	4,594,672
Proceeds from sale of equity securities	205,736	115,839	394,002
Purchases of fixed maturities and short-term investments	(7,529,962)	(8,098,862)	(17,481,304)
Purchases of equity securities	(631,169)	(157,963)	(19,827)
Net dispositions of investment affiliates	136,281	319,108	770,883
(Acquisition) disposition of subsidiaries, net of cash acquired			41,446
Other investments, net	(36,080)	24,854	(134,781)
Net cash provided by (used in) investing activities	$ 832,103	$ 261,481	$ 214,643

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009 (Continued)

(U.S. dollars in thousands)	2011	2010	2009
Cash Flows (Used in) Provided by Financing Activities:			
Proceeds from issuance of ordinary shares and exercise of stock options	$ 576,333	$ 1,182	$ 745,000
Proceeds from issuance of Series D preference ordinary shares	349,180		
Buybacks of ordinary shares	(667,022)	(522,024)	(626)
Repurchase of Redeemable Series C preference ordinary shares	(71,801)	(94,157)	(104,718)
Repurchase of Series D preference ordinary shares	(3,650)		
Repurchase of Series E preference ordinary shares	(465)		
Dividends paid on ordinary shares	(138,050)	(133,748)	(136,757)
Dividends paid on preference ordinary shares		(40,385)	(88,251)
Distributions to non-controlling interests	(71,483)	(37,392)	
Proceeds from issuance of debt	395,859		
Repayment of debt	(575,000)		(745,000)
Deposit liabilities	(152,617)	(646,819)	(389,575)
Collateral received on securities lending			108,906
Collateral returned on securities lending			(351,568)
Net cash (used in) provided by financing activities	$ (358,716)	$ (1,473,343)	$ (962,589)
Effects of exchange rate changes on foreign currency cash	1,668	(3,723)	80,577
Increase (decrease) in cash and cash equivalents	802,257	(620,829)	(710,129)
Cash and cash equivalents beginning of year	3,022,868	3,643,697	4,353,826
Cash and cash equivalents end of year	$ 3,825,125	$ 3,022,868	$ 3,643,697
Net taxes paid	$ 106,666	$ 75,429	$ 134,948
Interest paid on notes payable and debt	$ 149,133	$ 162,086	$ 172,927

See accompanying Notes to Consolidated Financial Statements

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

1. General

XL Group plc, through its operating subsidiaries (collectively the Company or XL), is a leading provider of insurance and reinsurance coverages to industrial, commercial and professional firms, insurance companies and other enterprises on a worldwide basis. The Company and its various subsidiaries operate globally in 24 countries, through its three business segments: Insurance, Reinsurance and Life operations. These segments are further discussed in Note 4, Segment Information.

For periods prior to July 1, 2010, unless the context otherwise indicates, references herein to the Company are to, and these financial statements include the accounts of, XLIT Ltd. (formerly, XL Capital Ltd), a Cayman Islands exempted company (XL-Cayman), and its consolidated subsidiaries. For periods subsequent to July 1, 2010, unless the context otherwise indicates, references herein to the Company are to, and these financial statements include the accounts of, XL Group plc, an Irish public limited company (XL-Ireland), and its consolidated subsidiaries.

On July 1, 2010, XL-Ireland and XL-Cayman completed a redomestication transaction in which all of the ordinary shares of XL-Cayman were exchanged for all of the ordinary shares of XL-Ireland (the Redomestication). As a result, XL-Cayman became a wholly owned subsidiary of XL-Ireland. On July 23, 2010, the Irish High Court approved XL-Ireland s creation of distributable reserves, subject to the completion of certain formalities under Irish Company law. These formalities were completed in early August 2010.

As described initially in the Company s Quarterly Report on Form 10-Q for the three months ended March 31, 2011, as part of the Redomestication, neither the Redeemable Series C preference ordinary shares nor the Series E preference ordinary shares were transferred from XL-Cayman to XL-Ireland. Accordingly, subsequent to July 1, 2010, these instruments represent non-controlling interests in the consolidated financial statements of the Company. The Redeemable Series C preference ordinary shares should have been reclassified as Non-controlling interest Redeemable Series C preference ordinary shares and the Series E preference ordinary shares should have been reclassified as Non-controlling interest in equity of consolidated subsidiaries. As a result, during the annual period ended December 31, 2010, amounts related to the Redeemable Series C preference ordinary shares and the Series E preference ordinary shares were not correctly classified in the consolidated financial statements of the Company. Management believes that the misclassifications are not material to the previously issued financial statements and accordingly, the Company has revised the December 31, 2010 financial statements in this report. The details of these classification errors are provided below for the annual period ended December 31, 2010. None of the revised classifications affected our total shareholders equity, net income or net income attributable to ordinary shareholders in any period. Details of the reclassifications are as follows:

Consolidated Balance Sheet at December 31, 2010 *(U.S. dollars in thousands)*:	**Previously Reported**	**Revised**
Series E preference ordinary shares, 1,000,000 authorized, par value $0.01; Issued and outstanding: (2010, 1,000,000; 2009, 1,000,000)	$ 10	$
Additional paid in capital	9,993,006	8,993,016
Shareholders equity attributable to XL Group plc	10,610,753	9,610,753
Non-controlling interest in equity of consolidated subsidiaries	2,296	1,002,296
Consolidated Statement of Income and Comprehensive Income for the year ended December 31, 2010 *(U.S. dollars in thousands)*:		
Non-controlling interests	$ (4)	$ (39,831)
Net income (loss) attributable to XL Group plc	643,377	603,550
Preference share dividends	(74,521)	(34,694)
Comprehensive income (loss)	1,886,639	1,846,812

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

2. Significant Accounting Policies

(a) Basis of Preparation and Consolidation

These consolidated financial statements include the accounts of the Company and all of its subsidiaries. These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). To facilitate period-to-period comparisons, certain reclassifications have been made to prior year consolidated financial statement amounts to conform to current year presentation. There was no effect on net income from this change in presentation.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company s most significant areas of estimation include:

unpaid losses and loss expenses and unpaid losses and loss expenses recoverable;

future policy benefit reserves;

valuation and other-than-temporary impairments of investments;

income taxes;

reinsurance premium estimates; and

goodwill carrying value.

While management believes that the amounts included in the consolidated financial statements reflect the Company s best estimates and assumptions, actual results could differ from these estimates.

(b) Fair Value Measurements

Financial Instruments subject to Fair Value Measurements

Accounting guidance over fair value measurements requires that a fair value measurement reflect the assumptions market participants would use in pricing an asset or liability based on the best information available. Assumptions include the risks inherent in a particular valuation technique (such as a pricing model) and/or the risks inherent in the inputs to the model. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

2. Significant Accounting Policies (Continued)

(b) Fair Value Measurements (Continued)

between market participants at the measurement date (the exit price). Instruments that the Company owns (long positions) are marked to bid prices and instruments that the Company has sold but not yet purchased (short positions) are marked to offer prices. Fair value measurements are not adjusted for transaction costs.

Basis of Fair Value Measurement

Fair value measurements accounting guidance also establishes a fair value hierarchy that prioritizes the inputs to the respective valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). An asset or liability s classification within the fair value hierarchy is based on the lowest level of significant input to its valuation. The three levels of the fair value hierarchy are described further below:

Level 1 Quoted prices in active markets for identical assets or liabilities (unadjusted); no blockage factors.

Level 2 Other observable inputs (quoted prices in markets that are not active or inputs that are observable either directly or indirectly) include quoted prices for similar assets/liabilities (adjusted) other than quoted prices in Level 1; quoted prices in markets that are not active; or other inputs that are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Unobservable inputs reflect the reporting entity s own assumptions about the assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose values are determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Details on assets and liabilities that have been included under the requirements of authoritative guidance on fair value measurements to illustrate the bases for determining the fair values of these items held by the Company are detailed in each respective significant accounting policy section of this note.

Fair values of investments and derivatives are based on published market values if available, estimates of fair values of similar issues, or estimates of fair values provided by independent pricing services and brokers. Fair values of financial instruments for which quoted market prices are not available or for which the company believes current trading conditions represent distressed markets are based on estimates using present value or other valuation techniques. The fair values estimated using such techniques are significantly affected by the assumptions used, including the discount rates and the estimated amounts and timing of future cash flows. In such instances, the derived fair value estimates cannot be substantiated by comparison to independent markets and are not necessarily indicative of the amounts that would be realized in a current market exchange.

(c) Total Investments

Investments Available For Sale

Investments that are considered available for sale (comprised of the Company s fixed maturities, equity securities and short-term investments) are carried at fair value. The fair values for available for sale investments are generally sourced from third parties. The fair value of fixed income securities is based upon quoted market values where available, evaluated bid prices provided by third party pricing services (pricing services) where quoted market values are not available, or by reference to broker or underwriter

2. Significant Accounting Policies (Continued)

(c) Total Investments (Continued)

bid indications where pricing services do not provide coverage for a particular security. To the extent the Company believes current trading conditions represent distressed transactions, the Company may elect to utilize internally generated models. The pricing services use market approaches to valuations using primarily Level 2 inputs in the vast majority of valuations, or some form of discounted cash flow analysis, to obtain investment values for a small percentage of fixed income securities for which they provide a price. Pricing services indicate that they will only produce an estimate of fair value if there is objectively verifiable information available to produce a valuation. Standard inputs to the valuations provided by the pricing services listed in approximate order of priority for use when available include: reported trades, benchmark yields, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data. The pricing services may prioritize inputs differently on any given day for any security, and not all inputs listed are available for use in the evaluation process on any given day for each security evaluation; however, the pricing services also monitor market indicators and industry and economic events. Information of this nature is a trigger to acquire further corroborating market data. When these inputs are not available, they identify buckets of similar securities (allocated by asset class types, sectors, sub-sectors, contractual cash flows/structure, and credit rating characteristics) and apply some form of matrix or other modeled pricing to determine an appropriate security value which represents their best estimate as to what a buyer in the marketplace would pay for a security in a current sale. While the Company receives values for the majority of the investment securities it holds from pricing services, it is ultimately management s responsibility to determine whether the values received and recorded in the financial statements are representative of appropriate fair value measurements. It is common industry practice to utilize pricing services as a source for determining the fair values of investments where the pricing services are able to obtain sufficient market corroborating information to allow them to produce a valuation at a reporting date. In addition, in the majority of cases, although a value may be obtained from a particular pricing service for a security or class of similar securities, these values are corroborated against values provided by other pricing services.

Broker/dealer quotations are used to value fixed maturities where prices are unavailable from pricing services due to factors specific to the security such as limited liquidity, lack of current transactions, or trades only taking place in privately negotiated transactions. These are considered Level 3 valuations, as significant inputs utilized by brokers may be difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification.

Prices provided by independent pricing services and independent broker quotes can vary widely even for the same security. The use of different methodologies and assumptions may have a material effect on the estimated fair value amounts. During periods of market disruption including periods of significantly rising or high interest rates, rapidly widening credit spreads or illiquidity, it may be difficult to value certain of the Company s securities, for example, collateralized loan obligations (CLOs), Alt-A and sub-prime mortgage backed securities, if trading becomes less frequent and/or market data becomes less observable. There may be certain asset classes that were in active markets with significant observable data that become illiquid due to the current financial environment. In such cases, more securities may fall to Level 3, meaning that more subjectivity and management judgment is required with regard to fair value. As such, valuations may include inputs and assumptions that are less observable or require greater estimation as well as valuation methods that are more sophisticated or require greater estimation, thereby resulting in values that may be different than the value at which the investments may be ultimately sold.

The net unrealized gain or loss on investments, net of tax, is included in accumulated other comprehensive income (loss).

Short-term investments include investments due to mature within one year from the date of purchase and are valued using the same external factors and in the same manner as fixed income securities.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

2. Significant Accounting Policies (Continued)

(c) Total Investments (Continued)

Equity securities include investments in open end mutual funds and shares of publicly traded alternative funds. The fair value of equity securities is based upon quoted market values (Level 1), or monthly net asset value statements provided by the investment managers upon which subscriptions and redemptions can be executed (Level 2).

All investment transactions are recorded on a trade date basis. Realized gains and losses on sales of equities and fixed income investments are determined on a first-in, first-out basis. Investment income is recognized when earned and includes interest and dividend income together with the amortization of premium and discount on fixed maturities and short-term investments. Amortization of discounts on fixed maturities includes amortization to expected recovery values for investments that have previously been recorded as other than temporarily impaired. For mortgage-backed securities, and any other holdings for which there is a prepayment risk, prepayment assumptions are evaluated and revised as necessary. Prepayment fees or call premiums that are only payable to the Company when a security is called prior to its maturity are earned when received and reflected in net investment income.

Investments Held to Maturity

Investments classified as held to maturity include securities for which the Company has the ability and intent to hold to maturity and are carried at amortized cost. For details see Note 5, Investments.

Investments In Affiliates

Investments in which the Company has significant influence over the operating and financial policies of the investee are classified as investments in affiliates on the Company s balance sheet and are accounted for under the equity method of accounting. Under this method, the Company records its proportionate share of income or loss from such investments in its results for the period as well as its portion of movements in certain of the investee shareholders equity balances. When financial statements of the affiliate are not available on a timely basis to record the Company s share of income or loss for the same reporting periods as the Company, the most recently available financial statements are used. This lag in reporting is applied consistently.

The Company generally records its alternative and private equity fund affiliates on a one month and three month lag, respectively, and its operating affiliates on a three month lag. Significant influence is generally deemed to exist where the Company has an investment of 20% or more in the common stock of a corporation or an investment of 3% or more in closed end funds, limited partnerships, LLCs or similar investment vehicles. Significant influence is considered for other strategic investments on a case-by-case basis. Investments in affiliates are not subject to fair value measurement guidance as they are not considered to be fair value measured investments under U.S. GAAP. However, impairments associated with investments in affiliates that are deemed to be other-than-temporary are calculated in accordance with fair value measurement guidance and appropriate disclosures included within the financial statements during the period the losses are recorded.

Other Investments

Contained within this asset class are equity interests in investment funds, limited partnerships and unrated tranches of collateralized debt obligations for which the Company does not have sufficient rights or ownership interests to follow the equity method of accounting. The Company accounts for equity securities that do not have readily determinable market values at estimated fair value as it has no significant influence over these entities. Also included within other investments are structured transactions which are carried at amortized cost.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

2. Significant Accounting Policies (Continued)

(c) Total Investments (Continued)

Fair values for other investments, principally other direct equity investments, investment funds and limited partnerships, are primarily based on the net asset value provided by the investment manager, the general partner or the respective entity, recent financial information, available market data and, in certain cases, management judgment may be required. These entities generally carry their trading positions and investments, the majority of which have underlying securities valued using Level 1 or Level 2 inputs, at fair value as determined by their respective investment managers; accordingly, these investments are generally classified as Level 2. Private equity investments are classified as Level 3. The net unrealized gain or loss on investments, net of tax, is included in Accumulated other comprehensive income (loss). Any unrealized loss in value considered by management to be other-than-temporary is charged to income in the period that it is determined.

Overseas deposits include investments in private funds related to Lloyd s syndicates in which the underlying instruments are primarily cash equivalents. The funds themselves do not trade on an exchange and therefore are not included within available for sale securities. Also included in overseas deposits are restricted cash and cash equivalent balances held by Lloyd s syndicates for solvency purposes. Given the restricted nature of these cash balances, they are not included within the cash and cash equivalents line in the balance sheet. Each of these investment types is considered a Level 2 valuation.

The Company historically participated in structured transactions that include cash loans supporting project finance transactions, providing liquidity facility financing to a structured project deal in 2009 and the Company also invested in a payment obligation with an insurance company. These transactions are carried at amortized cost. For further details see Note 3, Fair Value Measurements, and Note 7, Other Investments.

Cash Equivalents

Cash equivalents include fixed interest deposits placed with a maturity of under 90 days when purchased. Bank deposits are not considered to be fair value measurements and as such are not subject to fair value measurement disclosures. Money market funds are classified as Level 1 as these instruments are considered actively traded and values are quoted, however, certificates of deposit are classified as Level 2.

(d) Premiums and Acquisition Costs

Insurance premiums written are recorded in accordance with the terms of the underlying policies. Reinsurance premiums written are recorded at the inception of the policy and are estimated based upon information received from ceding companies and any subsequent differences arising on such estimates are recorded in the period they are determined.

Premiums are earned on a pro-rata basis over the period the coverage is provided. Unearned premiums represent the portion of premiums written applicable to the unexpired terms of policies in force. Net premiums earned are presented after deductions for reinsurance ceded, as applicable.

Mandatory reinstatement premiums are recognized and earned at the time a loss event occurs.

Life and annuity premiums from long duration contracts that transfer significant mortality or morbidity risks are recognized as revenue and earned when due from policyholders. Life and annuity premiums from long duration contracts that do not subject the Company to risks arising from policyholder mortality or morbidity are accounted for as investment contracts and presented within deposit liabilities.

2. Significant Accounting Policies (Continued)

(d) Premiums and Acquisition Costs (Continued)

The Company has periodically written retroactive loss portfolio transfer (LPT) contracts. These contracts are evaluated to determine whether they meet the established criteria for reinsurance accounting, and, if so, at inception, written premiums are fully earned and corresponding losses and loss expense recognized. The contracts can cause significant variances in gross premiums written, net premiums written, net premiums earned, and net incurred losses in the years in which they are written. Reinsurance contracts sold not meeting the established criteria for reinsurance accounting are recorded using the deposit method.

Acquisition costs, which vary with and are directly related to the acquisition of policies, consist primarily of commissions paid to brokers and cedants, and are deferred and amortized over the period that the premiums are earned. Acquisition costs are shown net of commissions earned on reinsurance ceded. Future earned premiums, the anticipated losses and other costs (and in the case of a premium deficiency, investment income) related to those premiums, are also considered in determining the level of acquisition costs to be deferred.

(e) Reinsurance

In the normal course of business, the Company seeks to reduce the potential amount of loss arising from claims events by reinsuring certain levels of risk assumed in various areas of exposure with other insurers or reinsurers. Reinsurance premiums ceded are expensed (and any commissions recorded thereon are earned) on a monthly pro-rata basis over the period the reinsurance coverage is provided. Ceded unearned reinsurance premiums represent the portion of premiums ceded applicable to the unexpired term of policies in force. Mandatory reinstatement premiums ceded are recorded at the time a loss event occurs. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Provisions are made for estimated unrecoverable reinsurance.

(f) Fee Income and Other

Fee income and other includes fees received for insurance and product structuring services provided and is earned over the service period of the contract. Any adjustments to fees earned or the service period are reflected in income in the period when determined.

(g) Other Than-Temporary Impairments (OTTI) of Available for Sale and Held to Maturity Securities

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

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

From April 1, 2009, in instances in which the Company determines that a credit loss exists but the Company does not intend to sell the security, and it is not more likely than not that the Company will be required to sell the security before the anticipated recovery of its remaining amortized cost basis, the OTTI is separated into (1) the amount of the total impairment related to the credit loss and (2) the amount of the total impairment related to all other factors (i.e. the noncredit portion). The amount of the total OTTI related to the credit loss is recognized in earnings and the amount of the total OTTI related to all other factors is recognized in accumulated other comprehensive loss. The total OTTI is presented in the income statement with an offset for the amount of the total OTTI that is recognized in accumulated other comprehensive loss. Absent the intent or requirement to sell a security, if a credit loss does not exist, any impairment is considered to be temporary.

2. Significant Accounting Policies (Continued)

(g) Other-Than-Temporary Impairments (OTTI) of Available for Sale and Held to Maturity Securities (Continued)

The noncredit portion of any OTTI losses on securities classified as available for sale is recorded as a component of other comprehensive income with an offsetting adjustment to the carrying value of the security. The fair value adjustment could increase or decrease the carrying value of the security. The noncredit portion of any OTTI losses recognized in accumulated other comprehensive loss for debt securities classified as held to maturity would be accreted over the remaining life of the debt security (in a pro rata manner based on the amount of actual cash flows received as a percentage of total estimated cash flows) as an increase in the carrying value of the security until the security is sold, the security matures, or there is an additional OTTI that is recognized in earnings.

In periods subsequent to the recognition of an OTTI loss, the other-than-temporarily impaired debt security is accounted for as if it had been purchased on the measurement date of the OTTI at an amount equal to the previous amortized cost basis less the credit-related OTTI recognized in earnings. For debt securities for which credit-related OTTI is recognized in earnings, the difference between the new cost basis and the cash flows expected to be collected is accreted into interest income over the remaining life of the security in a prospective manner based on the estimated amount and timing of future estimated cash flows.

With respect to securities where the decline in value is determined to be temporary and the security s amortized cost is not written down, a subsequent decision may be made to sell that security and realize a loss. Subsequent decisions on security sales are made within the context of overall risk monitoring, changing information, market conditions generally and assessing value relative to other comparable securities. Day-to-day management of the Company s investment portfolio is outsourced to third party investment manager service providers. While these investment manager service providers may, at a given point in time, believe that the preferred course of action is to hold securities with unrealized losses that are considered temporary until such losses are recovered, the dynamic nature of the portfolio management may result in a subsequent decision to sell the security and realize the loss, based upon a change in market and other factors described above. The Company believes that subsequent decisions to sell such securities are consistent with the classification of the Company s portfolio as available for sale.

There are risks and uncertainties associated with determining whether declines in the fair value of investments are other-than-temporary. These include subsequent significant changes in general economic conditions as well as specific business conditions affecting particular issuers, the Company s liability profile, subjective assessment of issue-specific factors (seniority of claims, collateral value, etc.), future financial market effects, stability of foreign governments and economies, future rating agency actions and significant disclosure of accounting, fraud or corporate governance issues that may adversely affect certain investments. In addition, significant assumptions and management judgment are involved in determining if the decline is other-than-temporary. If management determines that a decline in fair value is temporary, then a security s value is not written down at that time. However, there are potential effects upon the Company s future earnings and financial position should management later conclude that some of the current declines in the fair value of the investments are other-than-temporary declines. For further details on the factors considered in evaluation of OTTI see Note 5, Investments.

2. Significant Accounting Policies (Continued)

(h) Derivative Instruments

The Company recognizes all derivatives as either assets or liabilities in the balance sheet and measures those instruments at fair value. The changes in fair value of derivatives are shown in the consolidated statement of income as net realized and unrealized gains and losses on derivative instruments unless the derivatives are designated as hedging instruments. The accounting for derivatives which are designated as hedging instruments is discussed below. Changes in fair value of derivatives may create volatility in the Company s results of operations from period to period. Amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) are offset against net fair value amounts recognized in the consolidated balance sheet for derivative instruments executed with the same counterparty under the same netting arrangement.

Derivative contracts can be exchange-traded or over-the-counter (OTC). Exchange-traded derivatives (futures and options) typically fall within Level 1 of the fair value hierarchy depending on whether they are deemed to be actively traded or not. OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources where an understanding of the inputs utilized in arriving at the valuations is obtained. Where models are used, the selection of a particular model to value an OTC derivative depends upon the contractual terms and specific risks inherent in the instrument as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, interest rate swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment. Such instruments comprise the majority of derivatives held by the Company and are typically classified within Level 2 of the fair value hierarchy.

Certain OTC derivatives trade in less liquid markets with limited pricing information, or required model inputs which are not directly market corroborated, which causes the determination of fair value for these derivatives to be inherently more subjective. Accordingly, such derivatives are classified within Level 3 of the fair value hierarchy. The valuations of less standard or liquid OTC derivatives are typically based on Level 1 and/or Level 2 inputs that can be observed in the market, as well as unobservable Level 3 inputs. Level 1 and Level 2 inputs are regularly updated to reflect observable market changes. Level 3 inputs are only changed when corroborated by evidence such as similar market transactions, pricing services and/or broker or dealer quotations. The Company conducts its non-hedging derivatives activities in three main areas: investment related derivatives, credit derivatives and other non-investment related derivatives; until early 2009, it also utilized weather and energy derivatives.

The Company uses derivative instruments, primarily interest rate swaps, to manage the interest rate exposure associated with certain assets and liabilities. These derivatives are recorded at fair value. On the date the derivative contract is entered into, the Company may designate the derivative as a hedge of the fair value of a recognized asset or liability (fair value hedge); a hedge of the variability in cash flows of a forecasted transaction or of amounts to be received or paid related to a recognized asset or liability (cash flow hedge); or a hedge of a net investment in a foreign operation; or the Company may not designate any hedging relationship for a derivative contract. In addition, the Company previously wrote a number of resettable strike swaps contracts relating to an absolute return index and diversified basket of funds, all of which are recorded within Investment Related Derivatives Financial Market Exposures. These resettable strike swaps have all expired at December 31, 2011.

2. Significant Accounting Policies (Continued)

(h) Derivative Instruments (Continued)

Fair Value Hedges

Changes in the fair value of a derivative that is designated and qualifies as a fair value hedge, along with the changes in the fair value of the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings (through net realized and unrealized gains and losses on derivative instruments) with any differences between the net change in fair value of the derivative and the hedged item representing the hedge ineffectiveness. Periodic derivative net coupon settlements are recorded in net investment income with the exception of hedges of Company issued debt, which are recorded in interest expense. The Company may designate fair value hedging relationships where interest rate swaps are used to hedge the changes in fair value of certain fixed rate liabilities and fixed maturity securities due to changes in the designated benchmark interest rate.

Cash Flow Hedges

Changes in the fair value of a derivative that is designated and qualifies as a cash flow hedge are recorded in accumulated other comprehensive income (AOCI) and are reclassified into earnings when the variability of the cash flow of the hedged item impacts earnings. Gains and losses on derivative contracts that are reclassified from AOCI to current period earnings are included in the line item in the consolidated statements of operations in which the cash flows of the hedged item are recorded. Any hedge ineffectiveness is recorded immediately in current period earnings as net realized and unrealized gains and losses on derivative instruments. Periodic derivative net coupon settlements are recorded in net investment income. The Company may designate cash flow hedging relationships where interest rate swaps are used to mitigate interest rate risk associated with anticipated issuances of debt or other forecasted transactions.

Hedges of the Net Investment in a Foreign Operation

Changes in fair value of a derivative used as a hedge of a net investment in a foreign operation, to the extent effective as a hedge, are recorded in the foreign currency translation adjustments account within AOCI. Cumulative changes in fair value recorded in AOCI are reclassified into earnings upon the sale or complete or substantially complete liquidation of the foreign entity. Any hedge ineffectiveness is recorded immediately in current period earnings as net realized and unrealized gains and losses on derivative instruments.

Hedge Documentation and Effectiveness Testing

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated changes in value or cash flow of the hedged item. At hedge inception, the Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking each hedge transaction. The documentation process includes linking derivatives that are designated as fair value, cash flow, or net investment hedges to specific assets or liabilities on the balance sheet or to specific forecasted transactions. The Company also formally assesses, both at the hedge s inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. In addition, certain hedging relationships are considered highly effective if the changes in the fair value or discounted cash flows of the hedging instrument are within a ratio of 80-125% of the inverse changes in the fair value or discounted cash flows of the hedged item. Hedge ineffectiveness is measured using qualitative and quantitative methods. Qualitative methods may include comparison of critical terms of the derivative to the hedged item. Depending on the hedging strategy, quantitative methods may include the Change in Variable Cash Flows Method, the Change in Fair Value Method, the Hypothetical Derivative Method and the Dollar Offset Method.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

2. Significant Accounting Policies (Continued)

(h) Derivative Instruments (Continued)

Discontinuance of Hedge Accounting

The Company discontinues hedge accounting prospectively when it is determined that the derivative is no longer highly effective in offsetting changes in the fair value or cash flows of a hedged item; the derivative is dedesignated as a hedging instrument; or the derivative expires or is sold, terminated or exercised. When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective fair-value hedge, the derivative continues to be carried at fair value on the balance sheet with changes in its fair value recognized in current period earnings through net realized and unrealized gains and losses on derivative instruments. When hedge accounting is discontinued because the Company becomes aware that it is not probable that the forecasted transaction will occur, the derivative continues to be carried on the balance sheet at its fair value, and gains and losses that were accumulated in AOCI are recognized immediately in earnings.

(i) Cash Equivalents

Cash equivalents include fixed interest deposits placed with a maturity of under 90 days when purchased. Bank deposits are not considered to be fair value measurements and as such are not subject to the authoritative guidance on fair value measurement disclosures. Money market funds are classified as Level 1 as these instruments are considered actively traded; however, certificates of deposit are classified as Level 2.

(j) Foreign Currency Translation

Assets and liabilities of foreign operations whose functional currency is not the U.S. dollar are translated at prevailing year end exchange rates. Revenue and expenses of such foreign operations are translated at average exchange rates during the year. The net effect of the translation adjustments for foreign operations, net of applicable deferred income taxes, as well as any gains or losses on intercompany balances for which settlement is not planned or anticipated in the foreseeable future, are included in accumulated other comprehensive income (loss).

Monetary assets and liabilities denominated in currencies other than the functional currency of the applicable entity are revalued at the exchange rate in effect at the balance sheet date and revenues and expenses are translated at the exchange rate on the date the transaction occurs with the resulting foreign exchange gains and losses on settlement or revaluation recognized in income.

(k) Goodwill and Other Intangible Assets

The Company has recorded goodwill in connection with various acquisitions in prior years. Goodwill represents the excess of the purchase price over the fair value of net assets acquired. In accordance with accounting guidance over goodwill and other intangible assets, the Company tests goodwill for potential impairment annually as of June 30 and between annual tests if an event occurs or circumstances change that may indicate that potential exists for the fair value of a reporting unit to be reduced to a level below its carrying amount. For further details on the factors considered in the goodwill impairment evaluation see Note 8, Goodwill and Other Intangible Assets.

The Company s other intangible assets consist of both amortizable and non-amortizable intangible assets. The Company s amortizable intangible assets consist primarily of acquired customer relationships and acquired software. All of the Company s amortizable intangible assets are carried at net book value and are amortized over their estimated useful lives. The amortization periods approximate the periods over which the Company expects to generate future net cash inflows from the use of these assets. Accordingly, customer relationships are amortized over a useful life of 10 years and acquired software is amortized over a useful life of 5 years. The Company s policy is to amortize intangibles on a straight-line basis.

2. Significant Accounting Policies (Continued)

(k) Goodwill and Other Intangible Assets (Continued)

All of the Company s amortizable intangible assets, as well as other amortizable or depreciable long-lived assets such as premises and equipment, are subject to impairment testing in accordance with authoritative guidance for the impairment or disposal of long-lived assets when events or conditions indicate that the carrying value of an asset may not be fully recoverable from future cash flows. A test for recoverability is done by comparing the asset s carrying value to the sum of the undiscounted future net cash inflows expected to be generated from the use of the asset over its remaining useful life. In accordance with the authoritative guidance on property, plant and equipment under GAAP, impairment exists if the sum of the undiscounted expected future net cash inflows is less than the carrying amount of the asset. Impairment would result in a write-down of the asset to its estimated fair value. The estimated fair values of these assets are based on the discounted present value of the stream of future net cash inflows expected to be derived over their remaining useful lives. If an impairment write-down is recorded, the remaining useful life of the asset will be evaluated to determine whether revision of the remaining amortization or depreciation period is appropriate.

The Company s indefinite lived intangible assets consist primarily of acquired insurance and reinsurance licenses. These assets are deemed to have indefinite useful lives and are therefore not subject to amortization. In accordance with the authoritative guidance on intangibles and goodwill and other assets under GAAP, all of the Company s non-amortized intangible assets are subject to a test for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. Pursuant to the authoritative guidance, if the carrying value of a non-amortized intangible asset is in excess of its fair value, the asset must be written down to its fair value through the recognition of an impairment charge to earnings.

(l) Losses and Loss Expenses

Unpaid losses and loss expenses include reserves for reported unpaid losses and loss expenses and for losses incurred but not reported. The reserve for reported unpaid losses and loss expenses for the Company s property and casualty operations is established by management based on claims reported from insureds or amounts reported from ceding companies, and represent the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company.

The reserve for losses incurred but not reported is estimated by management based on loss development patterns determined by reference to the Company s underwriting practices, the policy form, type of program and historical experience. The Company s actuaries employ a variety of generally accepted methodologies to determine estimated ultimate loss reserves, including the Bornhuetter-Ferguson incurred loss method and frequency and severity approaches.

Certain workers compensation and U.K. motor liability claims liabilities are considered fixed and determinable and are subject to tabular reserving. Reserves associated with these liabilities are discounted.

Management believes that the reserves for unpaid losses and loss expenses are sufficient to cover losses that fall within coverages assumed by the Company. However, there can be no assurance that losses will not exceed the Company s total reserves. The methodology of estimating loss reserves is periodically reviewed to ensure that the assumptions made continue to be appropriate and any adjustments resulting from such reviews are reflected in income of the year in which the adjustments are made.

(m) Deposit liabilities

Contracts entered into by the Company which are not deemed to transfer significant underwriting and/or timing risk are accounted for as deposits, whereby liabilities are initially recorded at an amount equal to the assets received. The Company uses a portfolio rate of return of equivalent duration to the liabilities in determining risk transfer. An initial accretion rate is established based on actuarial estimates whereby the deposit liability is increased to the estimated amount payable over the term of the contract.

The deposit accretion rate is the rate of return required to fund expected future payment obligations (this is equivalent to the best estimate of future cash flows), which are determined actuarially based upon the nature of the underlying indemnifiable losses. Accretion of the liability is recorded as interest expense.

2. Significant Accounting Policies (Continued)

(m) Deposit liabilities (Continued)

The Company periodically reassesses the estimated ultimate liability. Any changes to this liability are reflected as adjustments to interest expense to reflect the cumulative effect of the period the contract has been in force, and by an adjustment to the future accretion rate of the liability over the remaining estimated contract term.

(n) Future policy benefit reserves

The Company estimates the present value of future policy benefits related to long duration contracts using assumptions for investment yields, mortality, and expenses, including a provision for adverse deviation.

The assumptions used to determine future policy benefit reserves are best estimate assumptions that are determined at the inception of the contracts and are locked-in throughout the life of the contract unless a premium deficiency develops. As the experience on the contracts emerges, the assumptions are reviewed. If such review would produce reserves in excess of those currently held then the lock-in assumptions will be revised and a claim and policy benefit is recognized at that time.

Certain life insurance and annuity contracts provide the holder with a guarantee that the benefit received upon death will be no less than a minimum prescribed amount. The contracts are accounted for in accordance with the authoritative guidance on Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Separate Accounts, which requires that the best estimate of future experience be combined with actual experience to determine the benefit ratio used to calculate the policy benefit reserve.

(o) Income Taxes

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The deferral of tax losses is evaluated based upon management s estimates of the future profitability of the Company s taxable entities based on current forecasts and the period for which losses may be carried forward. A valuation allowance is established for any portion of a deferred tax asset that management believes will not be realized. The Company continues to evaluate income generated in future periods by its subsidiaries in different jurisdictions in determining the recoverability of its deferred tax asset. If it is determined that future income generated by these subsidiaries is insufficient to cause the realization of the net operating losses within a reasonable period, a valuation allowance is established at that time.

2. Significant Accounting Policies (Continued)

(p) Stock Plans

The Company adopted authoritative guidance on the fair value recognition provisions for accounting for stock-based compensation, under the prospective method for options granted subsequent to January 1, 2003. Prior to 2003, the Company accounted for options under the disclosure-only provisions of the guidance and no stock-based employee compensation cost was included in net income as all options granted had an exercise price equal to the market value of the Company s ordinary shares on the date of the grant. At December 31, 2011, the Company had several stock based Performance Incentive Programs, which are described more fully in Item 8, Note 18, Share Capital. Stock-based compensation issued under these plans generally have a life of not longer than ten years and vest as set forth at the time of grant. Awards currently vest annually over three or four years from the date of grant. The Company recognizes compensation costs for stock-based awards on a straight-line basis over the requisite service period (usually the vesting period) for each award.

Share-based payments to employees, including grants of employee stock options, are recognized in the financial statements over the vesting period based on their grant date fair values.

Authoritative guidance requires that compensation costs be recognized for unvested stock-based compensation awards over the period through the date that the employee is no longer required to provide future services to earn the award, rather than over the explicit service period. Accordingly, the Company follows a policy of recognizing compensation cost to coincide with the date that the employee is eligible to retire, rather than the actual retirement date, for all stock based compensation granted.

(q) Per Share Data

Basic earnings per ordinary share is based on weighted average ordinary shares outstanding and excludes any dilutive effects of options and convertible securities. Diluted earnings per ordinary share assumes the exercise of all dilutive stock options and conversion of convertible securities where the contingency for conversion has occurred or been satisfied.

(r) Recent Accounting Pronouncements

In January 2010, the FASB issued an accounting standards update on Improving Disclosures about Fair Value Measurements. The provisions of this authoritative guidance require new disclosure about recurring and nonrecurring fair value measurements, including significant transfers into and out of Level 1 and Level 2 fair value measurements and information on purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair value measurements. This guidance was effective for the Company beginning on January 1, 2010, except for the Level 3 reconciliation disclosures, which were effective for annual periods beginning after December 15, 2010. See Note 3, Fair Value Measurements, for changes to Level 3 reconciliation disclosure. This standard affects disclosure only and, accordingly, did not have an impact on the Company s financial condition or results of operations.

In July 2010, the FASB amended the general accounting principles for receivables as they relate to the disclosures about the credit quality of financing receivables and the allowance for credit losses. This amendment requires additional disclosures that provide a greater level of disaggregated information about the credit quality of financing receivables and the allowance for credit losses. It also requires the disclosure of credit quality indicators, past due information, and modifications of financing receivables. The new disclosures are required for interim and annual periods ending after December 15, 2010, although the disclosures of reporting period activity (i.e., allowance roll-forward and modification disclosures) were required for interim and annual periods beginning after December 15, 2010. This standard affects disclosures only and, accordingly, did not have an impact on the Company s financial condition or results of operations. During the fourth quarter of 2010, the Company recorded a provision of $9.9 million related to two structured loan investments. This provision was $9.2 million at December 31, 2011. The Company holds investments in six separate structured loans with aggregate net carrying values of $40.5 million and $42.3 million at December 31, 2011 and December 31, 2010, respectively. In addition, the Company had gross reinsurance balances receivable and reinsurance recoverables on unpaid losses and loss expense of $3.9 billion and $3.8 billion at December 31, 2011 and 2010, respectively, against which an allowance of $99.2 million and $121.9 million was recorded at December 31, 2011 and 2010, respectively. There were no charge offs recorded during the year.

2. Significant Accounting Policies (Continued)

(r) Recent Accounting Pronouncements (Continued)

In October 2010, the FASB issued an accounting standards update to address disparities in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. The provisions of the guidance specify that incremental direct costs of contract acquisition and certain costs related directly to the acquisition activities incurred in the acquisition of new or renewal contracts should be capitalized in accordance with the amendments in the updated guidance. Costs directly related to those activities include only the portion of an employee s total compensation (excluding any compensation that is capitalized as incremental direct costs of contract acquisition) and payroll-related fringe benefits related directly to time spent performing those activities for actual acquired contracts, and other costs related directly to those activities that would not have been incurred if the contract had not been acquired. Administrative costs, rent, depreciation, occupancy, equipment and all other general overhead costs are considered indirect costs and should be charged to expense as incurred. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. The Company will adopt this guidance on a retrospective basis on January 1, 2012, and expects the impact to result in a reduction of opening retained earnings by approximately $20 million.

In May 2011, the FASB issued further updated accounting guidance to amend existing requirements for fair value measurements and disclosures. The guidance expands the disclosure requirements around fair value measurements categorized in Level 3 of the fair value hierarchy, requiring quantitative information to be disclosed related to (1) the valuation processes used, (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, and (3) use of a nonfinancial asset in a way that differs from the asset s highest and best use. The guidance requires disclosure of the level in the fair value hierarchy of items that are not measured at fair value but whose fair value must be disclosed. It also clarifies and expands upon existing requirements for fair value measurements of financial assets and liabilities as well as instruments classified in shareholders equity. This guidance is effective for interim and annual periods beginning after December 15, 2011 and early application is prohibited. The Company will adopt this guidance from January 1, 2012. While the adoption will result in additional disclosures in the area of fair values, it will not impact the Company s consolidated financial position or results of operations.

In June 2011, the FASB issued an accounting standards update on the presentation of comprehensive income in financial statements. This guidance will allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Under both options, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income and a total amount for comprehensive income. This guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders equity. The guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance must be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, except for the provision requiring entities to present components of reclassifications of other comprehensive income on the face of the income statement, which the FASB voted to defer indefinitely during the fourth quarter of 2011. The Company will adopt this standard on a retrospective basis on January 1, 2012. This guidance affects disclosure only and will not have an impact on the Company s financial condition or results of operations.

In September 2011, the FASB issued an accounting standards update to simplify how entities test goodwill for impairment, by allowing an entity the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting entity is less than its carrying amount, as a basis for determining whether it is necessary to perform the two-step goodwill impairment test required in FASB Accounting Standards Codification Topic 350. After assessing the circumstances that should be considered in making the qualitative assessment, if an entity determines that the fair value of a reporting unit as compared to its carrying value meets the threshold, then performing the two-step impairment step is unnecessary. In other circumstances, performance of the two-step test is required. The guidance also eliminates the option for an entity to carry forward its detailed calculation of a reporting unit s fair value in certain situations, as previously permitted. The amendments do not change the current guidance for testing other indefinite-lived intangible assets for impairment. The new guidance is effective for annual and interim goodwill tests performed for fiscal years beginning after December 15, 2011. The Company will adopt this guidance from January 1, 2012. It will not have an impact on the Company s consolidated financial condition or results of operations. See Note 8, Goodwill and Other Intangible Assets, for further information regarding goodwill.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

3. Fair Value Measurements

(a) Fair Value Summary

The following tables set forth the Company s assets and liabilities that were accounted for at fair value as of December 31, 2011 and December 31, 2010 by level within the fair value hierarchy (for further information, see Note 2 (b), Significant Accounting Policies Fair Value Measurements :

December 31, 2011 *(U.S. dollars in thousands)*	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Collateral and Counterparty Netting**	**Balance at December 31, 2011**
Assets					
U.S. Government and Government-Related/Supported	$	$ 1,990,983	$	$	$ 1,990,983
Corporate (1)		10,438,697	23,818		10,462,515
Residential mortgage-backed securities Agency		5,347,365	32,041		5,379,406
Residential mortgage-backed securities Non-Agency		641,815			641,815
Commercial mortgage-backed securities		974,835			974,835
Collateralized debt obligations		7,751	650,851		658,602
Other asset-backed securities		969,804	16,552		986,356
U.S. States and political subdivisions of the States		1,797,378			1,797,378
Non-U.S. Sovereign Government, Supranational and Government-Related		3,298,135			3,298,135
Total fixed maturities, at fair value	$	$ 25,466,763	$ 723,262	$	$ 26,190,025
Equity securities, at fair value (2)	239,175	229,022			468,197
Short-term investments, at fair value (1) (3)		359,063			359,063
Total investments available for sale	$ 239,175	$ 26,054,848	$ 723,262	$	$ 27,017,285
Cash equivalents (4)	1,686,101	1,068,264			2,754,365
Other investments (5)		547,598	113,959		661,557
Other assets (6)(7)		143,622		(77,888)	65,734
Total assets accounted for at fair value	$ 1,925,276	$ 27,814,332	$ 837,221	$ (77,888)	$ 30,498,941
Liabilities					
Financial instruments sold, but not yet purchased (8)	$	$ 20,844	$	$	$ 20,844
Other liabilities (6)(7)		16,871	42,644	(809)	58,706
Total liabilities accounted for at fair value	$	$ 37,715	$ 42,644	$ (809)	$ 79,550

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

3. Fair Value Measurements (Continued)

(a) Fair Value Summary (Continued)

December 31, 2010 *(U.S. dollars in thousands)*	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Collateral and Counterparty Netting**	**Balance at December 31, 2010**
Assets					
U.S. Government and Government-Related/Supported	$	$ 2,565,444	$	$	$ 2,565,444
Corporate (1)		10,932,105	36,866		10,968,971
Residential mortgage-backed securities Agency		5,173,456	30,255		5,203,711
Residential mortgage-backed securities Non-Agency		1,016,859	4,964		1,021,823
Commercial mortgage-backed securities		1,170,884	1,623		1,172,507
Collateralized debt obligations		12,566	721,572		734,138
Other asset-backed securities		935,882	24,650		960,532
U.S. States and political subdivisions of the States		1,360,456			1,360,456
Non-U.S. Sovereign Government, Supranational and Government-Related		3,150,856	3,667		3,154,523
Total fixed maturities, at fair value	$	$ 26,318,508	$ 823,597	$	$ 27,142,105
Equity securities, at fair value (2)	71,284	13,483			84,767
Short-term investments, at fair value (1) (3)		450,681			450,681
Total investments available for sale	$ 71,284	$ 26,782,672	$ 823,597	$	$ 27,677,553
Cash equivalents (4)	1,358,619	540,646			1,899,265
Other investments (5)		432,166	133,717		565,883
Other assets (6)(7)		108,056	7,882	(22,995)	92,943
Total assets accounted for at fair value	$ 1,429,903	$ 27,863,540	$ 965,196	$ (22,995)	$ 30,235,644
Liabilities					
Financial instruments sold, but not yet purchased (8)	$ 256	$ 21,270	$	$	$ 21,526
Other liabilities (6)(7)		13,591	47,077		60,668
Total liabilities accounted for at fair value	$ 256	$ 34,861	$ 47,077	$	$ 82,194

Notes:

(1) Included within Corporate are certain medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes, which are in a gross unrealized loss position, had a fair value of $266.0 million and $454.8 million and an amortized cost of $297.7 million and $504.6 million at December 31, 2011 and 2010, respectively. These notes allow the investor to participate in cash flows of the underlying bonds, including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(2) Included within equity securities are investments fixed income funds of $91.6 million and nil at December 31, 2011 and 2010, respectively.

(3) Short-term investments consist primarily of Corporate securities and U.S. Government and Government-Related/Supported securities.

(4) Cash equivalents balances subject to fair value measurement include certificates of deposit and money market funds. Operating cash balances are not subject to fair value measurement guidance.

(5) The Other investments balance excludes certain structured transactions, including certain investments in project finance transactions, a payment obligation and liquidity financing provided to a structured credit vehicle as a part of a third party medium term note facility. These investments are carried at amortized cost that totaled $323.7 million and $327.7 million at December 31, 2011 and 2010, respectively.

(6) Other assets and other liabilities include derivative instruments.

(7) The derivative balances included in each category above are reported on a gross basis by level with a netting adjustment presented separately in the Collateral and Counterparty Netting column. The Company often enters into different types of derivative contracts with a single counterparty and these contracts are covered under a netting agreement. In addition, the Company held net cash collateral related to derivative positions of approximately $77.1 million and $23.0 million at December 31, 2011 and 2010, respectively. This balance is included within cash and cash equivalents and the corresponding liability to return the collateral has been offset against the derivative positions within the balance sheet as appropriate under the netting agreement. The fair values of the individual derivative contracts are reported gross in their respective levels based on the fair value hierarchy.

(8) Financial instruments sold, but not yet purchased represent short sales and are included within Payable for investments purchased on the balance sheet.

3. Fair Value Measurements (Continued)

(b) Level 3 Gains and Losses

The tables below present additional information about assets and liabilities measured at fair value on a recurring basis and for which Level 3 inputs were utilized to determine fair value. The tables reflect gains and losses for the twelve month periods ended December 31, 2011 and 2010 for all financial assets and liabilities categorized as Level 3 at December 31, 2011 and 2010, respectively. The tables do not include gains or losses that were reported in Level 3 in prior periods for assets that were transferred out of Level 3 prior to December 31, 2011 and 2010. Gains and losses for assets and liabilities classified within Level 3 in the table below may include changes in fair value that are attributable to both observable inputs (Levels 1 and 2) and unobservable inputs (Level 3). Further, it should be noted that the following tables do not take into consideration the effect of offsetting Level 1 and 2 financial instruments entered into by the Company that are either economically hedged by certain exposures to the Level 3 positions or that hedge the exposures in Level 3 positions.

In general, Level 3 assets include securities for which values were obtained from brokers where either significant inputs were utilized in determining the value that were difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification. Transfers into or out of Level 3 primarily arise as a result of the valuations utilized by the Company changing between either those provided by independent pricing services that do not contain significant observable inputs, or other valuations sourced from brokers which are considered Level 3.

There were no transfers between Level 1 and Level 2 during the twelve month periods ended December 31, 2011 and 2010.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

3. Fair Value Measurements (Continued)

(b) Level 3 Gains and Losses (Continued)

	Level 3 Assets and Liabilities Year Ended December 31, 2011				
(U.S. dollars in thousands)	Corporate	Residential mortgage-backed securities Agency	Residential mortgage-backed securities Non Agency	Commercial mortgage-backed securities	Collateralized debt obligations
Balance, beginning of period	$ 36,866	$ 30,255	$ 4,964	$ 1,623	$ 721,572
Realized gains (losses)	(276)	(11)			(3,458)
Movement in unrealized gains (losses)	92	(145)			2,404
Purchases and issuances	14,840	6,176			2,379
Sales and settlements	(10,049)	(4,186)			(68,165)
Transfers into Level 3	2,105	2,655			1,886
Transfers out of Level 3	(19,760)	(2,703)	(4,964)	(1,623)	(5,767)
Fixed maturities to short-term investments classification change					
Balance, end of period	$ 23,818	$ 32,041	$	$	$ 650,851
Movement in total gains (losses) above relating to instruments still held at the reporting date	$ 92	$ (156)	$	$	$ (6,431)

	Level 3 Assets and Liabilities Year Ended December 31, 2011 (Continued)				
(U.S. dollars in thousands)	Other asset backed securities	Non-U.S. Sovereign Government and Supranationals and Government-Related	Short-term Investments	Other investments	Derivative Contracts - Net
Balance, beginning of period	$ 24,650	$ 3,667	$	$ 133,717	$ (39,195)
Realized gains (losses)	(849)			11,592	
Movement in unrealized gains (losses)	6,896			14,108	(3,173)
Purchases and issuances				12,177	
Sales and settlements	(9,114)			(57,635)	(276)
Transfers into Level 3					
Transfers out of Level 3	(5,031)	(3,667)			

Fixed maturities to short-term investments classification change					
Balance, end of period	$ 16,552	$	$	$ 113,959	$ (42,644)
Movement in total gains (losses) above relating to instruments still held at the reporting date	$ 12,334	$	$	$ 23,391	$ (3,173)

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

3. Fair Value Measurements (Continued)

(b) Level 3 Gains and Losses (Continued)

	Level 3 Assets and Liabilities Year Ended December 31, 2010				
(U.S. dollars in thousands)	Corporate	Residential mortgage-backed securities Agency	Residential mortgage-backed securities Non Agency	Commercial mortgage-backed securities	Collateralized debt obligations
Balance, beginning of period	$ 10,311	$ 7,894	$ 42,190	$ 2,755	$ 197,149
Realized gains (losses)	(7,257)	(360)	(1,452)	(908)	(28,253)
Movement in unrealized gains (losses)	1,748	(74)	306	1,062	120,932
Purchases and issuances	20,328	30,689			
Sales and settlements	(2,164)		(2,226)	(685)	(7,525)
Transfers into Level 3	14,749		5,601		471,211
Transfers out of Level 3	(849)	(7,894)	(39,455)		(59)
Fixed maturities to short-term investments classification change				(601)	(31,883)
Balance, end of period	$ 36,866	$ 30,255	$ 4,964	$ 1,623	$ 721,572
Movement in total gains (losses) above relating to instruments still held at the reporting date	$ 1,964	$ (74)	$ (28)	$ 223	$ 117,764

	Level 3 Assets and Liabilities Year Ended December 31, 2010 (Continued)				
(U.S. dollars in thousands)	Other asset backed securities	Non-U.S. Sovereign Government and Supranationals and Government-Related	Short-term Investments	Other investments	Derivative Contracts - Net
Balance, beginning of period	$ 38,179	$ 3,217	$	$ 75,584	$ 100,515
Realized gains (losses)	(18,107)			3,677	874
Movement in unrealized gains (losses)	14,685	34		14,461	57,688
Purchases and issuances	4,356			15,443	(198,272)
Sales and settlements	(1,504)			(26,180)	
Transfers into Level 3	1,355	416		18,248	
Transfers out of Level 3	(14,314)				

Fixed maturities to short-term investments classification change				32,484	
Balance, end of period	$ 24,650	$ 3,667	$	$ 133,717	$ (39,195)
Movement in total gains (losses) above relating to instruments still held at the reporting date	$ 8,747	$ 34	$	$ 14,286	$ 57,688

3. Fair Value Measurements (Continued)

(c) Fixed maturities and short-term investments

During the year ended December 31, 2010, certain collateralized debt obligations (CDOs) that were previously classified as Level 2 due to sufficient market data being available to allow a price to be determined and provided by third party pricing vendors, were transferred to Level 3 because third party vendor prices were no longer believed to be the most appropriate pricing source. Broker quotes, for which sufficient information regarding the specific inputs utilized by the broker was not available to support a Level 2 classification, are the primary source of the valuations for these CDO securities.

The remainder of the Level 3 assets relate to private equity investments where the nature of the underlying assets held by the investee include positions such as private business ventures and are such that significant Level 3 inputs are utilized in the valuation, and certain derivative positions.

(d) Other investments

Included within the Other investments component of the Company s Level 3 valuations are private investments and alternative fund investments where the Company is not deemed to have significant influence over the investee. The fair value of these investments is based upon net asset values received from the investment manager or general partner of the respective entity. The nature of the underlying investments held by the investee which form the basis of the net asset value include assets such as private business ventures and are such that significant Level 3 inputs are utilized in the determination of the individual underlying holding values and, accordingly, the fair value of the Company s investment in each entity is classified within Level 3. The Company also incorporates factors such as the most recent financial information received, the values at which capital transactions with the investee take place, and management s judgment regarding whether any adjustments should be made to the net asset value in recording the fair value of each position. Investments in alternative funds included in Other investments utilize strategies including arbitrage, directional, event driven and multi-style. These funds potentially have lockup and gate provisions which may limit redemption liquidity. See Note 7, Other Investments, for further details.

(e) Derivative instruments

Derivative instruments classified within Level 3 include guaranteed minimum income benefits (GMIB) embedded within a certain reinsurance contract and credit derivatives sold providing protection on senior tranches of structured finance transactions where the value is obtained directly from the investment bank counterparty and sufficient information regarding the inputs utilized in such valuation was not obtained to support a Level 2 classification. The majority of inputs utilized in the valuations of these types of derivative contracts are considered Level 1 or Level 2; however, each valuation includes at least one Level 3 input that was significant to the valuation and, accordingly, the values are disclosed within Level 3. In addition, see Note 2(h), Significant Accounting Policies, for a general discussion of types of assets and liabilities that are classified within Level 3 of the fair value hierarchy as well as the Company s valuation policies for such instruments.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

3. Fair Value Measurements (Continued)

(f) Non-recurring Fair Value Measurement

During the year ended December 31, 2011, the Company recorded a non-recurring fair value measurement relating to a goodwill impairment charge. This is a Level 3 fair value measurement as it reflected the Company s own assumptions about the assumptions that market participants would use in valuing the carried goodwill and was determined using a combination of discounted cash flow analysis and market value multiple based methodologies. See Note 8, Goodwill and Other Intangible Assets for further information.

(g) Financial Instruments Not Carried at Fair Value

Authoritative guidance over disclosures about the fair value of financial instruments requires additional disclosure of fair value information for financial instruments not carried at fair value in both interim and annual reporting periods. Certain financial instruments, particularly insurance contracts, are excluded from these fair value disclosure requirements. The carrying values of cash and cash equivalents, accrued investment income, net receivable from investments sold, other assets, net payable for investments purchased, other liabilities and other financial instruments not included below approximated their fair values. The following table includes financial instruments for which the carrying value differs from the estimated fair values at December 31, 2011 and 2010:

	2011		2010	
(U.S. dollars in thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Fixed maturities, held to maturity	$ 2,668,978	$ 2,895,668	$ 2,728,335	$ 2,742,626
Other investments structured transactions	323,705	297,124	327,686	317,524
Financial Assets	$ 2,992,683	$ 3,192,792	$ 3,056,021	$ 3,060,150
Deposit Liabilities	$ 1,608,108	$ 1,809,812	$ 1,684,606	$ 1,737,107
Notes payable and debt	2,275,327	2,340,148	2,457,003	2,439,328
Financial Liabilities	$ 3,883,435	$ 4,149,960	$ 4,141,609	$ 4,176,435
Redeemable series C preference ordinary shares	$	$	$ 71,900	$ 61,115

The Company historically participated in structured transactions. Remaining structured transactions include cash loans supporting project finance transactions, providing liquidity facility financing to structured project deals and an investment in a payment obligation with an insurance company. These transactions are carried at amortized cost. The fair value of these investments held by the Company is determined through use of internal models utilizing reported trades, benchmark yields, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data.

Deposit liabilities include obligations under structured insurance and reinsurance transactions. For purposes of fair value disclosures, the Company determined the estimated fair value of the deposit liabilities by assuming a discount rate equal to the appropriate U.S. Treasury rate plus 161.8 basis points and the appropriate U.S. Treasury rate plus 142.3 basis points at December 31, 2011 and 2010, respectively. The discount rate incorporates the Company s own credit risk into the determination of estimated fair value.

The fair values of the Company s notes payable and debt outstanding are determined based on quoted market prices.

The fair value of the Company s Redeemable Series C preference ordinary shares outstanding is determined based on indicative quotes provided by brokers. During the third quarter of 2011 all outstanding Redeemable Series C preference ordinary shares were repurchased and canceled. At December 31, 2011, no Redeemable Series C preference ordinary shares were outstanding.

There are no significant concentrations of credit risk within the Company s financial instruments as defined in the authoritative guidance over disclosures of fair value of financial instruments not carried at fair value, which excludes certain financial instruments, particularly insurance contracts.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

4. Segment Information

The Company is organized into three operating segments: Insurance, Reinsurance and Life operations. The Company s general investment and financing operations are reflected in Corporate.

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

Year ended December 31, 2011: *(U.S. dollars in thousands, except ratios)*	**Insurance**	**Reinsurance**	**Total P&C**	**Life Operations**	**Corporate**	**Total**
Gross premiums written	$ 4,824,665	$ 2,073,619	$ 6,898,284	$ 394,555	$	$ 7,292,839
Net premiums written	3,707,664	1,725,724	5,433,388	362,362		5,795,750
Net premiums earned	3,663,727	1,663,385	5,327,112	363,018		5,690,130
Net losses and loss expenses	(2,951,413)	(1,126,978)	(4,078,391)	(535,074)		(4,613,465)
Acquisition costs	(461,965)	(324,128)	(786,093)	(40,318)		(826,411)
Operating expenses (1)	(683,814)	(176,167)	(859,981)	(9,311)		(869,292)
Underwriting profit (loss)	$ (433,465)	$ 36,112	$ (397,353)	$ (221,685)	$	$ (619,038)
Net investment income			745,138	318,061		1,063,199
Net results from structured products (2)	10,976	12,053	23,029			23,029
Net fee income and other (3)	(16,370)	3,903	(12,467)	219		(12,248)
Net realized gains (losses) on investments			(98,360)	(89,999)		(188,359)
Contribution from P&C, Life Operations and Corporate			$ 259,987	$ 6,596	$	$ 266,583
Corporate & other:						
Net realized & unrealized gains (losses) on derivative instruments					$ (10,738)	$ (10,738)
Net income (loss) from investment fund affiliates and operating affiliates					103,039	103,039
Exchange gains (losses)					40,640	40,640
Corporate operating expenses					(159,158)	(159,158)
Interest expense (4)					(154,084)	(154,084)
Non-controlling interests					(70,877)	(70,877)
Impairment of goodwill (5)					(429,020)	(429,020)
Income taxes & other					(61,145)	(61,145)
Net income (loss) attributable to XL Group plc						$ (474,760)
Ratios P&C operations: (6)						

Loss and loss expense ratio	80.6%	67.8%	76.6%
Underwriting expense ratio	31.2%	30.0%	30.9%
Combined ratio	111.8%	97.8%	107.5%

Notes:

(1) Operating expenses exclude Corporate operating expenses, shown separately.

(2) The net results from P&C structured products include net investment income, interest expense and operating expenses of $74.6 million, $51.5 million and nil, respectively.

(3) Net fee income and other includes operating expenses from the Company s loss prevention consulting services business and expenses related to the cost of an endorsement facility with National Indemnity Company.

(4) Interest expense excludes interest expense related to deposit liabilities recorded in the Insurance and Reinsurance segments.

(5) Represents goodwill impairment charges recorded in the fourth quarter of 2011, associated with the Company s insurance operations.

(6) Ratios are based on net premiums earned from P&C operations.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

4. Segment Information (Continued)

Year ended December 31, 2010:

(U.S. dollars in thousands, except ratios)	Insurance	Reinsurance	Total P&C	Life Operations	Corporate	Total
Gross premiums written	$ 4,418,380	$ 1,842,951	$ 6,261,331	$ 411,938	$	$ 6,673,269
Net premiums written	3,461,150	1,538,438	4,999,588	382,075		5,381,663
Net premiums earned	3,529,138	1,501,999	5,031,137	382,924		5,414,061
Net losses and loss expenses	(2,505,502)	(706,298)	(3,211,800)	(513,833)		(3,725,633)
Acquisition costs	(418,146)	(321,008)	(739,154)	(49,104)		(788,258)
Operating expenses (1)	(642,103)	(175,586)	(817,689)	(10,470)		(828,159)
Underwriting profit (loss)	$ (36,613)	$ 299,107	$ 262,494	$ (190,483)	$	$ 72,011
Net investment income			803,358	313,172		1,116,530
Net results from structured products (2)	14,696	3,075	17,771		9,804	27,575
Net fee income and other (3)	(15,564)	2,488	(13,076)	249	2	(12,825)
Net realized gains (losses) on investments			(206,877)	(54,444)	(9,482)	(270,803)
Contribution from P&C, Life Operations and Corporate			$ 863,670	$ 68,494	$ 324	$ 932,488
Corporate & other:						
Net realized & unrealized gains (losses) on derivative instruments					$ (33,843)	$ (33,843)
Net income (loss) from investment fund affiliates and operating affiliates					172,474	172,474
Exchange gains (losses)					10,161	10,161
Corporate operating expenses					(90,686)	(90,686)
Interest expense (4)					(159,118)	(159,118)
Non-controlling interests					(39,831)	(39,831)
Loss on termination of guarantee					(23,500)	(23,500)
Income taxes & other					(164,595)	(164,595)
Net income (loss) attributable to XL Group plc						$ 603,550
Ratios P&C operations: (5)						
Loss and loss expense ratio	71.0%	47.0%	63.8%			
Underwriting expense ratio	30.0%	33.1%	31.0%			
Combined ratio	101.0%	80.1%	94.8%			

Notes:

(1) Operating expenses exclude Corporate operating expenses, shown separately.
(2) The net results from P&C and Corporate structured products include net investment income, interest expense and operating expenses of $69.0 million, $52.9 million and $1.6 million (credit) and $12.5 million, $1.7 million and $1.0 million, respectively.
(3) Net fee income and other includes operating expenses from the Company s loss prevention consulting services business and expenses related to the cost of an endorsement facility with National Indemnity Company.
(4) Interest expense excludes interest expense related to deposit liabilities recorded in the Insurance and Reinsurance segments and Corporate.
(5) Ratios are based on net premiums earned from P&C operations.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

4. Segment Information (Continued)

Year ended December 31, 2009: *(U.S. dollars in thousands, except ratios)*	**Insurance**	**Reinsurance**	**Total P&C**	**Life Operations**	**Corporate**	**Total**
Gross premiums written	$ 4,251,888	$ 1,859,423	$ 6,111,311	$ 576,162	$	$ 6,687,473
Net premiums written	3,273,380	1,470,332	4,743,712	532,852		5,276,564
Net premiums earned	3,559,793	1,591,946	5,151,739	555,101		5,706,840
Net losses and loss expenses	(2,399,747)	(769,090)	(3,168,837)	(677,562)		(3,846,399)
Acquisition costs	(429,170)	(346,699)	(775,869)	(77,689)		(853,558)
Operating expenses (1)	(689,131)	(190,596)	(879,727)	(16,009)		(895,736)
Underwriting profit (loss)	$ 41,745	$ 285,561	$ 327,306	$ (216,159)	$	$ 111,147
Net investment income			882,748	332,425		1,215,173
Net results from structured products (2)	16,660	26,374	43,034		16,609	59,643
Net fee income and other (3)	(14,241)	6,209	(8,032)	290		(7,742)
Net realized gains (losses) on investments			(659,687)	(232,375)	(29,375)	(921,437)
Contribution from P&C, Life Operations and Corporate			$ 585,369	$ (115,819)	$ (12,766)	$ 456,784
Corporate & other:						
Net realized & unrealized gains (losses) on derivative instruments					$ (33,647)	$ (33,647)
Net income (loss) from investment fund affiliates and operating affiliates					139,347	139,347
Exchange gains (losses)					(84,813)	(84,813)
Corporate operating expenses					(107,877)	(107,877)
Interest expense (4)					(172,764)	(172,764)
Non-controlling interest in net (income) loss of subsidiary					104	104
Loss on termination of guarantee						
Income taxes & other					(122,143)	(122,143)
Net income (loss) attributable to XL Group plc						$ 74,991
Ratios P&C operations: (5)						
Loss and loss expense ratio	67.4%	48.3%	61.5%			
Underwriting expense ratio	31.4%	33.8%	32.1%			
Combined ratio	98.8%	82.1%	93.6%			

Notes:
(1) Operating expenses exclude Corporate operating expenses, shown separately.
(2) The net results from P&C and Corporate structured products include net investment income, interest expense and operating expenses of $79.3 million, $36.3 million and nil, and $25.3 million, $7.4 million and $1.3 million, respectively.
(3) Net fee income and other includes operating expenses from the Company s loss prevention consulting services business and expenses related to the cost of an endorsement facility with National Indemnity Company.

(4) Interest expense excludes interest expense related to deposit liabilities recorded in the Insurance and Reinsurance segments and Corporate.
(5) Ratios are based on net premiums earned from P&C operations.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

4. Segment Information (Continued)

The following tables summarize the Company s net premiums earned by line of business:

Year ended December 31, 2011: *(U.S. dollars in thousands)*	**Insurance**	**Reinsurance**	**Life Operations**	**Total**
P&C Operations:				
Casualty professional lines	$ 1,287,230	$ 213,949	$	$ 1,501,179
Casualty other lines	695,094	256,853		951,947
Property catastrophe		387,523		387,523
Other property	481,148	587,611		1,068,759
Marine, energy, aviation and satellite	528,454	130,855		659,309
Other specialty lines (1)	665,727			665,727
Other (2)	3,552	90,776		94,328
Structured indemnity	2,522	(4,182)		(1,660)
Total P&C Operations	$ 3,663,727	$ 1,663,385	$	$ 5,327,112
Life Operations:				
Other Life	$	$	$ 230,786	$ 230,786
Annuity			132,232	132,232
Total Life Operations	$	$	$ 363,018	$ 363,018
Total	$ 3,663,727	$ 1,663,385	$ 363,018	$ 5,690,130

Year ended December 31, 2010: *(U.S. dollars in thousands)*	**Insurance**	**Reinsurance**	**Life Operations**	**Total**
P&C Operations:				
Casualty professional lines	$ 1,316,172	$ 222,720	$	$ 1,538,892
Casualty other lines	611,674	219,154		830,828
Property catastrophe		323,588		323,588
Other property	416,806	534,422		951,228
Marine, energy, aviation and satellite	540,319	88,855		629,174
Other specialty lines (1)	621,839			621,839
Other (2)	7,577	112,303		119,880
Structured indemnity	14,751	957		15,708
Total P&C Operations	$ 3,529,138	$ 1,501,999	$	$ 5,031,137
Life Operations:				
Other Life	$	$	$ 255,905	$ 255,905
Annuity			127,019	127,019
Total Life Operations	$	$	$ 382,924	$ 382,924
Total	$ 3,529,138	$ 1,501,999	$ 382,924	$ 5,414,061

Year ended December 31, 2009: *(U.S. dollars in thousands)*	**Insurance**	**Reinsurance**	**Life Operations**	**Total**
P&C Operations:				
Casualty professional lines	$ 1,276,005	$ 196,624	$	$ 1,472,629
Casualty other lines	655,126	257,610		912,736
Property catastrophe	2,396	312,780		315,176
Other property	424,045	560,379		984,424
Marine, energy, aviation and satellite	546,806	83,532		630,338
Other specialty lines (1)	634,436			634,436
Other (2)	12,217	172,588		184,805
Structured indemnity	8,762	8,433		17,195
Total P&C Operations	$ 3,559,793	$ 1,591,946	$	$ 5,151,739
Life Operations:				
Other Life	$	$	$ 422,594	$ 422,594
Annuity			132,507	132,507
Total Life Operations	$	$	$ 555,101	$ 555,101
Total	$ 3,559,793	$ 1,591,946	$ 555,101	$ 5,706,840

(1) Other specialty lines within the Insurance segment includes: environmental, programs, equine, warranty, specie, middle markets and excess and surplus lines.

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

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

4. Segment Information (Continued)

The following table shows an analysis of the Company s net premiums written by geographical location of subsidiary where the premium is written for the years ended December 31:

P&C operations: *(U.S. dollars in thousands)*	**2011**	**2010**	**2009**
Bermuda	$ 572,825	$ 561,514	$ 545,965
United States	2,320,274	2,143,240	2,342,656
Europe and other	2,540,289	2,294,834	1,855,091
Total P&C operations	$ 5,433,388	$ 4,999,588	$ 4,743,712
Life Operations: *(U.S. dollars in thousands)*			
Bermuda	$ 75,219	$ 79,033	$ 80,498
United States			31,478
Europe and other	287,143	303,042	420,876
Total Life Operations	$ 362,362	$ 382,075	$ 532,852
Total	$ 5,795,750	$ 5,381,663	$ 5,276,564

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments

(a) Fixed Maturities, Short-Term Investments and Equity Securities

Amortized Cost and Fair Value Summary

The cost (amortized cost for fixed maturities and short-term investments), fair value, gross unrealized gains and gross unrealized (losses), including, other-than-temporary impairments (OTTI) recorded in accumulated other comprehensive income (AOCI) of the Company s available for sale (AFS) and held to maturity (HTM) investments at December 31, 2011 and 2010 were as follows:

		Included in Accumulated Other Comprehensive Income (AOCI)			
			Gross Unrealized Losses		
December 31, 2011 *(U.S. dollars in thousands)*	**Cost or Amortized Cost**	**Gross Unrealized Gains**	**Related to Changes In Estimated Fair Value**	**OTTI Included In Other Comprehensive Income (Loss)(1)**	**Fair Value**
Fixed maturities AFS					
U.S. Government and Government-Related/Supported (2)	$ 1,864,354	$ 130,874	$ (4,245)	$	$ 1,990,983
Corporate (3) (4)	10,212,083	539,389	(237,291)	(51,666)	10,462,515
Residential mortgage-backed securities Agency	5,189,473	193,782	(3,849)		5,379,406
Residential mortgage-backed securities Non-Agency	851,557	19,667	(112,867)	(116,542)	641,815
Commercial mortgage-backed securities	927,684	56,704	(2,405)	(7,148)	974,835
Collateralized debt obligations	843,553	6,624	(186,578)	(4,997)	658,602
Other asset-backed securities	995,903	18,534	(21,776)	(6,305)	986,356
U.S. States and political subdivisions of the States	1,698,573	101,025	(2,220)		1,797,378
Non-U.S. Sovereign Government, Supranational and Government-Related/Supported (2)	3,188,535	127,439	(17,839)		3,298,135
Total fixed maturities AFS	$ 25,771,715	$ 1,194,038	$ (589,070)	$ (186,658)	$ 26,190,025
Total short-term investments (2) (3)	$ 359,378	$ 519	$ (834)	$	$ 359,063
Total equity securities	$ 480,685	$ 27,947	$ (40,435)	$	$ 468,197
Total investments AFS	$ 26,611,778	$ 1,222,504	$ (630,339)	$ (186,658)	$ 27,017,285
Fixed maturities HTM					
U.S. Government and Government-Related/Supported (2)	$ 10,399	$ 1,510	$	$	$ 11,909
Corporate	1,298,266	91,313	(14,747)		1,374,832
Residential mortgage-backed securities Non-Agency	80,955	6,520	(32)		87,443
Other asset-backed securities	280,684	20,875	(6)		301,553

Non-U.S. Sovereign Government, Supranational and Government-Related/Supported (2)	998,674	127,227	(5,950)		1,119,951
Total fixed maturities HTM	$ 2,668,978	$ 247,445	$ (20,735)	$	$ 2,895,688

(1) Represents the amount of OTTI losses in AOCI, which from April 1, 2009 was not included in earnings following authoritative accounting guidance.

(2) U.S. Government and Government-Related/Supported, Non-U.S. Sovereign Government, Provincials, Supranationals and Government-Related/Supported and Total short-term investments includes government-related securities with an amortized cost of $1,878.3 million and fair value of $1,915.6 million and U.S. Agencies with an amortized cost of $494.0 million and fair value of $541.2 million.

(3) Included within Corporate are certain medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes have a fair value of $266.0 million and an amortized cost of $297.7 million. These notes allow the investor to participate in cash flows of the underlying bonds including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(4) Included within Corporate are Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments, which are senior to the common and preferred equities of the financial institutions. These securities have a fair value of $386.1 million and an amortized cost of $494.9 million at December 31, 2011.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(a) Fixed Maturities, Short-Term Investments and Equity Securities (Continued)

Amortized Cost and Fair Value Summary (Continued)

		Included in Accumulated Other Comprehensive Income (AOCI)			
			Gross Unrealized Losses		
December 31, 2010 *(U.S. dollars in thousands)*	**Cost or Amortized Cost**	**Gross Unrealized Gains**	**Related to Changes In Estimated Fair Value**	**OTTI Included In Other Comprehensive Income (Loss)(1)**	**Fair Value**
Fixed maturities AFS					
U.S. Government and Government-Related/Supported (2)	$ 2,499,079	$ 102,685	$ (36,320)	$	$ 2,565,444
Corporate (3) (4)	10,962,804	361,154	(281,849)	(73,138)	10,968,971
Residential mortgage-backed securities Agency	5,059,249	153,106	(8,644)		5,203,711
Residential mortgage-backed securities Non-Agency	1,257,474	26,361	(133,761)	(128,251)	1,021,823
Commercial mortgage-backed securities	1,135,075	55,852	(7,960)	(10,460)	1,172,507
Collateralized debt obligations	920,501	11,014	(188,563)	(8,814)	734,138
Other asset-backed securities	979,539	16,111	(26,954)	(8,164)	960,532
U.S. States and political subdivisions of the States	1,379,150	16,755	(35,449)		1,360,456
Non-U.S. Sovereign Government, Supranational and Government-Related/Supported (2)	3,129,971	70,499	(45,947)		3,154,523
Total fixed maturities AFS	$ 27,322,842	$ 813,537	$ (765,447)	$ (228,827)	$ 27,142,105
Total short-term investments (2) (3)	$ 450,491	$ 680	$ (490)	$	$ 450,681
Total equity securities	$ 56,737	$ 28,083	$ (53)	$	$ 84,767
Total investments AFS	$ 27,830,070	$ 842,300	$ (765,990)	$ (228,827)	$ 27,677,553
Fixed maturities HTM					
U.S. Government and Government-Related/Supported (2)	$ 10,541	$ 164	$ (9)	$	$ 10,696
Corporate	1,337,797	6,370	(16,325)		1,327,842
Residential mortgage-backed securities Non-Agency	82,763	634	(546)		82,851
Other asset-backed securities	287,109	1,134	(1,410)		286,833
Non-U.S. Sovereign Government, Supranational and Government-Related/Supported (2)	1,010,125	30,680	(6,401)		1,034,404

Total fixed maturities	**HTM**	$ 2,728,335	$ 38,982	$ (24,691)	$	$ 2,742,626

(1) Represents the amount of OTTI losses in AOCI, which from April 1, 2009 was not included in earnings following authoritative accounting guidance.

(2) U.S. Government and Government-Related/Supported, Non-U.S. Sovereign Government, Provincials, Supranationals and Government-Related/Supported and Total short-term investments includes government-related securities with an amortized cost of $2,101.0 million and fair value of $2,131.2 million and U.S. Agencies with an amortized cost of $1,019.2 million and fair value of $1,072.6 million.

(3) Included within Corporate are certain medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes have a fair value of $454.8 million and an amortized cost of $504.6 million. These notes allow the investor to participate in cash flows of the underlying bonds including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(4) Included within Corporate are Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments, which are senior to the common and preferred equities of the financial institutions. These securities have a fair value of $757.8 million and an amortized cost of $883.0 million at December 31, 2010.

5. Investments (Continued)

(a) Fixed Maturities, Short-Term Investments and Equity Securities (Continued)

Amortized Cost and Fair Value Summary (Continued)

At December 31, 2011 and 2010, approximately 2.4% and 3.5%, respectively, of the Company s fixed income investment portfolio at fair value was invested in securities which were below investment grade or not rated. Approximately 31.4% and 29.4% of the gross unrealized losses in the Company s fixed income securities portfolio at December 31, 2011 and 2010, respectively, related to securities that were below investment grade or not rated.

Classification of Fixed Income Securities

During the third quarter of 2011, the Company changed the manner in which it classifies fixed income securities between Fixed maturities and Short-term investments on the balance sheet and related note disclosures. Short-term investments under the Company s previous classification comprised investments with a remaining maturity of less than one year from the reporting date. Under this prior presentation, longer term securities were reclassified from Fixed maturities to Short-term investments as they neared maturity. Under the Company s new classification, Short-term investments include investments due to mature within one year from the date of purchase and are valued using the same external factors and in the same manner as Fixed maturities. No reclassifications will be made between Fixed maturities and Short-term investments subsequent to the initial date of purchase. The Company s new accounting classification aligns its presentation with that of its peer companies.

This change in classification did not have an impact on the total value of investments available for sale on the balance sheet, nor did it impact the consolidated statements of income, comprehensive income, shareholders equity or cash flows. The only impact, other than the changes in the balance sheet line items, are changes required within the detailed tables included within this note as well as Note 3, Fair Value Measurements, to allocate securities previously classified as Short-term investments under the former practice into the appropriate categories of Fixed maturities within each table to conform to the new accounting presentation for current and comparative periods.

During 2009 and 2010, the Company elected to hold certain fixed income securities to maturity. Consistent with this intention, the Company reclassified these securities from AFS to HTM in the consolidated financial statements. As a result of this classification, these fixed income securities are reflected in the HTM portfolio and recorded at amortized cost in the consolidated balance sheets and not fair value. The HTM portfolio is comprised of long duration non-U.S. securities, which are Euro and U.K. sterling denominated. The Company believes this HTM strategy is achievable due to the relatively stable and predictable cash flows of the Company s long-term liabilities within its Life operations, along with its ability to substitute other assets at a future date in the event that liquidity was required due to changes in expected cash flows or other transactions entered into related to the long-term liabilities supported by the HTM portfolio. At December 31, 2011, 98.1% of the HTM securities were rated A or higher. The unrealized appreciation at the dates of these reclassifications continues to be reported as a separate component of shareholders equity and is being amortized over the remaining lives of the securities as an adjustment to yield in a manner consistent with the amortization of any premium or discount. At the time of the reclassifications, the unrealized U.S. dollar equivalent appreciation related to securities reclassified was $127.4 million in total, with $108.4 million and $119.0 million unamortized at December 31, 2011 and December 31, 2010, respectively.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(a) Fixed Maturities, Short-Term Investments and Equity Securities (Continued)

Contractual Maturities Summary

The contractual maturities of AFS and HTM fixed income securities at December 31, 2011 and 2010 are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	2011 (1)		2010 (1)	
(U.S. dollars in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Fixed maturities - AFS				
Due less than one year	$ 2,025,446	$ 2,041,814	$ 1,583,265	$ 1,570,909
Due after 1 through 5 years	7,874,145	8,049,150	9,021,926	9,118,229
Due after 5 through 10 years	3,788,673	3,953,496	4,137,260	4,198,362
Due after 10 years	3,275,281	3,504,551	3,228,553	3,161,894
	16,963,545	17,549,011	17,971,004	18,049,394
Residential mortgage-backed securities Agency	5,189,473	5,379,406	5,059,249	5,203,711
Residential mortgage-backed securities Non-Agency	851,557	641,815	1,257,474	1,021,823
Commercial mortgage-backed securities	927,684	974,835	1,135,075	1,172,507
Collateralized debt obligations	843,553	658,602	920,501	734,138
Other asset-backed securities	995,903	986,356	979,539	960,532
Total mortgage and asset-backed securities	8,808,170	8,641,014	9,351,838	9,092,711
Total fixed maturities - AFS	$ 25,771,715	$ 26,190,025	$ 27,322,842	$ 27,142,105
Fixed maturities - HTM				
Due less than one year	$ 11,796	$ 11,768	$	$
Due after 1 through 5 years	122,091	123,871	125,449	125,416
Due after 5 through 10 years	393,865	402,424	348,797	346,494
Due after 10 years	1,779,587	1,968,629	1,884,217	1,901,032
	2,307,339	2,506,692	2,358,463	2,372,942
Residential mortgage-backed securities Non-Agency	80,955	87,443	82,763	82,851
Other asset-backed securities	280,684	301,553	287,109	286,833
Total mortgage and asset-backed securities	361,639	388,996	369,872	369,684
Total fixed maturities - HTM	$ 2,668,978	$ 2,895,688	$ 2,728,335	$ 2,742,626

(1) Included in the table above are Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments, which are senior to the common and preferred equities of the financial institutions, at their fair value of $386.1 million and $757.8 million at

December 31, 2011 and 2010, respectively. These securities are reflected in the table based on their call date and have net unrealized losses of $108.8 million and $143.7 million at December 31, 2011 and 2010, respectively.

5. Investments (Continued)

(a) Fixed Maturities, Short-Term Investments and Equity Securities (Continued)

OTTI Considerations

Under final authoritative accounting guidance, a debt security for which amortized cost exceeds fair value is deemed to be other-than-temporarily impaired if it meets either of the following conditions: (a) the Company intends to sell, or it is more likely than not that the Company will be required to sell, the security before a recovery in value, or (b) the Company does not expect to recover the entire amortized cost basis of the security. Other than in a situation in which the Company has the intent to sell a debt security or more likely than not will be required to sell a debt security, the amount of the OTTI related to a credit loss on the security is recognized in earnings, and the amount of the OTTI related to other factors (e.g., interest rates, market conditions, etc.) is recorded as a component of OCI. The net amount recognized in earnings (credit loss impairments) represents the difference between the amortized cost of the security and the net present value of its projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment (NPV). The remaining difference between the security s NPV and its fair value is recognized in OCI. Subsequent changes in the fair value of these securities are included in OCI unless a further impairment is deemed to have occurred.

In the scenario where the Company has the intent to sell a security in which its amortized cost exceeds its fair value, or it is more likely than not it will be required to sell such a security, the entire difference between the security s amortized cost and its fair value is recognized in earnings.

The determination of credit losses is based on detailed analyses of underlying cash flows. Such analyses require the use of certain assumptions to develop the estimated performance of underlying collateral. Key assumptions used include, but are not limited to, items such as RMBS default rates based on collateral duration in arrears, severity of losses on default by collateral class, collateral reinvestment rates and expected future general corporate default rates.

Factors considered in determining that a gross unrealized loss is not other-than-temporarily impaired include management s consideration of current and near term liquidity needs and other available sources of funds, an evaluation of the factors and time necessary for recovery and an assessment of whether the Company has the intention to sell or considers it more likely than not that it will be forced to sell a security.

Pledged Assets

Certain of the Company s invested assets are held in trust and pledged in support of insurance and reinsurance liabilities. Such pledges are largely required by the Company s operating subsidiaries that are non-admitted under U.S. state insurance regulations, in order for the U.S. cedant to receive statutory credit for reinsurance. Also, certain deposit liabilities and annuity contracts require the use of pledged assets. As further outlined in Note 17(f) Commitments and Contingencies Letters of Credit, certain assets of the investment portfolio are collateralized for the Company s letter of credit facilities. At December 31, 2011 and 2010, the Company had $17.2 billion and $16.1 billion in pledged assets, respectively.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(b) Gross Unrealized Losses

The following is an analysis of how long the AFS and HTM securities at December 31, 2011 had been in a continual unrealized loss position:

	Less than 12 months		Equal to or greater than 12 months	
December 31, 2011 *(U.S. dollars in thousands)*	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses (1)**
Fixed maturities and short-term investments - AFS:				
U.S. Government and Government-Related/Supported	$ 289,260	$ (332)	$ 43,622	$ (3,984)
Corporate (2) (3)	1,108,177	(42,978)	1,200,717	(246,566)
Residential mortgage-backed securities Agency	310,318	(849)	36,960	(3,000)
Residential mortgage-backed securities Non-Agency	106,294	(31,714)	449,138	(197,695)
Commercial mortgage-backed securities	69,109	(2,716)	39,444	(6,837)
Collateralized debt obligations	3,357	(2,261)	636,362	(189,456)
Other asset-backed securities	197,585	(2,497)	146,130	(25,584)
U.S. States and political subdivisions of the States	25,309	(199)	27,646	(2,021)
Non-U.S. Sovereign Government, Supranational and Government-Related	265,766	(4,707)	202,890	(13,166)
Total fixed maturities and short-term investments - AFS	$ 2,375,175	$ (88,253)	$ 2,782,909	$ (688,309)
Total equity securities (4)	$ 361,585	$ (40,435)	$	$
Fixed maturities HTM:				
U.S. Government and Government-Related/Supported	$	$	$	$
Corporate	155,579	(8,084)	62,343	(6,663)
Residential mortgage-backed securities Non-Agency	9,372	(32)		
Other asset-backed securities			1,106	(6)
Non-U.S. Sovereign Government, Supranational and Government-Related/Supported	79,242	(1,206)	18,330	(4,744)
Total fixed maturities HTM	$ 244,193	$ (9,322)	$ 81,779	$ (11,413)

(1) On securities impacted by the April 1, 2009 changes to OTTI values, length of time of impairment is measured from the point at which securities returned to a net unrealized loss position (i.e., from April 1, 2009).

(2) Included within Corporate are certain medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes, which are in a gross unrealized loss position, have a fair value of $266.0 million and an amortized cost of $297.7 million. These notes allow the investor to participate in cash flows of the underlying bonds including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(3)

Included within Corporate are Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments, which are senior to the common and preferred equities of the financial institutions. These securities, which are in a gross unrealized loss position, have a fair value of $386.1 million and an amortized cost of $494.9 million at December 31, 2011.

(4) Included within equity securities are investments in fixed income funds with a fair value of $91.6 million and an amortized cost of $100.0 million at December 31, 2011.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(b) Gross Unrealized Losses

The following is an analysis of how long the AFS and HTM securities at December 31, 2010 had been in a continual unrealized loss position:

	Less than 12 months		Equal to or greater than 12 months	
December 31, 2010 *(U.S. dollars in thousands)*	**Fair Value**	**Gross Unrealized Losses (1)**	**Fair Value**	**Gross Unrealized Losses (1)**
Fixed maturities and short-term investments - AFS:				
U.S. Government and Government-Related/Supported	$ 307,082	$ (25,482)	$ 117,394	$ (10,417)
Corporate (2) (3)	2,271,887	(80,276)	1,627,083	(275,023)
Residential mortgage-backed securities Agency	280,390	(6,736)	34,186	(1,913)
Residential mortgage-backed securities Non-Agency	40,052	(2,574)	843,168	(259,715)
Commercial mortgage-backed securities	46,419	(2,472)	69,475	(15,967)
Collateralized debt obligations	2,500	(51)	715,295	(197,535)
Other asset-backed securities	122,548	(1,619)	226,946	(33,546)
U.S. States and political subdivisions of the States	734,893	(30,033)	40,907	(5,452)
Non-U.S. Sovereign Government, Supranational and Government-Related	459,686	(5,116)	418,322	(40,837)
Total fixed maturities and short-term investments - AFS	$ 4,265,457	$ (154,359)	$ 4,092,776	$ (840,405)
Total equity securities	$ 158	$ (53)	$	$
Fixed maturities HTM:				
U.S. Government and Government-Related/Supported	$ 1,755	$ (9)	$	$
Corporate	764,397	(16,325)		
Residential mortgage-backed securities Non-Agency	37,899	(546)		
Other asset-backed securities	232,673	(1,410)		
Non-U.S. Sovereign Government, Supranational and Government-Related/Supported	175,382	(6,401)		
Total fixed maturities HTM	$ 1,212,106	$ (24,691)	$	$

(1) On securities impacted by the April 1, 2009 changes to OTTI values, length of time of impairment is measured from the point at which securities returned to a net unrealized loss position (i.e., from April 1, 2009).

(2) Included within Corporate are certain medium term notes supported primarily by pools of European investment grade credit with varying degrees of leverage. The notes have a fair value of $370.8 million and an amortized cost of $423.9 million. These notes allow the investor to participate in cash flows of the underlying bonds including certain residual values, which could serve to either decrease or increase the ultimate values of these notes.

(3) Included within Corporate are Tier One and Upper Tier Two securities, representing committed term debt and hybrid instruments senior to the common and preferred equities of the financial institutions. These securities have a fair value of $757.8 million and an amortized cost of $883.0 million at December 31, 2010.

The Company had gross unrealized losses totaling $817.0 million on 1,890 securities out of a total of 7,146 held at December 31, 2011 on its available for sale portfolio and $20.7 million on 36 securities out of a total of 213 held on its held-to-maturity portfolio, which it considers to be temporarily impaired or includes non-credit losses on OTTI. Individual security positions comprising this balance have been evaluated by management to determine the severity of these impairments and whether they should be considered other-than-temporary.

5. Investments (Continued)

(b) Gross Unrealized Losses (Continued)

Gross unrealized losses of $817.0 million on available for sale and $20.7 million on HTM assets at December 31, 2011 can be attributed to the following significant drivers:

gross unrealized losses of $229.4 million related to the Non-Agency residential mortgage-backed securities (RMBS) portfolio (which consists of the Company s holdings of sub-prime Non-Agency securities, second liens, asset-backed securities (ABS) CDOs with sub-prime collateral, Alt-A mortgage exposures and Prime RMBS), which had a fair value of $722.8 million at December 31, 2011. The Company, in conjunction with its investment manager service providers, undertook a security level review of these securities and recognized charges to the extent it believed the discounted cash flow value of any security was below its amortized cost. The Company has recognized realized losses, consisting of charges for OTTI and realized losses from sales, of approximately $1.4 billion since the beginning of 2007 through December 31, 2011 on these asset classes.

gross unrealized losses of $244.3 million related to the Company s Life operations investment portfolio, which had a fair value of $6.5 billion at December 31, 2011. Of these gross unrealized losses, $144.9 million related to $1.2 billion of exposures to corporate financial institutions, including $301.0 million Tier One and Upper Tier Two securities. At December 31, 2011, this portfolio had an average interest rate duration of 8.6 years, primarily denominated in U.K. sterling and Euros. As a result of the long duration, significant gross losses have arisen as the fair values of these securities are more sensitive to prevailing government interest rates and credit spreads. This portfolio is generally matched to corresponding long duration liabilities. A hypothetical parallel increase in interest rates and credit spreads of 50 and 25 basis points, respectively, would increase the unrealized losses related to this portfolio at December 31, 2011 by approximately $274.5 million and $104.0 million, respectively, on both the available for sale and HTM portfolios. Given the long term nature of this portfolio, the level of credit spreads on financial institutions at December 31, 2011 relative to historical averages within the U.K. and Euro-zone, and the Company s liquidity needs at December 31, 2011, the Company believes that these assets will continue to be held until such time as they mature, or credit spreads on financial institutions revert to levels more consistent with historical averages.

gross unrealized losses of $191.7 million related to the non-life portfolio of Core CDO holdings (defined by the Company as investments in non-subprime CDOs), which consisted primarily of collateral loan obligations (CLOs) and had a fair value of $662.9 million at December 31, 2011. The Company evaluated each of these securities in conjunction with its investment manager service providers and recognized charges to the extent it believed the discounted cash flow value of the security was below the amortized cost. The Company believes that the level of impairment is primarily a function of continually wide spreads in the CDO market, driven by the level of illiquidity in this market. The Company believes it is likely these securities will be held until either maturity or a recovery of value.

gross unrealized losses of $133.2 million related to the corporate holdings within the Company s non-life fixed income portfolios, which had a fair value of $8.3 billion at December 31, 2011. During the year ended December 31, 2011, as a result of declining credit spreads, the gross unrealized losses on these holdings has decreased. Of the gross unrealized losses noted above, $72.9 million relate to financial institutions. In addition, $33.3 million relate to medium term notes primarily supported by pools of investment grade European investment grade credit with varying degrees of leverage. These had a fair value of $237.4 million at December 31, 2011. Management believes that expected cash flows from these bonds over the expected holding period will be sufficient to support the remaining reported amortized cost.

Management, in its assessment of whether securities in a gross unrealized loss position are temporarily impaired, considers the significance of the impairments. The Company had structured credit securities with gross unrealized losses of $84.4 million, with a fair value of $39.6 million, which at December 31, 2011 had cumulative fair value declines of greater than 50% of amortized costs. All of these are mortgage and asset-backed securities. The Company, in conjunction with its investment manager service providers, undertook a security level review of these securities and recognized charges to the extent it believed the discounted cash flow value of any security was below its amortized cost. These securities include gross unrealized losses of $61.2 million on non-Agency RMBS, $22.6 million on Core CDOs and $0.7 million of commercial mortgage-backed security (CMBS) holdings.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(c) Net Investment Income

Net investment income is derived from the following sources:

Year ended December 31 *(U.S. dollars in thousands)*	2011	2010	2009
Fixed maturities, short-term investments and cash equivalents	$ 1,178,038	$ 1,245,185	$ 1,369,503
Equity securities and other investments	17,804	20,693	13,753
Funds withheld	12,240	12,738	14,649
Total gross investment income	1,208,082	1,278,616	1,397,905
Investment expenses	(70,313)	(80,578)	(78,082)
Net investment income	$ 1,137,769	$ 1,198,038	$ 1,319,823

(d) Net Realized Gains (Losses)

The following represents an analysis of net realized gains (losses) and the change in unrealized (losses) gains on investments:

Year ended December 31 *(U.S. dollars in thousands)*	2011	2010	2009
Net realized gains (losses):			
Fixed maturities, short-term investments, cash and cash equivalents:			
Gross realized gains	$ 185,530	$ 133,521	$ 349,629
Gross realized losses on investments sold	(225,360)	(193,396)	(405,342)
OTTI on investments, net of amounts transferred to other comprehensive income	(159,435)	(197,377)	(811,572)
Net realized (losses)	(199,265)	(257,252)	(867,285)
Equity securities:			
Gross realized gains	2,194	11,605	65,289
Gross realized losses on investments sold	(4,264)	(11,195)	(129,516)
OTTI on investments, net of amounts transferred to other comprehensive income			
Net realized gains (losses)	(2,070)	410	(64,227)
Other investments:			
Gross realized gains	18,505	4,889	27,647
Gross realized losses on investments sold	(4,792)	(11,094)	(5,763)
OTTI on investments, net of amounts transferred to other comprehensive income	(737)	(7,756)	(886)
Net realized gains (losses)	12,976	(13,961)	20,998
Realized loss on sale of U.S. life reinsurance business			(10,923)
Net realized (losses) on investments	(188,359)	(270,803)	(921,437)
Net realized and unrealized (losses) on investment related derivative instruments	(22,981)	(16,321)	(29,709)

Net realized (losses) on investments and net realized and unrealized (losses) on investment related derivative instruments	(211,340)	(287,124)	(951,146)
Change in unrealized gains (losses):			
Fixed maturities and short-term investments, available for sale	598,542	1,095,762	2,112,244
Fixed maturities, held to maturity	212,419	30,039	(15,748)
Equity securities	(40,518)	22,595	(18,619)
Affiliates and other investments	25,268	44,314	14,464
Net change in unrealized gains (losses) on investments	795,711	1,192,710	2,092,341
Total net realized (losses) on investments, net realized and unrealized (losses) on investment related derivative instruments, and net change in unrealized gains (losses) on investments	$ 584,371	$ 905,586	$ 1,141,195

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

5. Investments (Continued)

(d) Net Realized Gains (Losses) (Continued)

The Company recorded net impairment charges of $160.2 million for the year ended December 31, 2011. The components of the impairments include:

For structured credit securities, the Company recorded net impairments of $78.7 million principally on non-Agency RMBS. The Company determined that the likely recovery on these securities was below the carrying value, and, accordingly, recorded an impairment on the securities to the discounted value of the cash flows of these securities.

For medium term notes backed primarily by investment grade European investment grade credit, the Company recorded net impairments of $31.0 million. The Company adjusted the estimated remaining holding period of certain notes resulting in a shorter reinvestment spectrum.

For corporate securities, excluding medium term notes, the Company recorded net impairments totaling $6.5 million, principally on hybrid securities.

The Company recorded impairments of $44.0 million primarily related to foreign exchange losses arising on U.S. dollar denominated securities held in a Swiss franc functional currency entity. These foreign exchange losses are recorded as part of the foreign currency revaluation process; however, because the Company s consolidated reporting currency is U.S. dollars, the foreign exchange impairment recorded on these securities is fully offset by a cumulative foreign currency translation adjustment gain recorded upon the consolidation of the foreign currency entity.

As discussed in Note 2, a portion of certain OTTI losses on fixed income securities and short-term investments are recognized in Other comprehensive income (loss) (OCI). Under final authoritative accounting guidance effective April 1, 2009, other than in a situation in which the Company has the intent to sell a security or more likely than not will be required to sell a security, the amount of the OTTI related to a credit loss is recognized in earnings, and the amount of the OTTI related to other factors (i.e., interest rates, market conditions, etc.) is recorded as a component of other comprehensive income (loss). The net amount recognized in earnings (credit loss impairments) represents the difference between the amortized cost of the security and the net present value of its projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment. Any remaining difference between the fair value and amortized cost is recognized in OCI. The following table sets forth the amount of credit loss impairments on fixed income securities held by the Company as of the dates indicated, for which a portion of the OTTI loss was recognized in OCI, and the corresponding changes in such amounts.

	OTTI related to credit losses recognized in earnings	
Year Ended December 31, *(U.S. dollars in thousands)*	**2011**	**2010**
Balance, January 1	$ 426,372	$ 537,121
Credit loss impairment recognized in the current period on securities not previously impaired	28,910	55,515
Credit loss impairments previously recognized on securities which matured, paid down, prepaid or were sold during the period	(209,187)	(125,653)
Credit loss impairments previously recognized on securities impaired to fair value during the period		(130,891)
Additional credit loss impairments recognized in the current period on securities previously impaired	88,016	113,292
Accretion of credit loss impairments previously recognized due to an increase in cash flows expected to be collected	(732)	(23,012)
Balance, December 31	$ 333,379	$ 426,372

During the years ended December 31, 2011 and 2010, the $209.2 million and $125.7 million, respectively, of credit loss impairment previously recognized on securities that matured, or were paid down, prepaid or sold, includes $128.9 million and $100.2 million, respectively, of non-Agency RMBS.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

6. Investments in Affiliates

The Company s investment portfolio includes certain investments over which the company is considered to have significant influence and which, therefore, are accounted for using the equity method. Significant influence is generally deemed to exist where the Company has an investment of 20% or more in the common stock of a corporation or an investment of 3% or more in closed end funds, limited partnerships, LLCs or similar investment vehicles. The Company generally records its alternative and private equity fund affiliates on a one month and three month lag, respectively, and its operating affiliates on a three month lag. See Note 7, Other Investments for investments in alternative and private equity funds in which the Company generally owns less than 3% and are accounted for as Other Investments.

Investments in affiliates comprised the following at December 31, 2011 and 2010:

Year ended December 31, *(U.S. dollars in thousands)*	**2011**	**2010**
Investment fund affiliates	$ 768,851	$ 829,059
Operating affiliates	283,878	298,122
Total investment affiliates	$ 1,052,729	$ 1,127,181

(a) Investment Fund Affiliates

The Company has invested in certain closed end funds, certain limited partnerships, LLCs and similar investment vehicles, including funds managed by certain of its investment manager affiliates. Collectively, these investments in funds, partnerships and other vehicles are classified as investment fund affiliates. The Company s equity investment in investment fund affiliates and equity in net income (loss) from such affiliates as well as certain summarized financial information of the investee as a whole are included below:

Year ended December 31, 2011: *(U.S. dollars in thousands, except percentages)*	**XL Group Investment**			**Combined Funds**
	Carrying Value	**Equity in Net Income (Loss) for the Year**	**Weighted Average XL Percentage Ownership**	**Total Net Assets (Estimated) (2)**
Alternative Funds (1):				
Arbitrage	$ 123,969	$ 1,291	3.4%	$ 3,678,904
Directional	217,779	9,154	6.0%	3,619,272
Event Driven	229,956	(60)	3.1%	7,472,680
Multi-Style	425	(9)	17.6%	2,410
Total alternative funds	572,129	10,376	3.9%	14,773,266
Private equity funds (1)	196,722	15,877	5.1%	3,820,497
	$ 768,851	$ 26,253	4.1%	$ 18,593,763

Year ended December 31, 2010: *(U.S. dollars in thousands, except percentages)*	**XL Group Investment**	**Combined Funds**

	Carrying Value	Equity in Net Income (Loss) for the Year	Weighted Average XL Percentage Ownership	Total Net Assets (Estimated) (2)
Alternative Funds (1):				
Arbitrage	$ 156,511	$ 9,477	4.1%	$ 3,797,962
Directional	166,644	5,972	5.9%	2,819,306
Event Driven	261,252	7,605	2.5%	10,267,525
Multi-Style	787	30	8.1%	9,688
Total alternative funds	585,194	23,084	3.5%	16,894,481
Private equity funds (1)	243,865	28,018	5.5%	4,408,189
	$ 829,059	$ 51,102	3.9%	$ 21,302,670

(1) The Company generally records its alternative fund affiliates on a one month lag and its private equity fund affiliates on a one quarter lag.

(2) Total estimated net assets are generally as at November 30 and September 30, respectively.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

6. Investments in Affiliates (Continued)

(a) Investment Fund Affiliates (Continued)

Certain funds have a lock-up period. A lock-up period refers to the initial amount of time an investor is contractually required to invest before having the ability to redeem. At the point at which funds provide for periodic redemptions, the funds may, depending on their governing documents, have the ability to deny or delay a redemption request, called a gate, or suspend redemptions as a whole. The fund may implement the gate restriction because the aggregate amount of redemption requests as of a particular date exceeds a specified level, generally ranging from 15% to 25% of the fund s net assets. The gate is a method for executing an orderly redemption process that reduces the possibility of adversely affecting the remaining investors in the fund in the event of substantial redemption requests falling on a single redemption date. Typically, the imposition of a gate delays a portion of the requested redemption, with the remaining portion settled in cash shortly after the redemption date.

The carrying value of the Company s holdings in funds that are subject to lockups and/or that have gate provisions in their governing documents as at December 31, 2011 and 2010 was $419.4 million and $428.6 million, respectively. The carrying value of the Company s holdings in funds where a gate was imposed as at December 31, 2011 and 2010 was nil and $13.5 million, respectively.

Certain funds may be allowed to invest a portion of their assets in illiquid securities, such as private equity or convertible debt. In such cases, a common mechanism used is a side-pocket, whereby the illiquid security is assigned to a separate memorandum capital account or designated account. Typically, the investor loses its redemption rights in the designated account. Only when the illiquid securities in the side-pocket are sold, or otherwise deemed liquid by the fund, may investors redeem that portion of their interest that has been side-pocketed . As at December 31, 2011 and 2010, the carrying value of our funds held in side-pockets were $30.7 million and $31.9 million, respectively. The underlying assets within these positions are generally expected to be liquidated over a period of approximately two to four years.

(b) Operating Affiliates

The Company has invested in investment and (re)insurance affiliates and investment management companies securities or other forms of ownership interests. Collectively, these investments are classified as operating affiliates.

The Company s equity investment in operating affiliates and equity in net income (loss) from such affiliates as well as certain summarized financial information of the investee as a whole are included below:

Year ended December 31, 2011: *(U.S. dollars in thousands)*	**XL Investment**		**Combined Investee Summarized Financial Data (Estimated) (1)**			
	Carrying Value	**Equity in Net Income (Loss) for the Year**	**Total Assets**	**Total Liabilities**	**Total Revenue (Loss)**	**Net Income (Loss)**
(U.S. dollars in thousands)						
Operating affiliates:						
Financial operating affiliates	$ 732	$ (1,018)	$ 11,957,534	$ 11,931,662	$ 12,564	$ 1,115
Other strategic operating affiliates	153,955	20,891	1,295,921	967,264	348,831	48,641
Investment manager affiliates (2)	129,191	56,913	601,511	38,349	319,984	222,260
Total	$ 283,878	$ 76,786	$ 13,854,966	$ 12,937,275	$ 681,379	$ 272,016

Year ended December 31, 2010: *(U.S. dollars in thousands)*	**XL Investment**	**Combined Investee Summarized Financial Data (Estimated) (1)**

	Carrying Value	Equity in Net Income (Loss) for the Year	Total Assets	Total Liabilities	Total Revenue (Loss)	Net Income (Loss)
(U.S. dollars in thousands)						
Operating affiliates:						
Financial operating affiliates	$ 1,750	$ 53,031	$ 6,212,583	$ 6,179,978	$ (688)	$ (15,641)
Other strategic operating affiliates	122,266	28,161	1,075,578	772,572	274,786	48,792
Investment manager affiliates	174,106	40,180	654,229	70,816	375,384	348,615
Total	$ 298,122	$ 121,372	$ 7,942,390	$ 7,023,366	$ 649,482	$ 381,766

(1) The Company generally records its operating affiliates on a one quarter lag. Estimated assets and liabilities are generally at September 30, 2011 and 2010, respectively.

(2) During the year ended December 31, 201,1 the Company received distributions from its Investment Manager Affiliates of approximately $23.2 million, sold its interests in Finisterre for total proceeds of $35.0 million as explained below at Investment Manager Affiliates, and received $44.2 million as repayment of a note.

6. Investments in Affiliates (Continued)

(b) Operating Affiliate (Continued)

In certain investments, the carrying value is different from the share of the investee s underlying net assets. The differences represent goodwill on acquisition, OTTI recorded with respect to the investment, or differences in the retained capital accounts of the various equity holders (including the Company).

See Note 17(c), Commitments and Contingencies Investments in Affiliates, for further information regarding commitments related to investment in affiliates.

Financial Operating Affiliates

The Company had no significant financial operating affiliates during 2011 following the sale, during the fourth quarter of 2010, of approximately 76% of its investment in Primus Guaranty, Ltd. (Primus), reducing the Company s ownership interest from 39.7% to 9.8% at December 31, 2010. This sale generated total proceeds of $51.6 million during the year ended December 31, 2010. Given management s view of the risk exposure, expected losses and the uncertainty facing the entire financial guarantee industry in 2007, the Company had reduced the reported value of its investment in Primus to nil at December 31, 2007. The Company did not record any equity earnings during 2010, 2009 or 2008 in relation to Primus because of the significant losses and negative book value reported by Primus during these periods. Therefore, the sale in the fourth quarter of 2010 resulted in the recording of a gain of $51.6 million through Income from operating affiliates. Subsequent to the sale, the Company s ownership of Primus shares is accounted for as an available for sale equity security.

Other Strategic Operating Affiliates

The Company s strategic operating affiliates included an investment in ARX Holding Corporation of 45.7% at both December 31, 2011 and 2010. During the second quarter of 2010, the Company s 49.9% investment in the Brazilian joint venture ITAU XL Seguros Corporativos S.A. (ITAU) was sold.

Investment Manager Affiliates

During the years ended December 31, 2011, 2010, and 2009, the Company s larger investment manager affiliates included Highfields Capital, a global equity investment firm, Polar Capital, an investment firm offering traditional and alternative products and HighVista Strategies, a diversified wealth management firm. The Company recorded, through net income in affiliates, other-than-temporary declines in the values of certain investment manager affiliates totaling $0.6 million, $4.4 million and $6.9 million, for the years ended December 31, 2011, 2010 and 2009, respectively.

During the third quarter of 2011, the Company sold its interests in Finisterre for total proceeds of $35.0 million resulting in a gain of $25.3 million. In addition, this transaction includes the potential for additional amounts to be paid to the Company during 2013 and 2014 subject to the investment manager meeting certain performance targets. These amounts, if any, will be recorded when known with certainty.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

7. Other Investments

Contained within this asset class are equity interests in investment funds, limited partnerships and unrated tranches of collateralized debt obligations for which the Company does not have sufficient rights or ownership interests to follow the equity method of accounting. The Company accounts for such equity securities at estimated fair value with changes in fair value recorded through AOCI as it has no significant influence over these entities. Also included within other investments are structured transactions which are carried at amortized cost.

Other investments comprised the following at December 31, 2011 and 2010:

Year ended December 31, *(U.S. dollars in thousands)*	**2011**	**2010**
Alternative Investment Funds:		
Arbitrage	$ 132,847	$ 73,010
Directional	228,544	177,785
Multi-Style	93,664	97,506
Total alternative funds	455,055	348,301
Private investment funds	87,491	79,662
Overseas deposits	91,425	80,006
Structured transactions	323,705	330,185
Other	27,586	55,416
Total other investments	$ 985,262	$ 893,570

(a) Alternative and Private Equity Funds

At December 31, 2011, the alternative fund portfolio, accounted for as other investments, employed three strategies invested in 13 underlying funds, respectively. The Company is able to redeem the hedge funds on the same terms that the underlying funds can be redeemed. In general, the funds in which the Company is invested require at least 30 days notice of redemption, and may be redeemed on a monthly, quarterly, semi-annual, annual, or longer basis, depending on the fund.

Certain funds have a lock-up period. A lock-up period refers to the initial amount of time an investor is contractually required to invest before having the ability to redeem. At the point at which funds provide for periodic redemptions, the funds may, depending on their governing documents, have the ability to deny or delay a redemption request, called a gate, or suspend redemptions as a whole. The fund may implement the gate restriction because the aggregate amount of redemption requests as of a particular date exceeds a specified level, generally ranging from 15% to 25% of the fund s net assets. The gate is a method for executing an orderly redemption process that reduces the possibility of adversely affecting the remaining investors in the fund in the event of substantial redemption requests falling on a single redemption date. Typically, the imposition of a gate delays a portion of the requested redemption, with the remaining portion settled in cash shortly after the redemption date.

The fair value of the Company s holdings in funds that may be subject to lockups and/or that have gate provisions in their governing documents as at December 31, 2011 and 2010 was $240.0 million and $155.1 million, respectively. The Company did not have any holdings in funds where a gate was imposed as at December 31, 2011 or 2010.

Certain funds may be allowed to invest a portion of their assets in illiquid securities, such as private equity or convertible debt. In such cases, a common mechanism used is a side-pocket, whereby the illiquid security is assigned to a separate memorandum capital account or designated account. Typically, the investor loses its redemption rights in the designated account. Only when the illiquid securities in the side-pocket are sold, or otherwise deemed liquid by the fund, may investors redeem that portion of their interest that has been side-pocketed . As at December 31, 2011 and 2010, the fair value of our funds held in side-pockets were $28.4 million and $38.8 million, respectively. The underlying assets within these positions are generally expected to be liquidated over a period of approximately two to four years.

An increase in market volatility and an increase in volatility of hedge funds in general, as well as a decrease in market liquidity, could lead to a higher risk of a large decline in value of the hedge funds in any given time period.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

7. Other Investments (Continued)

(a) Alternative and Private Equity Funds (Continued)

The following represents an analysis of the net realized gains and the net unrealized gains on the Company s alternative investment funds and private equity funds:

	Net Unrealized Gains (Losses)		Net Realized Gains (Losses)		
December 31, 2011 *(U.S. dollars in thousands)*	**2011**	**2010**	**2011**	**2010**	**2009**
Alternative Investment Funds	$ 96,873	$ 86,053	$ 10,120	$ 526	$ 21,809
Private Investment Funds	33,725	18,098	3,585	3,049	
Total	$ 130,598	$ 104,151	$ 13,705	$ 3,575	$ 21,809

(b) Overseas Deposits

Overseas deposits include investments in private funds related to Lloyd s syndicates in which the underlying instruments are primarily government and government-related/supported and corporate fixed income securities. The funds themselves do not trade on an exchange and therefore are not included within available for sale securities. Also included in overseas deposits are restricted cash and cash equivalent balances held by Lloyd s syndicates for solvency purposes. Given the restricted nature of these cash balances, they are not included within the cash and cash equivalents category in the balance sheet.

(c) Structured Transactions

Project Finance Loans

The Company historically participated in structured transactions in project finance related areas under which the Company provided a cash loan supporting trade finance transactions. These transactions are accounted for in accordance with guidance governing accounting by certain entities (including entities with trade receivables) that lend to or finance the activities of others under which the loans are considered held for investment as the Company has the intent and ability to hold for the foreseeable future or until maturity or payoff. Accordingly, these funded loan participations are reported in the balance sheet at outstanding principal adjusted for any allowance for loan losses as considered necessary by management.

The following table shows a summary of the structured project finance loans:

Year ended December 31, *(U.S. dollars in thousands except term to maturity)*	**2011**	**2010**
Project Finance Loans:		
Aggregate carrying value	$ 49,650	$ 52,182
Allowance for loan losses	(9,167)	(9,900)
Amounts charged off		
Aggregate net carrying value	$ 40,483	$ 42,282
Number of individual loan participations	Six	Six

Number of individual loan participations relating to the allowance for loan losses	Two	Two
Weighted average contractual term to maturity	2.13 years	3.25 years
Weighted average credit rating	BB-	BB
Range of individual credit ratings	BB+ to CCC	BB+ to B+

Surveillance procedures are conducted over each structured project finance loan on an ongoing basis with current expectations of future collections of contractual interest and principal used to determine whether any allowance for loan losses may be required at each period end. If it is determined that a future credit loss on a specific contract is reasonably possible and an amount can be estimated, an allowance is recorded. The contractual receivable is only charged off when the final outcome is known and the Company has exhausted all commercial efforts to try and collect any outstanding balances.

7. Other Investments (Continued)

(c) Structured Transactions (Continued)

During the year ended December 31, 2011 and 2010, management conducted separate reviews of each loan participation and determined loss allowance estimates, as shown in the table above, using a recovery value concept. Management considers recovery value to be the percentage of all future contractual interest and principal that the Company expects to receive from the borrower through any combination of regular debt service, other payments, salvage and recovery. The allowances for loan losses are made when it is probable that a loss will be incurred based upon current information received from the borrower.

At December 31, 2011, one of the loan participations was being restructured by the borrower and participating lenders. Management determined the expected recovery value for this participation based on multiple risk factors, including but not limited to a difficult trading environment where margins are compressed below the historical mean, a working capital shortage that has interrupted production and prompted lawsuits from suppliers, earnings on the project are well below plan, and local bankruptcy law is untested and may make it difficult to exercise the existing security package. A second loan participation has credit risk to the operations of a borrower that is experiencing a difficult trading environment. Management determined the expected recovery value for this participation based on multiple risk factors, including but not limited to increased raw material costs adversely impacting margins, the borrower is currently operating at a net loss and has high leverage, construction risk remains as the project is behind schedule, and exposure to natural hazards that have caused a long shut down of operations.

National Indemnity Endorsement

On June 9, 2009, XL Specialty Insurance Company (XL Specialty), a wholly-owned subsidiary of XL Capital Ltd, entered into an agreement with National Indemnity Company, an insurance company subsidiary of Berkshire Hathaway Inc. (National Indemnity). Under the agreement, and a related reinsurance agreement, National Indemnity would issue endorsements (Endorsements) to certain directors and officers liability insurance policies known as Side A coverage policies underwritten by XL Specialty (the Facility).

The Endorsements entitle policyholders to present claims under such D&O policies directly to National Indemnity in the event that XL Specialty is unable to meet its obligations due to an order of insolvency, liquidation or an injunction that prohibits XL Specialty from paying claims. Under the terms of the Facility, National Indemnity would issue Endorsements with aggregate premiums of up to $140 million. The Endorsements will terminate on the tenth anniversary of their issuance. The Facility provided that National Indemnity was obligated to issue Endorsements on D&O policies issued during an eighteen month period that commenced on June 8, 2009.

In connection with the Facility, XL Insurance (Bermuda) Ltd (XLIB) purchased a payment obligation (the Obligation) in an aggregate principal amount of $150 million from National Indemnity. In addition, XL Specialty established a trust to hold the premiums (net of commissions) on the D&O policies endorsed by National Indemnity. XL Specialty also arranged to provide National Indemnity with a letter of credit in the event the assets in the trust are insufficient to meet XL Specialty s obligations under the Facility (the Letter of Credit). The trust, the Letter of Credit and the payment obligations collateralize XL Specialty s indemnity obligations under the Facility to National Indemnity for any payments National Indemnity is required to make under the Endorsements.

The outstanding Obligation was recorded in Other Investments at an estimated fair value of $128.1 million, pays a coupon of 3.5%, and is being accreted to $150 million over the 11.5 year term of the payment obligation. The difference between the estimated fair value of the Obligation and the cost of that Obligation at the time of the transaction was approximately $21.9 million and was recorded in Other Assets. This difference, together with fees of $2.5 million, was amortized in relation to the earning of the underlying policies written. During the years ended December 31, 2011, 2010 and 2009, amortization of $9.4 million, $9.5 million and $5.5 million, respectively, was recorded.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

7. Other Investments (Continued)

(c) Structured Transactions (Continued)

Other Structured Transactions

On July 17, 2009, XLIB, a wholly-owned subsidiary of the Company, purchased notes with an aggregate face amount of $155 million. The carrying value of these notes at December 31, 2011 and 2010 was $147.5 million and $147.3 million, respectively. The issuer of the notes is a structured credit vehicle that holds underlying assets including corporate debt and preferred equity securities, including some securities issued by European financial institutions, as well as project finance debt securities. The notes, which are callable under certain criteria, have a final maturity of July 22, 2039.

These structured transactions are not considered to be fair value measurements under U.S. GAAP and accordingly they have been excluded from the fair value measurement disclosures. See Note 3, Fair Value Measurements for details surrounding the estimated fair value of these investments.

(d) Other

The Company regularly reviews the performance of these other investments. The Company recorded losses of $0.7 million, $7.8 million and $0.9 million in the years ended December 31, 2011, 2010 and 2009, respectively, due to other than temporary declines in values of these other investments.

See Note 17(b), Commitments and Contingencies Other Investments, for further information regarding commitments related to other investments.

8. Goodwill and Other Intangible Assets

The following table presents an analysis of intangible assets broken down between goodwill, intangible assets with an indefinite life and intangible assets with a definite life for the years ended December 31, 2011, 2010 and 2009:

(U.S. dollars in thousands)	Goodwill	Intangible assets with an indefinite life	Intangible assets with a definite life	Total
Balance at December 31, 2008	$ 824,832	$ 18,666	$ 10,052	$ 853,550
Reclassification			(4,440)	(4,440)
Amortization		(3,300)	(1,858)	(5,158)
Foreign Currency Translation	1,177			1,177
Balance at December 31, 2009	$ 826,009	$ 15,366	$ 3,754	$ 845,129
Amortization			(1,859)	(1,859)
Foreign Currency Translation	(3,762)			(3,762)
Balance at December 31, 2010	$ 822,247	$ 15,366	$ 1,895	$ 839,508
Impairment	(429,020)			(429,020)
Amortization			(1,438)	(1,438)
Foreign Currency Translation	(1,729)			(1,729)
Balance at December 31, 2011	$ 391,498	$ 15,366	$ 457	$ 407,321

The Company recorded a non-cash impairment of $429.0 million during the fourth quarter of 2011 to write-off all of the goodwill associated with its Insurance segment reporting unit, as discussed further below. The Company s remaining goodwill as at December 31, 2011 relates to the reporting units within the Company s Reinsurance segment. The estimated fair values of these reporting units exceeded their net book values as of December 31, 2011 and 2010 and therefore no impairments were recorded. At December 31, 2011, the ending goodwill balance is comprised of gross goodwill of $1.8 billion, offset by accumulated impairment charges of $ 1.4 billion. At December 31, 2010, the accumulated impairment charge was $990 million.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

8. Goodwill and Other Intangible Assets (Continued)

The Company tests goodwill for impairment on an annual basis and on an interim basis when certain events or circumstances exist. The Company tests for impairment at the reporting unit level in accordance with the authoritative guidance on intangibles and goodwill. For the Reinsurance segment, a reporting unit is one level below the business segment, while for Insurance, the segment is also the reporting unit. The first step is to identify potential impairment by comparing the estimated fair value of a reporting unit to its estimated book value, including goodwill. The fair value of each reporting unit is derived based upon valuation techniques and assumptions the Company believes market participants would use to value the business and this is then compared to the book value of the business. The Company derives the net book value of its reporting units by estimating the amount of shareholders equity required to support the activities of each reporting unit. The estimated fair values of the reporting units are generally determined utilizing methodologies that incorporate price-to-net-tangible-book and price-to-earnings multiples of certain comparable companies in the industry, from an operational and economic standpoint. If such individual reporting unit estimated fair values - combined with an estimate of an appropriate control premium - exceed their related individual reporting unit net book values, goodwill for those individual reporting units is not deemed to be impaired. A control premium represents the value an investor would pay above non-controlling interest transaction prices in order to obtain a controlling interest in the respective company.

However, if the margin calculated between the estimated reporting unit fair value and its net book value indicates a potential impairment or a close call , a further analysis of the reporting unit s estimated fair value is performed, using an entity-specific discounted cash flow methodology. This methodology establishes fair value by estimating the present value of the projected future cash flows to be generated from the reporting unit. The discount rate applied to the projected future cash flows to arrive at the present value is intended to reflect all risks of ownership and the associated risks of realizing the stream of projected future cash flows. The discounted cash flow methodology uses the Company s projections of financial performance for a ten-year period combined with an estimated terminal value. The most significant assumptions used in the discounted cash flow methodology are the discount rate, the terminal value and expected future revenues, gross margins and operating margins, which vary among reporting units. If the individual reporting unit net book values exceed their related individual reporting unit estimated fair values based on this additional methodology, the second step of the goodwill impairment testing process is performed to measure the amount of impairment.

During the third quarter of 2011, the Company completed its annual goodwill impairment testing based on Company and industry data as of June 30, 2011, which ultimately did not result in any goodwill impairments being recorded by the Company. Although the results of this analysis did not indicate the need for any impairment charges, management evaluated the sensitivity of the fair value calculations in the goodwill impairment test and concluded that relatively small changes to key assumptions such as discount rate, the terminal value, expected future revenues, gross margins and operating margins could result in a calculated fair value insufficient to support the current level of goodwill in certain businesses. Management also concluded that the prolonged weakened market conditions resulted in the range of calculated fair values used for testing impairment in the reporting units being sufficiently close to the current net book values to warrant quarterly analysis until market conditions improve.

At December 31, 2011 the Company updated its impairment analytics utilizing all of the methodologies discussed above. As a result of the analysis performed, the Company concluded that the indicated ranges of fair values of the reporting units within the Reinsurance segment in which goodwill is carried was sufficient to support their goodwill balances; however, the indicated fair value of the Insurance segment reporting unit was not sufficient to support its goodwill balance, and thus did not pass step one of the impairment testing process. Therefore step two was required to quantify the amount of goodwill impairment. Following the step two valuation process, the $429 million carrying value of goodwill was deemed to be impaired. As a result of the continued losses in certain businesses within the segment and continued low industry market valuations, the Company increased the rate of return a market participant would require from that used in previous goodwill testing and decreased the level of control premiums added to market value multiples for the insurance reporting unit. These factors taken together, led to the conclusion that the impairment was required. The assumptions utilized within the Reinsurance Segment reporting unit valuations were not modified from those utilized during the third quarter as these units were not impacted by similar underperformance.

During 2009, the Company sold its U.S. life reinsurance business. The transaction closed during the fourth quarter of 2009. Accordingly, the full value of the licenses held relating to this business of $3.3 million was removed from intangible assets with an indefinite life as part of the sale transaction. In addition, during 2009 certain internal use software acquired as part of the XL GAPS acquisition, which occurred in late 2007, with a carried value of $4.4 million was reclassified from intangible assets with a definite life into other assets. No impairments were recorded on intangible assets during any of the years ended December 2011, 2010 and 2009.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

9. Reinsurance

The Company utilizes reinsurance and retrocession agreements principally to increase aggregate capacity and to reduce the risk of loss on business assumed. The Company s reinsurance and retrocession agreements provide for recovery of a portion of losses and loss expenses from reinsurers and reinsurance recoverables are recorded as assets. The Company is liable if the reinsurers are unable to satisfy their obligations under the agreements. Under its reinsurance security policy, the Company seeks to cede business to reinsurers generally with a financial strength rating of A or better. The Company considers reinsurers that are not rated or do not fall within the above rating categories and may grant exceptions to the Company s general policy on a case-by-case basis. The effect of reinsurance and retrocessional activity on premiums written and earned from property and casualty operations is shown below:

	Premiums Written Year Ended December 31,			Premiums Earned Year Ended December 31,		
(U.S. dollars in thousands)	**2011**	**2010**	**2009**	**2011**	**2010**	**2009**
Direct	$ 4,714,588	$ 4,398,753	$ 4,381,185	$ 4,624,557	$ 4,535,626	$ 4,861,073
Assumed	2,183,696	1,862,578	1,730,126	2,179,555	1,837,528	1,877,634
Ceded	(1,464,896)	(1,261,743)	(1,367,599)	(1,477,000)	(1,342,017)	(1,586,968)
Net	$ 5,433,388	$ 4,999,588	$ 4,743,712	$ 5,327,112	$ 5,031,137	$ 5,151,739

The Company recorded reinsurance recoveries on losses and loss expenses incurred of $1.1 billion, $1.0 billion and $0.8 billion for the years ended December 31, 2011, 2010 and 2009, respectively.

The following table presents an analysis of total unpaid losses and loss expenses and future policy benefit reserves recoverable for the year ended December 31:

(U.S. dollars in thousands)	**2011**	**2010**
P&C operations	$ 3,629,928	$ 3,649,290
Life operations	25,020	22,597
Total unpaid losses and loss expenses recoverable	$ 3,654,948	$ 3,671,887

At December 31, 2011 and 2010, the total reinsurance assets of $3.9 billion and $3.8 billion, respectively, included reinsurance receivables for paid losses and loss expenses of $220.0 million and $171.3 million, respectively, with $3.7 billion relating to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported for each year end. Although the contractual obligation of individual reinsurers to pay their reinsurance obligations is based on specific contract provisions, the collectability of such amounts requires significant estimation by management. The majority of the balance the Company has accrued as recoverable will not be due for collection until sometime in the future. Over this period of time, economic conditions and operational performance of a particular reinsurer may impact its ability to meet these obligations and while it may continue to acknowledge its contractual obligation to do so, it may not have the financial resources or willingness to fully meet its obligations to the Company.

At December 31, 2011 and 2010, the allowance for uncollectible reinsurance relating to both reinsurance balances receivable and unpaid losses and loss expenses recoverable were $99.2 million and $121.9 million, respectively. To estimate the provision for uncollectible reinsurance recoverable, the reinsurance recoverable must first be allocated to applicable reinsurers. As part of this process, ceded IBNR is allocated by reinsurer. The allocations are generally based on historical relationships between gross and ceded losses. If actual experience varies materially from historical experience, the allocation of reinsurance recoverable by reinsurer will change.

The Company uses a default analysis to estimate uncollectible reinsurance recoverables. The primary components of the default analysis are reinsurance recoverable balances by reinsurer, net of collateral, and default factors used to determine the portion of a reinsurer s balance deemed uncollectible. The definition of collateral for this purpose requires some judgment and is generally limited to assets held in trust, letters of credit, and liabilities held by the Company with the same legal entity for which the Company believes there is a right of offset. The Company is the beneficiary of letters of credit, trust accounts and funds withheld in the aggregate amount of $1.7 billion at December 31, 2011, collateralizing reinsurance recoverables with respect to certain reinsurers. Default factors require considerable judgment and are determined using the current financial strength rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions. The total allowance recorded relating to reinsurance recoverables was $55.3 million and $68.1 million at December 31, 2011 and 2010, respectively.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

9. Reinsurance (Continued)

The Company uses an aging analysis to estimate uncollectible reinsurance balances receivable relating to paid losses in addition to recording allowances relating to any specific balances with known collectability issues, irrespective of aging. The balances are aged from the date the expected recovery was billed to the reinsurer. Provisions are applied at specified percentages of the outstanding balances based upon the aging profile. Allowances otherwise required as a result of the aging process may not be recorded to the extent that specific facts and circumstances exist that lead management to believe that amounts will ultimately be collectible. The total allowance recorded relating to reinsurance balances receivable was $43.9 million and $53.8 million at December 31, 2011 and 2010, respectively.

At December 31, 2011, the use of different assumptions within the model could have a material effect on the bad debt provision reflected in the Company s Consolidated Financial Statements. To the extent the creditworthiness of the Company s reinsurers was to deteriorate due to an adverse event affecting the reinsurance industry, such as a large number of major catastrophes, actual uncollectible amounts could be significantly greater than the Company s bad debt provision. Such an event could have a material adverse effect on the Company s financial condition, results of operations, and cash flows.

Approximately 92.2% of the total unpaid loss and loss expense recoverable and reinsurance balances receivable (net of collateral held) outstanding at December 31, 2011 was due from reinsurers with a financial strength rating of A or better. The following is an analysis of the total recoverable and reinsurance balances receivable at December 31, 2011, by reinsurers owing 3% or more of such total:

Name of reinsurer	Reinsurer Financial Strength Rating	% of total
Munich Reinsurance Company	AA-/Stable	22.8%
Swiss Reinsurance Company	AA-/Stable	12.2%
Swiss Re Europe S.A.	AA-/Stable	5.1%
Transatlantic Reinsurance Company	A+/Stable	3.7%
Everest Reinsurance Company	A+/Stable	3.0%

The following table sets forth the ratings profile of the reinsurers that support the unpaid loss and loss expense recoverable and reinsurance balances receivable:

Reinsurer Financial Strength Rating	% of total
AAA	1.3%
AA	58.4%
A	32.3%
BBB	0.4%
BB and below	0.1%
Captives	4.8%
Not Rated	0.2%
Other	2.5%
Total	100.0%

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses

Unpaid losses and loss expenses are comprised of:

Year Ended December 31 *(U.S. dollars in thousands)*	2011	2010
Reserve for reported losses and loss expenses	$ 8,153,585	$ 8,510,605
Reserve for losses incurred but not reported	12,460,316	12,021,002
Unpaid losses and loss expenses	$ 20,613,901	$ 20,531,607

Net losses and loss expenses incurred are comprised of:

Year Ended December 31 *(U.S. dollars in thousands)*	2011	2010	2009
Loss and loss expenses payments	$ 4,911,737	$ 4,309,523	$ 5,138,951
Change in unpaid losses and loss expenses	260,631	(141,589)	(1,148,495)
Change in unpaid losses and loss expenses recoverable	(28,442)	(117,120)	441,397
Paid loss recoveries	(1,065,535)	(839,014)	(1,263,016)
Net losses and loss expenses incurred	$ 4,078,391	$ 3,211,800	$ 3,168,837

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

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

Unpaid losses and loss expenses at end of year	$ 20,613,901	$ 20,531,607	$ 20,823,524

(a) Current year net losses incurred

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

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses (Continued)

(a) Current year net losses incurred (Continued)

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

(b) Prior year net losses incurred

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

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

The significant developments in prior year loss reserve estimates for each of the years indicated within the Company s Insurance and Reinsurance segments are discussed below.

Insurance Segment

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

(U.S. dollars in millions)	2011	2010	2009
Property	$ (8.9)	$ (23.5)	$ (50.7)
Casualty and Professional	(47.1)	(105.2)	(41.0)
Specialty and Other	(20.5)	1.3	28.8
Total	$ (76.5)	$ (127.4)	$ (62.9)

Net favorable prior year reserve development for the Insurance segment of $76.5 million (corresponding gross development was $23.1 million unfavorable) for the year ended December 31, 2011 and was mainly attributable to the following:

For property lines, net prior year development during the year was $8.9 million favorable as a result of better than expected reported loss activity mainly for the 2010 accident year of $22.6 million for the international property book of business for the non-catastrophe exposures, partially offset by adverse development in the international construction ($5.0 million) and Bermuda property ($4.6 million) books of business (also primarily attributable to the 2010 accident year) for non-catastrophe exposures, and an increase in the reinsurance bad debt reserve ($2.8 million).

For casualty lines, net prior year development during the year was $40.5 million unfavorable (gross unfavorable of $158.5 million) mainly related to adverse development on large excess casualty claims associated with the Deepwater Horizon event in the 2010 accident year totaling $135.6 million gross and $33.4 million net. In addition, $150.0 million gross and $65.0 million net excess casualty IBNR reserves were reallocated to the 2010 accident year in respect of Deepwater Horizon exposures. These IBNR movements were entirely offset by reserve reductions in older accident years. This activity largely explains the difference between the gross and net prior year development for the Insurance segment.

Furthermore, there was modest adverse loss experience in the workers compensation profiles in the U.S. risk managment ($7.4 million) and U.S. middle market ($2.6 million) books of business spread across the 2004 to 2010 accident years. These were partially offset by the continued benign large loss experience in primary casualty for the 2002 and prior accident years.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses (Continued)

(b) Prior year net losses incurred (Continued)

For professional lines, the net prior year development during the year was $87.5 million favorable.

The core professional business benefited from releases in reserves for clash losses totaling $88.5 million. These were comprised of releases of $45.3 million for the 2006 and prior report years reflecting favorable development across these years and $54.3 million for report year 2010 to reflect the limited clash events in that year, partially offset by a modest strengthening of $11.1 million for the 2007 to 2009 report years. The core professional business also benefited from a $98.7 million favorable movement excluding clash due to better than expected incurred activity mainly in the 2007 and prior report years.

There was a strengthening in the U.S. Private Commercial business of $29.2 million reflecting worse than expected incurred activity primarily in the 2010 report year.

There was a $37.5 million strengthening in the Design portfolio covering architects and engineers professional liability across the 2004 to 2010 report years driven by worse than expected reported loss experience.

The Select business portfolio, which offers lawyers, real estate and miscellaneous professional liability to small and midsize firms in the U.S., had strengthening of $17.5 million due to worse than expected reported loss experience mainly in the 2009 and 2010 report years.

Finally, there was strengthening of unallocated loss adjustment expense reserves across all professional lines totaling $12.9 million.

For specialty and other lines, net prior year development during the year was $20.5 million favorable mainly due to better than expected reported loss experience for non-catastrophe exposures in several books of business, including aerospace ($20.8 million), specie ($7.9 million), international environmental ($7.1 million), marine ($16.9 million) and discontinued lines ($7.8 million). In addition, there was favorable development from better than expected reported loss experience in the marine book of business for catastrophe exposures of $9.7 million and a decrease in the reinsurance bad debt reserve of $8.3 million, which were partially offset by adverse development in the excess and surplus lines ($27.7 million) and programs ($7.1 million) books of business and adverse development in the run-off surety book of business of $20.9 million predominantly relating to one discontinued program.

Net favorable prior year reserve development for the Insurance segment of $127.4 million for the year ended December 31, 2010 was mainly attributable to the following:

For property lines, net prior year development during the year was $23.5 million favorable due mainly to lower than expected actual losses for non-catastrophe exposures for North America P&C and International P&C business.

For casualty lines, net prior year development during the year was $13.4 million unfavorable due mainly to a $45.1 million strengthening in the U.S. risk management lines, where there has been higher than expected actual losses and reserve assumptions have been revised to give greater weight to actual experience relative to industry benchmarks. The unfavorable development was partially offset by a $26.0 million decrease in the uncollectible reinsurance reserve from reduced exposures and lower estimated risk levels from the Swiss operations. On a gross basis, the excess casualty lines have experienced higher than expected actual losses which have only been partially offset by lower than expected actual losses in the primary casualty lines. However, the gross deterioration in excess casualty was heavily ceded so that on a net basis the strengthening in excess casualty has been almost entirely offset by the release in primary casualty.

For professional lines, net prior year development was $118.6 million favorable. This was driven by lower than expected actual losses in the core U.S. professional business ($89.8 million mainly from report years 2007 and prior) and International ($41.1 million in report year 2006) lines, favorable reserve development in Bermuda errors and omissions lines ($57.2 million for report years 2003 and prior), and favorable Clash development ($28.2 million from report years 2006 and prior). This was partially offset by higher than expected actual losses in the U.S. Private Commercial lines ($63.7 million), and in the small to midsize professional services lines, in particular in the miscellaneous professionals ($21.8 million), architects and engineers ($6.2 million), and real estate ($5.5 million) books.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses (Continued)

(b) Prior year net losses incurred (Continued)

For specialty and other lines, net prior year development was $1.3 million unfavorable due mainly to an unfavorable settlement in the surety lines ($40.4 million), higher than expected actual losses in the environmental lines ($15.5 million), and an unfavorable commutation in the financial lines ($9.1 million). This was mostly offset by lower than expected actual losses in the aerospace ($32.9 million), marine ($7.2 million), specie ($5.5 million) and equine ($3.1 million) lines as well as a reduction in the provision for unrecoverable reinsurance due to reduced exposures and lower estimated risk levels from the London Market operations ($13.1 million).

Net favorable prior year reserve development for the Insurance segment of $62.9 million for the year ended December 31, 2009 was mainly attributable to the following:

For property lines, net prior year development during the year was $50.7 million favorable largely as a result of a lower than expected level of attritional non-catastrophe claims across older accident years as well as reserve releases in the 2008 European general property portfolio due to lower than expected reported loss activity. Prior year catastrophe loss estimates remained stable.

For casualty lines, net prior year development during the year was $29.4 million unfavorable due to reserve strengthening on the European excess lines for accident years 2000 to 2004, and the recognition of potential excess casualty exposures on the discontinued casualty lines. Offsetting this reserve strengthening were reserve releases from the casualty primary business due to better than expected loss activity from the more recent accident years, and U.S. risk management lines due to greater reliance on actual loss experience over initial target loss ratios.

For professional lines, net prior year development was $70.4 million favorable, primarily as a result of lower incurred activity than expected based on the Company s prior valuation in global D&O lines, primarily for underwriting years 2002 to 2006. This release was partially offset by strengthening of global E&O reserves primarily in the 2000 and 2001 years due to large claims. In addition, there was a reallocation of subprime and related credit crisis reserves from the 2007 to 2008 report year to better reflect the indications of our latest exposure-based reserve analysis for these years.

For specialty and other lines, net prior year adverse development was $28.8 million due in part to a deterioration in environmental lines but mainly from discontinued specialty lines, specifically, for surety to reflect our assessment of the potential impact of the economic downturn on ultimate loss activity, the Lloyd s Accident & Health book where incurred development was higher than implied by the Company s selected benchmarks and the resulting lengthening of loss reporting patterns, and political risks where there was reserve strengthening on a specific potential claim. Offsetting the adverse development was favorable reserve development on the aerospace and marine and offshore energy lines due to better than expected activity and an update of development assumptions to reflect recent historical experience.

There is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on the Company s historical results.

Reinsurance Segment

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

(U.S. dollars in millions)	2011	2010	2009
Property and other short-tail lines	$ (64.3)	$ (145.8)	$ (142.5)
Casualty and other	(144.1)	(99.7)	(79.3)
Total	$ (208.4)	$ (245.5)	$ (221.8)

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses (Continued)

(b) Prior year net losses incurred (Continued)

Net favorable prior year reserve development for the Reinsurance segment of $208.4 million for the year ended December 31, 2011 was mainly attributable to the following:

Net favorable prior year development of $64.3 million for the short-tailed lines in the year ended December 31, 2011 and details of these by specific lines are as follows:

For property catastrophe lines, net prior year development during the year was $37.3 million favorable with the main components of this being better than expected loss development of $11.0 million from several European windstorm losses and $8.0 million from Hurricanes Katrina and Rita.

For property other lines, net prior year development during the year was $40.5 million favorable as a result of lower than expected reported losses across most lines of business and most underwriting years with the exception of one cedant in Latin America.

For marine and aviation lines, net prior year development during the year was $13.5 million unfavorable primarily due to reported claim development being above expectations mainly in marine lines of business.

Net favorable prior year development of $144.1 million for the long-tailed lines for the year ended December 31, 2011 and details of these by specific lines are as follows:

For casualty lines, net prior year development during the year was $109.4 million in favorable development primarily related to $56.0 million in better than expected claim activity in North America, $32.1 million in Europe and $20.0 million related to favorable development on Enron-related professional liability claims. The favorable development is primarily for the 1999 to 2006 underwriting years.

For other lines, net prior year development during the year was $34.7 million favorable due to reserve releases on whole account treaties written on Lloyd s syndicates for the 2008 underwriting year as well as releases on large losses and trade credit.

Net favorable prior year reserve development for the Reinsurance segment of $245.5 million for the year ended December 31, 2010 was mainly attributable to the following:

Net favorable prior year development of $145.8 million for the short-tailed lines in the year ended December 31, 2010 and details of these by specific lines are as follows:

$35.6 million in favorable property catastrophe development primarily due to better than expected activity in underwriting years 2007 to 2009, lowering of expected loss ratios to attritional levels on the 2009 underwriting year and reserve releases related to European windstorms of $7.2 million and Hurricane Katrina of $3.8 million.

$87.4 million in favorable property other releases driven by $50.7 million of releases from U.S. exposures for most underwriting years including $7.9 million from reduced exposures relating to a U.S agricultural program from underwriting year 2009, $20.0 million in releases from Latin America proportional exposures primarily from 2007 to 2009 underwriting years and $16.7 million in releases from Europe and Asia Pacific exposures from most underwriting years.

$22.8 million in marine and aviation lines due to favorable marine development of $10.9 million and favorable aviation development of $11.9 million due to better than expected activity in most underwriting years.

10. Losses and Loss Expenses (Continued)

(b) Prior year net losses incurred (Continued)

Net favorable prior year development of $99.7 million for the long-tailed lines for the year ended December 31, 2010 and details of these by specific lines are as follows:

$25.2 million in favorable casualty and professional development attributable to $33.0 million in releases due to settlements related to Enron losses, $21.6 million in releases mainly due to U.S. professional exposures in underwriting years 2005 and prior, $11.9 million primarily due to releases related to revision of European loss development factors and initial expected loss ratios, $7.1 million related to releases from run-off of Australia casualty exposures in underwriting years 2005 and prior offset by adverse development of $43.0 million related to Italian hospital medical malpractice exposures written through a Lloyd s syndicate and adverse development of $5.4 million related to European Financial Institution exposures in underwriting years 2002 and 2004.

$74.5 million in favorable other lines development primarily driven by $42.1 million in favorable development from whole account contracts written in Lloyd s syndicates of which $36.1m in releases related to reinsurance to close (RITC) in years of account 2007 and prior and $6.0 million due to better than expected activity in underwriting years 2008 and 2009.Contributions also from North American bond run-off exposures due to better than expected activity in underwriting years 2006 and prior resulting in releases of $12.6 million, a reduction of $7.5 million on one political risk loss, Latin America Surety releases of $5.6 million related to better than expected loss experience across most underwriting years, $3.7 million in relation to one specific contract commutation and $3.0 million in releases primarily due to favorable activity in European trade credit run-off exposures in most prior underwriting years.

Net favorable prior year reserve development for the Reinsurance segment of $221.8 million for the year ended December 31, 2009 was mainly attributable to the following:

Net favorable prior year development of $142.5 million for the short-tailed lines in the year ended December 31, 2009 and details of these by specific lines are as follows:

$46.2 million in favorable property catastrophe development due to lower than expected loss development, particularly on the 2008 underwriting year and $12.3 million in reserve reductions for several 2005 natural catastrophe events including European floods, windstorm Erwin and California wildfires.

$88.8 million in favorable development due primarily to lower than expected claim emergence from underwriting years 2005 to 2008 in Latin America ($27.5 million), Europe ($21.6 million), Bermuda ($20.6 million) and U.S. ($13.8 million).

$7.5 million in marine and aviation lines due to lower than expected claim emergence in the European marine book for underwriting years 2007 and 2008 offset by minimal net reserve increases on the aviation book.

Net favorable prior year development of $79.3 million for the long-tailed lines for the year ended December 31, 2009 and details of these by specific lines are as follows:

$21.0 million in favorable casualty development related primarily to the European General Liability and U.K. Motor portfolios in underwriting years 2004 to 2007.

$40.7 million in favorable professional development due primarily to U.S. exposures for underwriting years 2002 and prior in addition to professional indemnity exposures underwritten in Europe in years 2006 and prior.

$17.6 million in favorable development in non-casualty long tail lines largely in Latin America due to favorable emergence from surety exposures.

There is no assurance that conditions and trends that have affected the development of liabilities in the past will continue. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on the Company s historical results.

10. Losses and Loss Expenses (Continued)

(c) Exchange rate effects

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

(d) Net paid losses

Total net paid losses were $3.8 billion, $3.5 billion and $3.9 billion in each of 2011, 2010 and 2009, respectively.

(e) Other loss information

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

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

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

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

The nature of the Company s high excess of loss liability and catastrophe business can result in loss events that are both irregular and significant. Similarly, adjustments to reserves for individual years can be irregular and significant. Such adjustments are part of the normal course of business for the Company. Conditions and trends that have affected development of liability in the past may not continue in the future. Accordingly, it is inappropriate to extrapolate future redundancies or deficiencies based upon historical experience.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

10. Losses and Loss Expenses (Continued)

(f) Asbestos and Environmental Related Claims

The Company s reserving process includes a continuing evaluation of the potential impact on unpaid liabilities from exposure to asbestos and environmental claims, including related loss adjustment expenses. Liabilities are established to cover both known and incurred but not reported claims.

A reconciliation of the opening and closing unpaid losses and loss expenses related to asbestos and environmental exposure claims for the years indicated is as follows:

Year Ended December 31,	2011	2010	2009
(U.S. dollars in thousands)			
Net unpaid losses and loss expenses at beginning of year	$ 84,075	$ 100,922	$ 111,860
Net incurred losses and loss expenses	(41)	(130)	(312)
Less net paid losses and loss expenses	6,256	16,718	10,626
Net increase (decrease) in unpaid losses and loss expenses	(6,297)	(16,848)	(10,938)
Net unpaid losses and loss expenses at end of year	77,778	84,075	100,922
Unpaid losses and loss expenses recoverable at end of year	134,323	142,037	151,963
Gross unpaid losses and loss expenses at end of year	$ 212,101	$ 226,112	$ 252,885

Reserves for incurred but not reported losses, net of reinsurance, included in the above table were $47.2 million, $54.9 million and $68.5 million in 2011, 2010 and 2009, respectively. Unpaid losses recoverable are net of potential uncollectible amounts.

As of December 31, 2011, the Company had 1,038 open claim files for potential asbestos exposures and 362 open claim files for potential environmental exposures. Approximately 43%, 44% and 50% of the open claim files are due to precautionary claim notices in 2011, 2010 and 2009, respectively. Precautionary claim notices are submitted by the ceding companies in order to preserve their right to receive coverage under the reinsurance contract.

Such notices do not contain an incurred loss amount to the Company. The development of the number of open claim files for potential asbestos and environmental claims is as follows:

	Asbestos Claims	Environmental Claims
Total number of claims outstanding at December 31, 2008	1,546	548
New claims reported in 2009	221	38
Claims resolved in 2009	(330)	(102)
Total number of claims outstanding at December 31, 2009	1,437	484
New claims reported in 2010	125	31
Claims resolved in 2010	(362)	(98)
Total number of claims outstanding at December 31, 2010	1,200	417
New claims reported in 2011	106	36
Claims resolved in 2011	(268)	(91)

Total number of claims outstanding at December 31, 2011	1,038	362

10. Losses and Loss Expenses (Continued)

(f) Asbestos and Environmental Related Claims (Continued)

The Company s reserving process includes a continuing evaluation of the potential impact on unpaid liabilities from exposure to asbestos and environmental claims, including related loss adjustment expenses. Liabilities are established to cover both known and incurred but not reported claims.

The Company s exposure to asbestos and environmental claims arises from the following three sources:

(1) Reinsurance contracts written, both on a proportional and excess basis, after 1972. The Company discontinued writing contracts with these exposures in 1985. Business written was across many different policies, each with a relatively small contract limit. The Company s reported asbestos claims relate to both traditional products and premises and operations coverage.

(2) Winterthur business of Winterthur purchased by the Company from AXA Insurance (formerly Winterthur Swiss Insurance Company) in 2001. AXA reimburses the Company for asbestos claim payments pursuant to the Sale and Purchase Agreement.

(3) During 2006, the Company acquired $40.2 million in losses through a loss portfolio transfer contract of which $18.3 million in losses related to asbestos and environmental claims. Given the terms of the policy, the combined aggregate limit on the total acquired reserves is limited to $60.0 million, not including coverage for claims handling costs over a defined period.

The estimation of loss and loss expense liabilities for asbestos and environmental exposures is subject to much greater uncertainty than is normally associated with the establishment of liabilities for certain other exposures due to several factors, including: (i) uncertain legal interpretation and application of insurance and reinsurance coverage and liability; (ii) the lack of reliability of available historical claims data as an indicator of future claims development; (iii) an uncertain political climate which may impact, among other areas, the nature and amount of costs for remediating waste sites; and (iv) the potential of insurers and reinsurers to reach agreements in order to avoid further significant legal costs. Due to the potential significance of these uncertainties, the Company believes that no meaningful range of loss and loss expense liabilities beyond recorded reserves can be established. As the Company s net unpaid loss and loss expense reserves related to asbestos and environmental exposures are less than 1% of the total net reserves at December 31, 2011 and 2010, further adverse development is not expected to be material to the Company s overall net loss reserves. The Company believes it has made reasonable provision for its asbestos and environmental exposures and is unaware of any specific issues that would significantly affect its estimate for loss and loss expenses.

11. Deposit Liabilities

The Company has entered into certain insurance and reinsurance policies that transfer insufficient risk under GAAP to be accounted for as insurance or reinsurance transactions and are recognized as deposits. These structured property and casualty agreements have been recorded as deposit liabilities and are initially matched by an equivalent amount of investments. The Company has investment risk related to its ability to generate sufficient investment income to enable the total invested assets to cover the payment of the ultimate liability. See Note 5, Investments, for further information relating to the Company s net investment income as well as realized and unrealized investment (losses) gains. Each deposit liability accrues at a rate equal to the internal rate of return of the payment receipts and obligations due during the life of the agreement. Where the timing and/or amount of future payments are uncertain, cash flows reflecting the Company s actuarially determined best estimates are utilized. Deposit liabilities are initially recorded at an amount equal to the assets received.

Total deposit liabilities for the years ended December 31, 2011 and 2010 were $1.6 billion and $1.7 billion, respectively. Interest expense of $51.3 million, $54.4 million and $36.2 million was recorded related to the accretion of deposit liabilities for the years ended December 31, 2011, 2010 and 2009, respectively.

12. Future Policy Benefit Reserves

The Company enters into long duration contracts that subject the Company to mortality and morbidity risks and which were accounted for as life premiums earned. Future policy benefit reserves were established using appropriate assumptions for investment yields, mortality, and expenses, including a provision for adverse deviation. The average interest rate used for the determination of the future policy benefits for these contracts was 4.5% at December 31, 2011 and 2010. Total future policy benefit reserves for the year ended December 31, 2011 and 2010 were $4.8 billion and $5.1 billion, respectively. The decrease of $232.6 million in the Annuities is mainly due to foreign exchange movements and the usual releases on single premium annuities in line with benefits paid and mortality of underlying policyholders.

Future policy benefit reserves are comprised of the following:

Year ended December 31 *(U.S. dollars in thousands)*	**2011**	**2010**
Traditional Life	$ 812,628	$ 809,776
Annuities	4,032,766	4,265,351
Total future policy benefit reserves	$ 4,845,394	$ 5,075,127

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

13. Notes Payable and Debt and Financing Arrangements

At December 31, the Company s financing structure, which includes senior unsecured notes, bank and loan facilities available from a variety of sources, including commercial banks, and letter of credit facilities was as follows:

(U.S. dollars in thousands)	2011		2010	
	Commitment/ Debt	**In Use/ Outstanding (1)**	**Commitment/ Debt**	**In Use/ Outstanding (1)**
Debt:				
5-year revolver expiring 2012 (2)	$	$	$ 1,000,000	$
4-year revolver expiring 2015 (3)	1,000,000			
6.50% Guaranteed Senior Notes due 2012 (4)	600,000	599,971	600,000	599,294
5.25% Senior Notes due 2014	600,000	597,501	600,000	596,579
5.75% Senior Notes due 2021	400,000	395,963		
8.25% Senior Notes due 2021			575,000	572,538
6.375% Senior Notes due 2024	350,000	348,592	350,000	348,482
6.25% Senior Notes due 2027	325,000	322,591	325,000	322,435
Total debt	$ 3,275,000	$ 2,264,618	$ 3,450,000	$ 2,439,328
Adjustment to carrying value impact of fair value hedge		10,709		17,675
Carrying Value	$ 3,275,000	$ 2,275,327	$ 3,450,000	$ 2,457,003
Letters of Credit:				
5 facilities total	$ 4,000,000	$ 1,871,192	$ 5,000,114	$ 2,395,242

(1) In Use and Outstanding data represent December 31, 2011 and 2010 accreted values.
(2) The 2012 5-year revolving credit facilities shared a $1 billion revolving credit sub-limit. This facility was terminated in December 2011 in connection with entering into new credit facilities.
(3) This credit facility has a $1 billion revolving credit sub-limit.
(4) The 6.50% Guaranteed Senior Notes were repaid at maturity on January 15, 2012.

(a) Notes Payable and Debt

All outstanding debt of the Company, noted in the table above, at December 31, 2011 and 2010 was issued by XL-Cayman except for the $600 million par value 6.5% Guaranteed Senior Notes (the XLCFE Notes) which were issued by XL Capital Finance (Europe) plc (XLCFE) and were repaid at maturity on January 15, 2012. Both XL-Cayman and XLCFE are wholly-owned subsidiaries of XL-Ireland. The XLCFE Notes were fully and unconditionally guaranteed by XL Company Switzerland GmbH (XL-Switzerland). The Company s ability to obtain funds from its subsidiaries to satisfy any of its obligations under guarantees is subject to certain contractual restrictions, applicable laws and statutory requirements of the various countries in which the Company operates, including, among others, Bermuda, the United States, Ireland, Switzerland and the U.K. Aggregated required statutory capital and surplus for the principal operating subsidiaries of the Company was $6.7 billion and $6.5 billion at December 31, 2011 and 2010, respectively.

Concurrent with the issuance of ordinary shares and pursuant to the Company s shelf registration statement, the Company, in August 2008, issued 23.0 million 10.75% Equity Security Units (the 10.75% Units) in a public offering in order to fund payments in relation to the Master Commutation Release and Restructuring Agreement, dated July 28, 2008, as amended among XL Insurance (Bermuda) Ltd (XLIB) and affiliates

Syncora Holdings Ltd. and its affiliates (Syncora) and certain of Syncora s credit default swap counterparties (the Master Agreement) and remaining net proceeds were used for general corporate purposes. The Company received approximately $557.0 million in net proceeds from the sale of the 10.75% Units after deducting underwriting discounts. Each 10.75% Unit had a stated amount of $25 and consisted of (a) a purchase contract pursuant to which the holder agreed to purchase, for $25, a variable number of shares of the Company s Ordinary Shares on August 15, 2011 and (b) a one-fortieth, or 2.5%, ownership interest in a senior note issued by the Company due August 15, 2021 with a principal amount of $1,000. The senior notes were pledged by the holders to secure their obligations under the purchase contract.

13. Notes Payable and Debt and Financing Arrangements (Continued)

(a) Notes Payable and Debt (Continued)

The number of shares issued under the purchase contract was contingently adjustable based on, among other things, the share price of the Company on the stock purchase date and the dividend rate of the Company. The Company made quarterly payments at the annual rate of 2.50% and 8.25% under the purchase contracts and senior notes, respectively. For all periods reported, the Company had the right to defer the contract payments on the purchase contract, but not the senior notes, until the stock purchase date. In August 2011, the senior notes were remarketed whereby the interest rate on the senior notes was to be reset in order to generate sufficient remarketing proceeds to satisfy the 10.75% Unit holders obligations under the purchase contracts.

In connection with this transaction, $37.9 million, which is the estimated fair value of the purchase contract, was charged to Additional paid in capital and a corresponding liability was established. Of the $18.0 million total accrued costs associated with the issuance of the 10.75% Units, $14.7 million was charged to Additional paid in capital with the remainder deferred and amortized over the term of the senior debt.

In August 2011, in accordance with the terms of the 10.75% Units, XL-Cayman purchased and retired all of the 8.25% senior notes due August 2021 (the 8.25% Senior Notes) for $575 million in a remarketing. These notes comprised a part of the 10.75% Units. The proceeds from the remarketing were used to satisfy the purchase price for XL-Ireland s ordinary shares issued to holders of the 10.75% Units pursuant to the forward purchase contracts comprising a part of the 10.75% Units. Each forward purchase contract provided for the issuance of 1.3242 ordinary shares of XL-Ireland at a price of $25 per share. The settlement of the forward purchase contracts resulted in XL-Ireland s issuance of an aggregate of 30,456,600 ordinary shares for an aggregate purchase price of $575 million. As a result of the settlement of the forward purchase contracts, the 10.75% Units ceased to exist and are no longer traded on the NYSE.

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

(b) Letter of Credit Facilities and Other Sources of Collateral

The Company has several letter of credit facilities provided on a syndicated and bilateral basis from commercial banks. These facilities are utilized primarily to support non-admitted insurance and reinsurance operations in the U.S. and capital requirements at Lloyd s. The Company s letter of credit facilities and revolving credit facilities at December 31, were as follows:

Year ended December 31 *(U.S. dollars thousands except percentages)*	**2011 (1)**	**2010 (2)**
Revolving credit facilities (3)	$ 1,000,000	$ 1,000,000
Available letter of credit facilities commitment (4)	$ 4,000,000	$ 5,000,114
Available letter of credit facilities in use	$ 1,871,192	$ 2,395,242
Collateralized by certain of the Company s investment portfolio	93.8%	21.1%

(1) At December 31, 2011 there were five available letter of credit facilities.
(2) At December 31, 2010 there were five available letter of credit facilities.
(3) At December 31, 2011 and 2010 the revolving credit facilities were unutilized.
(4) The Company has the option to increase the size of the March 2011 Credit Agreement by an additional $500 million and the size of the facilities under the December 2011 Credit Agreements by an additional $500 million across both such facilities.

13. Notes Payable and Debt and Financing Arrangements (Continued)

(b) Letter of Credit Facilities and Other Sources of Collateral (Continued)

In 2011, the Company and certain of its subsidiaries (i) entered into three new credit agreements, which are described below and provide for an aggregate amount of outstanding letters of credit and revolving credit loans up to $3 billion, subject to certain options to increase the size of the facilities, and (ii) terminated the five-year credit agreement dated June 21, 2007 (the 2007 Credit Agreement), which had provided for an aggregate amount of outstanding letters of credit and revolving credit loans up to $4 billion.

On March 25, 2011, the Company and certain of its subsidiaries entered into a secured credit agreement (the March 2011 Credit Agreement) that currently provides for the issuance of letters of credit of up to $1 billion with the option to increase the size of the facility by an additional $500 million. The commitments under the 2011 Credit Agreement will expire on, and the credit facility is available on a continuous basis until, the earlier of (i) March 25, 2014 and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon an event of default.

In October 2011, the $75,000 letter of credit facility that was supporting a subsidiary of the Company was terminated.

On December 9, 2011, the Company and certain of its subsidiaries entered into (i) a new secured credit agreement (the December 2011 Secured Credit Agreement) and (ii) a new unsecured credit agreement (the December 2011 Unsecured Credit Agreement and together with the December 2011 Secured Credit Agreement, the December 2011 Credit Agreements). In connection with the December 2011 Credit Agreements, the 2007 Credit Agreement was terminated. The March 2011 Credit Agreement continues in force, but was amended to conform certain of its terms to those of the December 2011 Secured Credit Agreement.

The 2007 Credit Agreement had provided for letters of credit and for revolving credit loans of up to $750 million with the aggregate amount of outstanding letters of credit and revolving credit loans thereunder not to exceed $3 billion. At the time at which it was terminated and the December 2011 Credit Agreements became effective, there were no outstanding revolving credit loans under the 2007 Credit Agreement. A portion of the letters of credit outstanding under the 2007 Credit Agreement at the time of its termination were continued under the March 2011 Credit Agreement and the remainder were continued under the December 2011 Credit Agreements.

The December 2011 Secured Credit Agreement provides for issuance of letters of credit up to $650 million. The December 2011 Unsecured Credit Agreement is a $1.35 billion facility that provides for issuance of letters of credit and up to $1 billion of revolving credit loans. The Company has the option to increase the maximum amount of letters of credit available by an additional $500 million across the facilities under the December 2011 Credit Agreements.

The commitments under each December 2011 Credit Agreement expire on, and such credit facilities are available until, the earlier of (i) December 9, 2015 and (ii) the date of termination in whole of the commitments upon an optional termination or reduction of the commitments by the account parties or upon an event of default.

The availability of letters of credit under the December 2011 Secured Credit Agreement and the March 2011 Credit Agreements is subject to a borrowing base requirement, determined on the basis of specified percentages of the face value of eligible categories of assets varying by type of collateral.

On August 3, 2010, a $100 million five-year revolving credit facility expired and was not replaced, and on June 22, 2010, a $2.3 billion five-year letter of credit facility expired and was not replaced.

On December 14, 2009, the £450 million letter of credit facility issued on November 14, 2007 that was supporting the Company s syndicates at Lloyd s of London terminated. This facility was replaced by a $750 million bilateral secured letter of credit facility.

13. Notes Payable and Debt and Financing Arrangements (Continued)

(b) Letter of Credit Facilities and Other Sources of Collateral (Continued)

In addition to letters of credit, the Company has established insurance trusts in the U.S. that provide cedants with statutory relief required under state insurance regulation in the U.S. It is anticipated that the commercial facilities may be renewed on expiry but such renewals are subject to the availability of credit from banks utilized by the Company and may be renewed with materially different terms and conditions. In the event that such credit support is insufficient, the Company could be required to provide alternative security to cedants. This could take the form of additional insurance trusts supported by the Company s investment portfolio or funds withheld using the Company s cash resources. The value of letters of credit required is driven by, among other things, loss development of existing reserves, the payment pattern of such reserves, the expansion of business written by the Company and the loss experience of such business.

In general, all of the Company s bank facilities, indentures and other documents relating to the Company s outstanding indebtedness (collectively, the Company s Debt Documents), as described above, contain cross default provisions to each other and the Company s Debt Documents contain affirmative covenants. These covenants provide for, among other things, minimum required ratings of the Company s insurance and reinsurance operating subsidiaries and the level of secured indebtedness in the future. In addition, generally each of the Company s Debt Documents provide for an event of default in the event of a change of control of the Company or some events involving bankruptcy, insolvency or reorganization of the Company. The Company s credit facilities also contain minimum consolidated net worth covenants.

Under the March 2011 Credit Agreement and December 2011 Credit Agreements, in the event that XL Insurance (Bermuda) Ltd, XL Re Ltd or XL Re Europe Ltd fail to maintain a financial strength rating of at least A from A.M. Best, an event of default would occur.

Given that all of the Company s Debt Documents contain cross default provisions, this may result in all holders declaring such debt due and payable and an acceleration of all debt due under those documents. If this were to occur, the Company may not have funds sufficient at that time to repay any or all of such indebtedness.

In addition, the Company maintains off-balance sheet financing arrangements in the form of a contingent capital facility. For details of this facility, see Note 15, Off-Balance Sheet Arrangements.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments

The Company enters into derivative instruments for both risk management and investment purposes. The Company is exposed to potential loss from various market risks, and manages its market risks based on guidelines established by management and the Risk and Finance Committee. The Company recognizes all derivatives as either assets or liabilities in the balance sheet and measures those instruments at fair value with the changes in fair value of derivatives shown in the consolidated statement of income as net realized and unrealized gains and losses on derivative instruments unless the derivatives are designated as hedging instruments. The accounting for derivatives which are designated as hedging instruments is described in Note 2(h), Significant Accounting Policies Derivative Instruments. The following table summarizes information on the location and gross amounts of derivative fair values contained in the consolidated balance sheet as at December 31, 2011 and 2010:

	December 31, 2011				December 31, 2010			
(U.S. dollars in thousands)	Asset Derivative Notional Amount	Asset Derivative Fair Value (1)	Liability Derivative Notional Amount	Liability Derivative Fair Value (1)	Asset Derivative Notional Amount	Asset Derivative Fair Value (1)	Liability Derivative Notional Amount	Liability Derivative Fair Value (1)
Derivatives designated as hedging instruments:								
Interest rate contracts (2)	$ 156,271	$ 109,761	$	$	$ 161,028	$ 74,368	$	$
Foreign exchange contracts	2,033,428	25,387	457,892	(4,518)	1,850,092	43,226	244,731	(12,161)
Total derivatives designated as hedging instruments	$ 2,189,699	$ 135,148	$ 457,892	(4,518)	$ 2,011,120	$ 117,594	$ 244,731	(12,161)
Derivatives not designated as hedging instruments:								
Investment Related Derivatives:								
Interest rate exposure	$ 70,978	$ 1,946	$ 55,033	$ (43)	$ 117,689	$ 281	$ 41,063	$
Foreign exchange exposure	232,422	3,759	384,592	(11,737)	82,395	1,377	272,724	(6,329)
Credit exposure	172,500	5,271	449,513	(13,986)	128,450	8,143	532,000	(5,295)
Financial market exposure	19,869	615	14,321		135,912	705	4,575	(27)
Commodity futures	4,005							
Financial Operations Derivatives: (3)								
Credit exposure			81,678	(10,288)			246,292	(25,887)
Other Non-Investment Derivatives:								
Contingent capital facility					350,000			
Guaranteed minimum income benefit contract			78,777	(22,490)			80,025	(21,190)
Modified coinsurance funds withheld contract			77,200				72,509	

Total derivatives not designated as hedging instruments	$ 499,774	$ 11,591	$ 1,141,114	$ (58,544)	$ 814,446	$ 10,506	$ 1,249,188	$ (58,728)

(1) Derivative instruments in an asset or liability position are included within Other Assets or Other Liabilities, respectively, in the Balance Sheet.

(2) At December 31, 2011 and December 31, 2010, the Company held net cash collateral related to these derivative assets of $77.1 million and $23.0 million, respectively. The collateral balance is included within cash and cash equivalents and the corresponding liability to return the collateral has been offset against the derivative asset within the balance sheet as appropriate under the netting agreement.

(3) Financial operations derivatives represent interests in variable interest entities as described in Note 16, Variable Interest Entities.

(a) Derivative Instruments Designated as Fair Value Hedges

The Company designates certain of its derivative instruments as fair value hedges or cash flow hedges and formally and contemporaneously documents all relationships between the hedging instruments and hedged items and links the hedging derivative to specific assets and liabilities. The Company assesses the effectiveness of the hedge, both at inception and on an on-going basis and determines whether the hedge is highly effective in offsetting changes in fair value or cash flows of the linked hedged item.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments (Continued)

(a) Derivative Instruments Designated as Fair Value Hedges (Continued)

At December 31, 2011 and 2010, a portion of the Company s liabilities are hedged against changes in the applicable designated benchmark interest rate. Interest rate swaps are also used to hedge the changes in fair value of certain fixed rate liabilities and fixed income securities due to changes in the designated benchmark interest rate. In addition, the Company utilizes foreign exchange contracts to hedge the fair value of certain fixed income securities as well as to hedge certain net investments in foreign operations.

The following table provides the total impact on earnings relating to derivative instruments formally designated as fair value hedges along with the impacts of the related hedged items for the years ended December 31, 2011, 2010 and 2009:

		Hedged Items Amount of Gain/(Loss) Recognized in Income Attributable to Risk			
Derivatives Designated as Fair Value Hedges: *(U.S. dollars in thousands)*	**Gain/(Loss) Recognized in Income on Derivative**	**Deposit Liabilities**	**Fixed Maturity Investments**	**Notes Payable and Debt**	**Ineffective Portion of Hedging Relationship Gain/(Loss)**
December 31, 2011					
Interest rate exposure	$ 25,680				
Foreign exchange exposure	15,135				
Total	$ 40,815	$ (27,391)	$ (15,299)	$	$ (1,875)
December 31, 2010					
Interest rate exposure	$ 94,068				
Foreign exchange exposure	19,856				
Total	$ 113,924	$ (84,393)	$ (27,266)	$ (15,940)	$ (13,675)
December 31, 2009					
Interest rate exposure	$ (212,215)				
Foreign exchange exposure	7,526				
Total	$ (204,689)	$ 201,398	$ 1,711	$ 1,206	$ (374)

The gains (losses) recorded on both the derivatives instruments and specific items designated as being hedged as part of the fair value hedging relationships outlined above are recorded through net realized and unrealized gains (losses) on derivative instruments in the income statement along with any associated ineffectiveness in the relationships. In addition, the periodic coupon settlements relating to the interest rate swaps are recorded as adjustments to net investment income for the hedges of fixed maturity investments and as adjustments to interest expense for the hedges of deposit liabilities and notes payable and debt.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments (Continued)

(a) Derivative Instruments Designated as Fair Value Hedges (Continued)

The periodic coupon settlements resulted in an increase to net investment income of nil and $2.3 million for years ended December 31, 2011 and 2010, respectively.

The periodic coupon settlements also resulted in decreases to interest expense of $10.2 million and $49.8 million for years ended December 31, 2011 and 2010, respectively.

Settlement of Fair Value Hedges

During the year ended December 31, 2010, the Company settled the interest rate contracts designated as fair value hedges of certain issues of the Company s notes payable and debt and also settled three interest rate contracts designated as fair value hedges of certain of the Company s deposit liability contracts. The cumulative increase recorded to the carrying value of the hedged notes payable and debt, and the deposit liability contracts, representing the effective portion of the hedging relationship, is amortized through interest expense over the remaining term of the debt and deposit liability contracts, respectively. A summary of the fair value hedges that were settled in 2010 and their results during the years ended December 31, 2011 and 2010, including the gains on settlements is shown below:

Settlement of Fair Values Hedges Summary:

	Fair Value Hedges Notes Payable and Debt (1)		Fair Value Hedges Deposit Liabilities (2)	
(U.S. dollars in thousands except years)	**2011**	**2010**	**2011**	**2010**
Gain on settlements of fair value hedges	$	$ 21,624	$	$ 149,485
Cumulative reduction to interest expense	$ 10,915	$ 3,948	$ 9,376	$ 1,915
Remaining balance	$ 10,709	$ 17,675	140,109	147,570
Weighted average years remaining to maturity	2.5 years	3.2 years	30.7 years	36.3 years

(1) Two fair value hedges of certain issues of the Company s notes payable and debt were settled on June 7, 2010.
(2) Three fair value hedges of certain of the Company s deposit liability contracts were settled on October 27, 2010.

(b) Derivative Instruments Designated as Hedges of the Net Investment in a Foreign Operation

The Company utilizes foreign exchange contracts to hedge the fair value of certain net investments in foreign operations. During 2011 and 2010, the Company entered into foreign exchange contracts that were formally designated as hedges of the investment in foreign subsidiaries with the majority of which have functional currencies of either U.K. sterling or the Euro. There was no ineffectiveness resulting from these transactions.

The following table provides the weighted average U.S. dollar equivalent of foreign denominated net assets which were hedged and the resultant gain (loss) which was recorded in the cumulative translation adjustment account within AOCI for the years ended December 31, 2011 and 2010.

Year ended December 31

(U.S. dollars in thousands)	**2011**	**2010**
Weighted average of U.S. dollar equivalent of foreign denominated net assets	$ 1,733,555	$ 833,491
Derivative gains (losses) (1)	$ 36,836	$ (16,526)

(1) Derivative gains (losses) from derivative instruments designated as hedges of the net investment in a foreign operation are recorded in the cumulative translation adjustment account within AOCI for each period.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments (Continued)

(c) Derivative Instruments Not Formally Designated As Hedging Instruments

The following table provides the total impact on earnings relating to derivative instruments not formally designated as hedging instruments under authoritative accounting guidance. The impacts are all recorded through Net realized and unrealized gains (losses) on derivatives in the income statement for years ended December 31, 2011, 2010 and 2009:

Derivatives not designated as hedging instruments:
Year Ended December 31

(U.S. dollars in thousands)	2011	2010	2009
Investment Related Derivatives:			
Interest rate exposure	$ (1,021)	$ 3,511	$ 9,124
Foreign exchange exposure	(302)	(15,642)	9,387
Credit exposure	(16,527)	(6,315)	(51,579)
Financial market exposure	(4,827)	2,125	3,359
Commodity exposure	(304)		
Financial Operations Derivatives:			
Credit exposure	16,976	(7,281)	(2,667)
Other Non-Investment Derivatives:			
Contingent capital facility	(6,068)	(8,233)	(8,132)
Guaranteed minimum income benefit contract	(1,300)	1,719	4,644
Modified coinsurance funds withheld contract	4,510	9,948	(388)
Weather and Energy Derivatives:			
Structured weather risk management products			2,979
Total derivatives not designated as hedging instruments	(8,863)	(20,168)	(33,273)
Amount of gain (loss) recognized in income from ineffective portion of fair value hedges	(1,875)	(13,675)	(374)
Net realized and unrealized gains (losses) on derivative instruments	$ (10,738)	$ 33,843	$ (33,647)

The Company s objectives in using these derivatives are explained below.

(c)(i) Investment Related Derivatives

The Company, either directly or through its investment managers, may use derivative instruments within its investment portfolio, including interest rate swaps, inflation swaps, credit derivatives (single name and index credit default swaps), options, forward contracts and financial futures (foreign exchange, bond and stock index futures), primarily as a means of economically hedging exposures to interest rate, credit spread, equity price changes and foreign currency risk or in limited instances for investment purposes. The Company is exposed to credit risk in the event of non-performance by the counterparties under any swap contracts although the Company generally seeks to use credit support arrangements with counterparties to help manage this risk.

Investment Related Derivatives Interest Rate Exposure

The Company utilizes risk management and overlay strategies that incorporate the use of derivative financial instruments, primarily to manage its fixed income portfolio duration and exposure to interest rate risks associated with certain of its assets and liabilities primarily in relation to certain legacy other financial lines and structured indemnity transactions. The Company uses interest rate swaps to convert certain liabilities from a fixed rate to a variable rate of interest and may also use them to convert a variable rate of interest from one basis to another.

Investment Related Derivatives Foreign Exchange Exposure

The Company uses foreign exchange contracts to manage its exposure to the effects of fluctuating foreign currencies on the value of certain of its foreign currency fixed maturities primarily within its Life operations portfolio. These contracts are not designated as specific hedges for financial reporting purposes and therefore, realized and unrealized gains and losses on these contracts are recorded in income in the period in which they occur. These contracts generally have maturities of twelve months or less.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments (Continued)

(c)(i) Investment Related Derivatives (Continued)

In addition, certain of the Company s investment managers may, subject to investment guidelines, enter into forward contracts where potential gains may exist. The Company has exposure to foreign currency exchange rate fluctuations through its operations and in its investment portfolio.

Investment Related Derivatives Credit Exposure

Credit derivatives are purchased within the Company s investment portfolio in the form of single name and basket credit default swaps, which are used to mitigate credit exposure through a reduction in credit spread duration (i.e., macro credit strategies rather than single-name credit hedging) or exposure to selected issuers, including issuers that are not held in the underlying bond portfolio.

Investment Related Derivatives Financial Market Exposure

Stock index futures may be purchased within the Company s investment portfolio in order to create synthetic equity exposure and to add value to the portfolio with overlay strategies where market inefficiencies are believed to exist. The Company previously wrote a number of resettable strike swaps contracts relating to an absolute return index and diversified basket of funds. These resettable strike swaps have all expired at December 31, 2011. From time to time, the Company may enter into other financial market exposure derivative contracts on various indices including, but not limited to, inflation and commodity contracts.

(c)(ii) Financial Operations Derivatives Credit Exposure

At December 31, 2011 and 2010, the Company held two credit derivative exposures which were written as part of the Company s previous financial lines business and are outside of the Company s investment portfolio. These two contracts consisted of: one that provides credit protection on the senior tranches of a structured finance transaction, and the other, a European project finance loan participation. An aggregate summary of these credit derivative exposures for the years ended December 31 is as follows:

Financial Operations Derivatives Credit Exposure Summary:
Year ended December 31,

(U.S. dollars in thousands except term to maturity)	2011	2010
Principal outstanding	$ 78,425	$ 226,429
Interest outstanding	3,253	19,863
Aggregate outstanding exposure	$ 81,678	$ 246,292
Total liability recorded	$ 10,288	$ 25,887
Weighted average contractual term to maturity	4.6 years	5.3 years
Underlying obligations average credit rating	BB	B-

The credit protection related to the structured finance transaction is a credit default swap that was executed in 2000. The underlying collateral is predominantly securitized pools of leveraged loans and bonds. The transaction is in compliance with most of the coverage tests except the mezzanine overcollateralization tests. As a result, both interest and principal proceeds are currently redirected to amortize the most senior notes, which reduces the Company s exposure sooner than originally anticipated. As a result, in 2011 the Company s exposure to this transaction reduced by $147.8 million. Management continues to monitor its underlying performance. The European project finance loan participation benefits from an 80% deficiency guarantee from the German state and federal governments.

At December 31, 2011 and 2010, there were no reported events of default on these obligations. Credit derivatives are recorded at fair value, which is determined using models developed by the Company and is dependent upon a number of factors, including changes in interest rates, future default rates, credit spreads, changes in credit quality, future expected recovery rates and other market factors. The change resulting from movements in credit and credit quality spreads is unrealized as the credit derivatives are not traded to realize this resultant value.

186

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

14. Derivative Instruments (Continued)

(c)(iii) Other Non-Investment Derivatives

The Company entered into derivatives as part of its contingent capital facility, which was terminated during 2011 as discussed in Note 15, Off-Balance Sheet Arrangements, including put options, interest rate swaps, and asset return swaps. These derivatives are recorded at fair value with changes in fair value recognized in earnings.

The Company also has derivatives embedded in certain reinsurance contracts. For a particular life reinsurance contract, the Company pays the ceding company a fixed amount equal to the estimated present value of the excess of guaranteed benefit GMIB over the account balance upon the policyholder s election to take the income benefit. The fair value of this derivative is determined based on the present value of expected cash flows. In addition, the Company has modified coinsurance and funds withheld reinsurance agreements that provide for a return based on a portfolio of fixed income securities. As such, the agreements contain embedded derivatives. The embedded derivative is bifurcated from the funds withheld balance and recorded at fair value with changes in fair value recognized in earnings through net realized and unrealized gains and losses on derivative instrument.

(d) Contingent Credit Features

Certain derivatives agreements entered into by the Company or its subsidiaries contain rating downgrade provisions that permit early termination of the agreement by the counterparty if collateral is not posted following failure to maintain certain credit ratings from one or more of the principal credit rating agencies. If the Company were required to early terminate such agreements due to a rating downgrade, it could potentially be in a net liability position at time of settlement. The aggregate fair value of all derivatives agreements containing such rating downgrade provisions that were in a liability position and the collateral posted under any of these agreements as of December 31, 2011 or 2010 was as follows:

Contingent Credit Features Summary:
Year ended December 31,

(U.S. dollars in thousands)	2011	2010
Aggregate fair value of derivative agreements with downgrade provisions in a net liability position	$ 15,763	$ 25,887
Collateral posted to counterparty	$ 809	$

15. Off-Balance Sheet Arrangements

On December 5, 2006, the Company and certain operating subsidiaries (Ceding Insurers) entered into a securities issuance agreement (the Securities Issuance Agreement), and certain of the Company s foreign insurance and reinsurance subsidiaries (Ceding Insurers) entered into an excess of loss reinsurance agreement (the Reinsurance Agreement), with Stoneheath Re (Stoneheath). The net effect of these agreements to the Company was the creation of a contingent put option to issue $350.0 million of preference ordinary shares in the aggregate of XL-Cayman. The agreements provided the Company with a Reinsurance Collateral Account in support of certain covered perils named in the Reinsurance Agreement. The covered perils included United States wind, European wind, California earthquake and terrorism worldwide. After an initial three-month period, the covered perils as well as the attachment points and aggregate retention amounts could be changed by the Ceding Insurers in their sole discretion, which could have resulted in a material increase or decrease in the likelihood of payment under the Reinsurance Agreement. On each date on which a Ceding Insurer withdrew funds from the Reinsurance Collateral Account, the Company would have been required to issue and deliver to Stoneheath an amount of Series D Preference Ordinary Shares having an aggregate liquidation preference that is equal to the amount of funds so withdrawn from the Collateral Account. The Company was obligated to reimburse Stoneheath for certain fees and ordinary expenses. The initial term of the Reinsurance Agreement was for the period from the December 5, 2006 through June 30, 2007, with four annual mandatory extensions through June 30, 2011 (unless coverage is exhausted thereunder prior to such date). At the Ceding Insurers option, the Reinsurance Agreement was extended to December 31, 2011.

On October 15, 2011, the Company announced that the Stoneheath facility would be terminated and, as a result, XL-Cayman would issue Series D Preference Ordinary Shares. Under the terms of the Securities Issuance Agreement, XL-Cayman was required upon the occurrence of certain conditions to issue and deliver to Stoneheath for distribution to the holders of the non-cumulative perpetual preferred securities of Stoneheath (the Stoneheath Securities), Series D Preference Ordinary Shares having an aggregate liquidation preference equal to the remaining assets in the Reinsurance Collateral Account in exchange for a distribution of such assets from the Reinsurance Collateral Account to

XL-Cayman. One such condition, the termination of an asset swap agreement covering the assets held under the Reinsurance Collateral Account, occurred in accordance with the terms of the swap agreement because Stoneheath did not seek to extend or replace it prior to its termination date. As a result, on November 16, 2011, Stoneheath redeemed the Stoneheath Securities and distributed the Series D Preference Ordinary Shares it received from XL-Cayman in exchange for the $350 million in assets from the Reinsurance Collateral Account.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

16. Variable Interest Entities

At times, the Company has utilized VIEs both indirectly and directly in the ordinary course of the Company s business.

The Company invests in CDOs, and other investment vehicles that are issued through variable interest entities as part of the Company s investment portfolio. The activities of these VIEs are generally limited to holding the underlying collateral used to service investments therein. Our involvement in these entities is passive in nature and we are not the arranger of these entities. The Company has not been involved in establishing these entities. The Company is not the primary beneficiary of these variable interest entities as contemplated in current authoritative accounting guidance.

The Company has a limited number of remaining outstanding credit enhancement exposures, including written financial guarantee and credit default swap contracts. The obligations related to these transactions are often securitized through variable interest entities. The Company is not the primary beneficiary of these variable interest entities as contemplated in current authoritative accounting guidance on the basis that management does not believe that the Company has the power to direct the activities, such as asset selection and collateral management, which most significantly impact each entity s economic performance. For further details on the nature of the obligations and the size of the Company s maximum exposure, see Note 14, Derivative Instruments, and Note 17(h), Commitments and Contingencies Financial and Other Guarantee Exposures .

17. Commitments and Contingencies

(a) Concentrations of Credit Risk

The creditworthiness of any counterparty is evaluated by the Company, taking into account credit ratings assigned by rating agencies. The credit approval process involves an assessment of factors including, among others, the counterparty and country and industry credit exposure limits. Collateral may be required, at the discretion of the Company, on certain transactions based on the creditworthiness of the counterparty.

The areas where significant concentrations of credit risk may exist include unpaid losses and loss expenses recoverable and reinsurance balances receivable (collectively, reinsurance assets) and in the investment fixed income portfolio.

Reinsurance Assets

The Company s reinsurance assets resulted from reinsurance arrangements in the course of its operations. A credit exposure exists with respect to reinsurance assets as they may be uncollectible. The Company manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and if necessary, the Company may hold collateral in the form of funds, trust accounts and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. For further details regarding the Company s reinsurance assets, see, Note 9, Reinsurance.

Fixed Income Portfolio

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

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

17. Commitments and Contingencies (Continued)

(a) Concentrations of Credit Risk (Continued)

Broker credit risk

In addition, the Company underwrites a significant amount of its insurance and reinsurance property and casualty business through brokers and a credit risk exists should any of these brokers be unable to fulfill their contractual obligations with respect to the payments of insurance and reinsurance balances to the Company. During the three years ended December 31, 2011, 2010 and 2009, P&C gross written premiums generated from or placed by the below companies individually accounted for more than 10% of the Company s consolidated gross written premiums from P&C operations, as follows:

Year Ended December 31			
(Percentage of consolidated gross written premiums from P&C operations)	**2011**	**2010**	**2009**
AON Corporation and subsidiaries	20%	21%	20%
Marsh & McLennan Companies	20%	21%	18%
Willis Group and subsidiaries	12%	11%	9%

These companies are large, well established companies and there are no indications that any of them are financially troubled. No other broker and no one insured or reinsured accounted for more than 10% of gross premiums written from P&C operations in any of the three years ended December 31, 2011, 2010, or 2009.

(b) Other Investments

The Company has committed to invest in several limited partnerships and provide liquidity financing to a structured investment vehicle. At December 31, 2011, the Company has commitments, which include potential additional add-on clauses to fund further $100.6 million over approximately the next nine years.

(c) Investments in Affiliates

The Company owns a minority interest in certain closed-end funds, certain limited partnerships and similar investment vehicles, including funds managed by those companies. The Company has commitments, which include potential additional add-on clauses, to invest a further $34.6 million over approximately the next five years.

(d) Properties

The Company rents space for certain of its offices under leases that expire up to 2031. Total rent expense under operating leases for the years ended December 31, 2011, 2010 and 2009 was approximately $32.9 million, $31.8 million and $34.4 million, respectively. Future minimum rental commitments under existing operating leases are expected to be as follows:

Year Ended December 31,	
(U.S. dollars in thousands)	
2012	$ 34,867
2013	32,012
2014	24,865
2015	17,409
2016	16,004
2017-2031	55,779
Total minimum future rentals	$ 180,936

189

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

17. Commitments and Contingencies (Continued)

(d) Properties (Continued)

During 2003, the Company entered into a purchase, sale and leaseback transaction to acquire new office space in London. The Company has recognized a capital lease asset of $100.7 million and $107.4 million, and deferred a gain of $30.6 million and $32.6 million related to this lease at December 31, 2011 and 2010, respectively. The gain is being amortized to income in line with the amortization of the asset. The future minimum lease payments in the aggregate are expected to be $224.6 million and annually for the next five years are as follows:

Year Ended December 31, *(U.S. dollars in thousands)*	
2012	$ 11,169
2013	11,448
2014	11,734
2015	12,028
2016	12,328
2017-2028	165,937
Total future minimum lease payments	$ 224,644

(e) Tax Matters

The Company is an Irish corporation and, except as described below, neither it nor its non-U.S. subsidiaries have paid U.S. corporate income taxes (other than withholding taxes on dividend income) on the basis that they are not engaged in a trade or business or otherwise subject to taxation in the U.S. However, because definitive identification of activities which constitute being engaged in a trade or business in the U.S. is not provided by the Internal Revenue Code of 1986, regulations or court decisions, there can be no assurance that the Internal Revenue Service will not contend that the Company or its non-U.S. subsidiaries are engaged in a trade or business or otherwise subject to taxation in the U.S. If the Company or its non-U.S. subsidiaries were considered to be engaged in a trade or business in the U.S. (and, if the Company or such subsidiaries were to qualify for the benefits under the income tax treaty between the U.S. and Bermuda and other countries in which the Company operates, such businesses were attributable to a permanent establishment in the U.S.), the Company or such subsidiaries could be subject to U.S. tax at regular tax rates on its taxable income that is effectively connected with its U.S. trade or business plus an additional 30% branch profits tax on such income remaining after the regular tax, in which case there could be a significant adverse effect on the Company s results of operations and financial condition.

(f) Letters of Credit

At December 31, 2011 and 2010, $1.9 billion and $2.4 billion of letters of credit were outstanding, of which 93.8% and 21.1%, respectively, were collateralized by the Company s investment portfolios, primarily supporting U.S. non-admitted business and the Company s Lloyd s syndicates capital requirements.

(g) Claims and Other Litigation

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

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

17. Commitments and Contingencies (Continued)

(g) Claims and Other Litigation (Continued)

Legal actions are subject to inherent uncertainties, and future events could change management s assessment of the probability or estimated amount of potential losses from pending or threatened legal actions. Based on available information, it is the opinion of management that the ultimate resolution of pending or threatened legal actions, both individually and in the aggregate, will not result in losses having a material effect on the Company s financial position or liquidity at December 31, 2011.

If management believes that, based on available information, it is at least reasonably possible that a material loss (or additional material loss in excess of any accrual) will be incurred in connection with any legal actions or claims, the Company discloses an estimate of the possible loss or range of loss, either individually or in the aggregate, as appropriate, if such an estimate can be made, or discloses that an estimate cannot be made. Based on the Company s assessment as at December 31, 2011, no such disclosures are considered necessary.

(h) Financial and Other Guarantee Exposures

Financial and Other Guarantee Exposures Summary:
Year ended December 31,

(U.S. dollars in thousands except number of contracts and term to maturity)	2011	2010
Number of financial guarantee contracts at January 1	37	41
Number of financial guarantee contracts matured, prepaid or commuted during the year	(33)	(4)
Number of financial guarantee contracts at December 31	4	37
Principal outstanding	$ 115,464	$ 198,696
Interest outstanding		6,119
Aggregate outstanding exposure	$ 115,464	$ 204,814
Total gross claim liability recorded	$ 1,399	$ 23,470
Total unearned premiums and fees recorded	$ 425	$ 571
Weighted average contractual term to maturity	26.7 years	13.2 years

Financial Guarantee Exposures

As part of the Company s legacy financial guarantee business, during January 2011, the Company commuted 32 of the 37 financial guarantee transactions that were outstanding at December 31, 2010, including three non-performing transactions. This commutation eliminated $41.9 million of notional financial guarantee exposure (including principal and interest) for a payment of $22.1 million. The $22.1 million was included in the gross claim liability at December 31, 2010. In addition, during the fourth quarter of 2011, one guarantee was terminated upon prepayment of the underlying notes.

The Company s outstanding financial guarantee contracts at December 31, 2011 provide credit support for a variety of collateral types with the exposures comprised of (i) $108.3 million notional financial guarantee on three notes backed by zero coupon bonds and bank perpetual securities, including some issued by European financials; and (ii) $7.2 million notional financial guarantee relating to future scheduled repayments on a government-subsidized housing project. At December 31, 2011, there were no reported events of default on these obligations.

During 2010, in addition to the exposures discussed above, the Company also provided credit support for $386.5 million of notional financial guarantee exposure (including principal and interest) on a Chilean toll road structure. This was eliminated on August 5, 2010, when the issuer decided to prepay the debt. In addition, $47.5 million notional financial guarantee that was outstanding on a collateralized fund obligation was eliminated when the fund was wound-up in an orderly manner.

Surveillance procedures to track and monitor credit deteriorations in the insured financial obligations are performed by the primary obligors for each transaction on the Company s behalf. Information regarding the performance status and updated exposure values is provided to the Company on a quarterly basis and evaluated by management in recording claims reserves.

17. Commitments and Contingencies (Continued)

(h) Financial and Other Guarantee Exposures (Continued)

Other Guarantee Exposures

On June 28, 2010, the Company s subsidiary, XLIB, completed a commutation, termination and release agreement (the Termination Agreement) with European Investment Bank (EIB) which fully extinguished and terminated all of the guarantees issued to EIB by XLI in connection with financial guaranty policies between certain subsidiaries of Syncora Holdings and EIB. These guarantees were provided for the benefit of EIB relating to project finance transactions comprised of transportation, school and hospital projects with an average rating of BBB, written between 2001 and 2006 with anticipated maturities ranging between 2027 and 2038. The guarantees had been accounted for under Accounting Standards Codification (ASC) section 460-10, *Guarantees* (previously FIN 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.)

Under the Termination Agreement, XLIB paid $38 million to EIB, and all of XLIB s exposures under the EIB guarantees, with aggregate par outstanding of approximately $900 million, were eliminated. In addition, a further $0.5 million was paid to EIB for expenses in relation to the termination. Pursuant to the obligations of Syncora Holdings and its affiliates (collectively Syncora) under the Master Agreement, Syncora paid XLIB $15.0 million. The net cost of this transaction is reflected in the Company s Consolidated Statement of Income as Loss on Termination of Guarantee.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital

(a) Authorized and Issued

The authorized share capital is 999,990,000 ordinary shares of par value $0.01 each, 40,000 ordinary shares of par value 1.00 each, 350,000 Series D preference shares of par value $0.01 each, and 1,000,000 Series E preference ordinary shares of par value $0.01 each. Holders of ordinary shares are entitled to one vote for each share.

Ordinary Shares

The following table is a summary of ordinary shares issued and outstanding:

Year Ended December 31 *(in thousands)*	**2011**	**2010**
Balance beginning of year	316,396	342,119
Exercise of options	72	91
Net issuance of restricted shares	413	139
Share buybacks (1)	(31,692)	(25,953)
Issue of shares	30,457	
Balance end of year	315,646	316,396

(1) Includes share buybacks associated with authorized share buyback programs as well as purchases related to satisfying tax withholding obligations of employees in connection with the vesting of restricted shares granted under the Company s restricted stock plan.

Ordinary Share Buybacks

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

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

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital (Continued)

(a) Authorized and Issued (Continued)

Equity Security Units

In August 2011, in accordance with the terms of the 10.75% equity security units (the 10.75% Units), XL-Cayman purchased and retired all of the 8.25% senior notes due August 2021 (the 8.25% Senior Notes) for $575 million in a remarketing. These notes comprised a part of the 10.75% Units. The proceeds from the remarketing were used to satisfy the purchase price for XL-Ireland s ordinary shares issued to holders of the 10.75% Units pursuant to the forward purchase contracts comprising a part of the 10.75% Units. Each forward purchase contract provided for the issuance of 1.3242 ordinary shares of XL-Ireland at a price of $25 per share. The settlement of the forward purchase contracts resulted in XL-Ireland s issuance of an aggregate of 30,456,600 ordinary shares for an aggregate purchase price of $575 million. As a result of the settlement of the forward purchase contracts, the 10.75% Units ceased to exist and are no longer traded on the NYSE.

(b) Preferred shares and Non-controlling Interest in Equity of Consolidated Subsidiaries

Series C Preference Ordinary Shares

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

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

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

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

Series D Preference Ordinary Shares

On October 15, 2011, XL-Cayman issued $350 million Series D Preference Ordinary Shares for consideration of cash and liquid investments which were held in a trust account that was part of the Stoneheath facility. Holders of the Stoneheath Securities issued by Stoneheath in December 2006 received one Series D Preferred Share in exchange for each Stoneheath Security. Dividends on the Series D Preference Ordinary Shares are declared and paid quarterly at a floating rate of three-month LIBOR plus 3.120% on the liquidation preference. XL-Cayman used the consideration it received as partial funding for the repayment at maturity of the outstanding $600 million XLCFE Notes that were issued by XLCFE, with the balance available for general corporate purposes. For further details regarding Stoneheath, Note 15, Off-Balance Sheet Arrangements. The Series D Preference Ordinary Shares represent non-controlling interests in equity of consolidated subsidiaries.

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

194

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital (Continued)

(b) Preferred shares and Non-controlling Interest in Equity of Consolidated Subsidiaries (Continued)

Series E Preference Ordinary Shares

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

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

(c) Stock Plans

The Company s performance incentive programs provide for grants of stock options, restricted stock, restricted stock units and performance units and stock appreciation rights. Share based compensation granted by the Company generally contains a vesting period of three or four years, and certain awards also contain performance conditions. The Company records compensation expense related to each award over its vesting period incorporating the best estimate of the expected outcome of performance conditions where applicable. Compensation expense is generally recorded on a straight line basis over the vesting period of an award.

In connection with, and effective upon, the completion of the Redomestication, XL-Ireland assumed the existing liabilities, obligations and duties of XL-Cayman under the NAC Re Corp. 1989 Stock Option Plan (the 1989 Plan), the XL Group plc Amended and Restated 1991 Performance Incentive Program (the 1991 Program), the XL Group plc Amended and Restated 1999 Performance Incentive Program for Employees (the 1999 Program), the XL Group plc Directors Stock & Option Plan (the Directors Plan), the XL Group plc 2009 Cash Long-Term Incentive Program (the 2009 Program), the XL Group plc Supplemental Deferred Compensation Plan (the DC Plan, and together with the 1989 Plan, 1991 Program, the 1999 Program, the Directors Plan and the 2009 Program, the Programs). Furthermore, in connection with, and effective upon, the completion of the Redomestication, the Programs were amended by XL-Cayman, among other things to, (i) provide that XL-Ireland and its Board of Directors will succeed to all powers, authorities and obligations of XL-Cayman and its Board of Directors under each Program, (ii) provide that the securities to be issued pursuant to each Program will consist of ordinary shares of XL-Ireland and (iii) otherwise to reflect the completion of the Redomestication.

(d) Options

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2011	2010	2009
Dividend yield	1.90%	3.25%	3.25%
Risk free interest rate	2.60%	2.67%	2.38%
Volatility	50.03%	71.09%	94.27%
Expected lives	6.0 years	6.0 years	6.0 years

The risk free interest rate is based on U.S. Treasury rates. The expected lives are estimated using the historical exercise behavior of grant recipients. The expected volatility is determined based upon a combination of the historical volatility of the Company s stock and the implied volatility derived from publicly traded options.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital (Continued)

(d) Options (Continued)

The following is a summary of the stock option plans for the three years ended December 31:

Year Ended December 31 *(in thousands except for weighted average fair value)*	**2011**	**2010**	**2009**
Options granted to purchase ordinary shares under directors and employees incentive compensation plans	974	1,023	1,269
Weighted average grant date fair value	$ 9.81	$ 9.17	$ 2.85
Total intrinsic value of stock options exercised	$ 301	$ 667	$
Options exercised during the year	72	91	
Compensation expense related to stock option plans	$ 11,848	$ 12,766	$ 13,659
Estimated tax benefit related to stock option plans	$ 722	$ 2,347	$ 3,377

The following is a summary of stock options as of December 31, 2011, and related activity for the year then ended for the Company:

Year Ended December 31, 2011 *(in thousands except for option price and term)*	**Number of Shares**	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Term**	**Aggregate Intrinsic Value (000s)**
Outstanding beginning of year	13,794	$ 50.71	5.1 years	$ 30,362
Granted	974	23.34		
Exercised	(72)	18.52		
Canceled/Expired	(1,699)	70.11		
Outstanding end of year	12,997	$ 46.30	4.9 years	$ 20,585
Options exercisable	10,933	$ 51.54	4.2 years	$ 14,801
Options available for grant (1)	22,142			

(1) Available for grant includes shares that may be granted as either stock options, restricted stock, restricted stock units or performance units.

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company s closing stock price on the last trading day of the 2011 fiscal year and the exercise price, multiplied by the number of in-the-money-options) that would have been received by the option holders had all option holders exercised their options on December 31, 2011. Total unrecognized stock based compensation expense related to non-vested stock options was approximately $9.8 million at December 31, 2011, related to approximately 2.1 million options, which is expected to be recognized over a weighted-average period of 1.3 years. The exercise price of the Company s outstanding options granted is the market price of the Company s ordinary shares on the grant date, except that during 2004, 295,000 options were granted with an exercise price of $88.00 when the market price was $77.10.

(e) Restricted Stock, Restricted Stock Units and Performance Units

Restricted Stock

Restricted stock awards issued under the 1991 Performance Incentive Program and the Directors Stock and Option Plan vest as set forth in the applicable award agreements. Each restricted stock award represents the Company s obligation to deliver to the holder one ordinary share. The employees and directors who are granted a restricted stock award shall have all the rights of a shareholder, including the right to vote and receive dividends. These shares contained certain restrictions prior to vesting, relating to, among other things, forfeiture in the event of termination of employment and transferability.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital (Continued)

(e) Restricted Stock, Restricted Stock Units and Performance Units

Restricted Stock (Continued)

A summary of the restricted stock awards issued under the 1991 Performance Incentive Program and the Directors Stock and Option Plan for the three years ended December 31 is as follows:

Year Ended December 31 *(in thousands except for weighted average fair value)*	2011	2010	2009
Restricted ordinary shares granted	49	63	147
Weighted average grant date fair value	$ 23.33	$ 17.26	$ 11.24
Aggregate grant date fair value	$ 1,140	$ 1,080	$ 1,651
Compensation expense related to restricted stock awards	$ 7,101	$ 18,420	$ 32,231
Estimated tax benefit related to restricted stock awards	$ 1,546	$ 4,645	$ 7,724

Total unrecognized stock based compensation expense related to non-vested restricted stock awards was approximately $4.5 million as of the end of December 31, 2011, related to approximately 0.4 million restricted stock awards, which is expected to be recognized over 2.0 years.

Non-vested restricted stock awards as of December 31, 2011 and for the year then ended for the Company were as follows:

(in thousands except for weighted average fair value)	Number of Shares	Weighted-Average Grant Date Fair Value
Unvested at December 31, 2010	549	$ 42.86
Granted	49	$ 23.33
Vested	(208)	$ 38.27
Forfeited		$
Unvested at December 31, 2011	390	$ 42.86

Restricted Stock Units

Each restricted stock unit represents the Company s obligation to deliver to the holder one ordinary share upon satisfaction of the three year vesting term. Restricted stock units are granted at the closing market price on the day of grant and entitle the holder to receive dividends declared and paid in the form of additional ordinary shares contingent upon vesting.

A summary of the restricted stock units issued to officers of the Company and its subsidiaries for the three years ended December 31 is as follows:

Year Ended December 31 *(in thousands)*	2011	2010	2009 (1)
Restricted stock units granted	1,318	1,392	
Aggregate grant date fair value	$ 30,027	$ 25,887	$
Compensation expense related to restricted stock units	$ 15,033	$ 5,862	$
Estimated tax benefit related to restricted stock units	$ 3,998	$ 1,557	$

(1) During the year ended December 31, 2009, there were no shares granted under the Company s restricted stock plan.

Total unrecognized stock based compensation expense related to non-vested restricted stock units was approximately $31.7 million as of the end of December 31, 2011, related to approximately 2.1 million restricted stock units, which is expected to be recognized over 1.5 years.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

18. Share Capital (Continued)

(e) Restricted Stock, Restricted Stock Units and Performance Units (Continued)

Restricted Stock Units (Continued)

Non-vested restricted stock units as of December 31, 2011 and for the year then ended for the Company were as follows:

(in thousands except for weighted average fair value)	Number of Shares	Weighted-Average Grant Date Fair Value
Unvested at December 31, 2010	1,317	$ 18.61
Granted	1,318	$ 22.78
Vested	(447)	$ 18.80
Forfeited	(125)	$ 20.28
Unvested at December 31, 2011	2,063	$ 21.13

Performance Units

The performance units vest after three years and entitle the holder to shares of the Company s stock. There are no dividend rights associated with the performance units. Each grant of performance units has a target number of shares, with final payouts ranging from 0% to 200% of the grant amount depending upon a combination of corporate and business segment performance along with each employee s continued service through the vest date. Performance targets are based on relative and absolute financial performance metrics. A summary of the performance units issued to certain employees of the Company for the three years ended December 31 is as follows:

Year Ended December 31 *(in thousands except for number of shares and weighted average fair value)*	2011	2010 (1)	2009
Performance units granted	1,289	1,579	
Potential maximum share payout	2,578	3,158	
Aggregate grant date fair value	$ 28,544	$ 27,160	$
Compensation expense related to performance units	$ 7,242	$ 7,009	$
Estimated tax benefit related to performance units	$ 1,419	$ 1,470	$

(1) The performance units plan was introduced during the year ended December 31, 2010.

Total unrecognized stock based compensation expense related to non-vested performance units was approximately $21.8 million as of the end of December 31, 2011, related to approximately 1.7 million performance units, which is expected to be recognized over 1.9 years.

Non-vested restricted performance units as of December 31, 2011 were as follows:

(in thousands except for weighted average fair value)	Number of Shares	Weighted-Average Grant Date Fair Value
Unvested at December 31, 2010	1,517	$ 17.20
Granted	1,289	$ 22.14

Forfeited	(213)	$	19.43
Performance driven reduction	(858)	$	18.37
Unvested at December 31, 2011	1,735	$	19.47

(f) Voting

XL-Ireland s Articles of Association restrict the voting power of any person to less than approximately 10% of total voting power.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

19. Retirement Plans

The Company provides pension benefits to eligible employees through various defined contribution and defined benefit retirement plans sponsored by the Company, which vary for each subsidiary. Plan assets are invested principally in equity securities and fixed maturities.

(a) Defined contribution plans

The Company has qualified defined contribution plans which are managed externally and whereby employees and the Company contribute a certain percentage of the employee s gross compensation (base salary and annual bonus) into the plan each month. The Company s contribution generally vests over five years. The Company s expenses for its qualified contributory defined contribution retirement plans were $42.4 million, $37.8 million and $38.6 million at December 31, 2011, 2010 and 2009, respectively.

(b) Defined benefit plans

The Company maintains defined benefit plans that cover certain employees as follows:

U.S. Plan

A qualified non-contributory defined benefit pension plan exists to cover a number of its U.S. employees. This plan also includes a non-qualified supplemental defined benefit plan designed to compensate individuals to the extent that their benefits under the Company s qualified plan are curtailed due to IRS Code limitations. Benefits are based on years of service and compensation, as defined in the plan, during the highest consecutive three years of the employee s last ten years of employment. Under these plans, the Company s policy is to make annual contributions to the plan that are deductible for federal income tax purposes and that meet the minimum funding standards required by law. The contribution level is determined by utilizing the entry age cost method and different actuarial assumptions than those used for pension expense purposes.

In addition, certain former employees have received benefit type guarantees, not formally a part of any established plan. The liability recorded with respect to these agreements as at December 31, 2011 and 2010 was $3.3 million and $3.0 million, respectively, representing the entire unfunded projected benefit obligations.

Several assumptions and statistical variables are used in the models to calculate the expenses and liability related to the plans. The Company, in consultation with its actuaries, determines assumptions about the discount rate, the expected rate of return on plan assets and the rate of compensation increase. The table below includes disclosure of these rates on a weighted-average basis, encompassing all the international plans.

	2011	2010
Net Benefit Cost Weighted-average assumptions for the years ended December 31		
Discount rate	5.6%	6.0%
Expected long-term rate of return on plan assets	8.0%	8.0%
Benefit Obligation Weighted-average assumptions at December 31		
Discount rate	4.4%	5.6%

The U.S. Retirement plan assets at December 31, 2011 and 2010 consist of two mutual funds. The first fund employs a core bond portfolio strategy that seeks maximum current income and price appreciation consistent with the preservation of capital and prudent risk taking with the focus on intermediate term high quality bonds.

The second fund seeks long term growth of capital by investing in a diversified group of domestic and international companies. Using a quantitative approach, portfolio managers identify companies that they believe have favorable prospects for above average growth.

The fair value of the U.S. Plan assets at December 31, 2011 and 2010 was $25.9 million and $25.1 million, respectively. As both of the retirement plan s investments are mutual funds, they fall within Level 1 in the fair value hierarchy.

199

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

19. Retirement Plans (Continued)

(b) Defined benefit plans (Continued)

U.K. Plans

A contributory defined benefit pension plan exists in the U.K., but has been closed to new entrants since 1996. The Scheme has approximately 90 members, of whom approximately 57 are active or deferred members of the Scheme. Benefits are based on length of service and compensation as defined in the Trust Deed and Rules, and the Plan is subject to triennial funding valuations, the most recent of which was conducted in 2010 and was reported in 2011. The $2.7 million deficit is being funded over a 10 year period. Current contribution rates are 24.6% and 3% of pensionable salary for employer and employee respectively.

The U.K. pension plan assets are held in a separate Trustee administered fund to meet long term liabilities to past and present employees. The table below shows the composition of the Plan s assets and the fair value of each major category of plan assets as of December 31, 2011 and 2010, as well as the potential returns of the different asset classes. The total of the asset values held in various externally managed portfolios are provided by third party pricing vendors. There is no significant concentration of risk within plan assets.

The assets in the scheme and the expected rates of return were as follows: *(U.S. dollars in thousands, except percentages)*	Expected Return on Assets for 2011	Value at December 31, 2011	Expected Return on Assets for 2010	Value at December 31, 2010
Equities	7.0%	$ 6,351	7.5%	$ 5,542
Gilts	4.0%	1,350	4.5%	1,249
Corporate Bonds	5.5%	1,381	5.7%	1,187
Other (cash)	4.0%	12	4.2%	254
Total market value of assets		$ 9,094		$ 8,232

In addition, during 2003 six members who are still employed by the Company in the U.K. transferred from a defined benefit plan into a defined contribution plan. These employees have a contractual agreement with the Company that provides a no worse than final salary pension guarantee in the event that they are employed by the Company until retirement, whereby the Company guarantees to top-up their defined contribution pension to the level of pension that they would have been entitled to receive had they remained in the defined benefit scheme. The pension liability recorded with respect to these individuals was $3.3 million and $3.4 million at December 31, 2011 and 2010, respectively, representing the entire unfunded projected obligation.

European Plans

Certain contributory defined benefit pension plans exist in several European countries, most notably Germany, which are closed to new entrants. Benefits are generally based on length of service and compensation defined in the related agreements. Included in the projected obligation amounts of $72.3 million and $66.3 million at December 31, 2011 and 2010, respectively, in the table below, are total unfunded projected obligations in relation to the European defined benefit schemes of $14.6 million and $16.0 million, respectively.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

19. Retirement Plans (Continued)

(b) Defined benefit plans (Continued)

European Plans (Continued)

As a part of the purchase of XL GAPS, the Company acquired certain defined benefit pension liabilities. The related balances are not included in the tables below as the liabilities are insured under an annuity type contract.

The status of the above mentioned plans at December 31, 2011 and 2010 is as follows:

(U.S. dollars in thousands)	2011	2010
Change in projected benefit obligation:		
Projected benefit obligation beginning of year	$ 66,327	$ 56,998
Service cost (1)	919	737
Interest cost	3,393	3,021
Actuarial (gain) / loss	3,837	8,197
Benefits and expenses paid	(1,612)	(1,419)
Foreign currency losses / (gains)	(597)	(1,207)
Projected benefit obligation end of year	$ 72,267	$ 66,327

(1) Service costs include cost of living adjustments on curtailed plans.

	2011	2010
Change in plan assets:		
Fair value of plan assets beginning of year	$ 33,294	$ 29,548
Actual return on plan assets	969	3,695
Employer contributions	1,941	1,295
Benefits and expenses paid	(1,132)	(995)
Foreign currency gains (losses)	(116)	(249)
Fair value of plan assets end of year	$ 34,956	$ 33,294
Funded status end of year	$ (37,312)	$ (33,033)
Accrued pension liability	$ 37,312	$ 33,033

The components of the net benefit cost for the years ended December 31, 2011 and 2010 are as follows:

(U.S. dollars in thousands)	2011	2010
Components of net benefit cost:		

Service cost	$ 919	$ 736
Interest cost	3,337	3,021
Expected return on plan assets	(1,558)	(1,576)
Amortization of net actuarial loss	373	198
Net benefit cost	$ 3,071	$ 2,379

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

20. Accumulated Other Comprehensive Income (Loss)

The related tax effects allocated to each component of the change in accumulated other comprehensive income (loss) were as follows:

(U.S. dollars in thousands)	Before Tax Amount	Tax (Benefit) Expense	Net of Tax Amount
Year Ended December 31, 2011:			
Unrealized gains on investments:			
Unrealized gains (losses) arising during year	$ 281,302	$ (51,418)	$ 332,720
Less reclassification for (losses) realized in income	(188,359)	(9,927)	(178,432)
Net unrealized gains (losses) on investments	469,661	(41,491)	511,152
Change in value of cash flow hedge	439		439
Change in underfunded pension liability	(2,622)		(2,622)
Foreign currency translation adjustments	(27,802)	(1,102)	(26,700)
Change in accumulated other comprehensive income	$ 439,676	$ (42,593)	$ 482,269
Year Ended December 31, 2010:			
Unrealized gains on investments:			
Unrealized gains (losses) arising during year	$ 885,910	$ (46,859)	$ 932,769
Less reclassification for (losses) realized in income	(270,803)	(5,369)	(265,434)
Net unrealized gains (losses) on investments	1,156,713	(41,490)	1,198,203
Change in value of cash flow hedge	439		439
Change in net unrealized gain on future policy benefit reserves	(3,714)		(3,714)
Change in underfunded pension liability	(2,619)		(2,619)
Foreign currency translation adjustments	47,265	(3,688)	50,953
Change in accumulated other comprehensive income	$ 1,198,084	$ (45,178)	$ 1,243,262
Year Ended December 31, 2009:			
Unrealized (losses) on investments:			
Unrealized gains (losses) arising during year	$ 1,246,562	$ 119,675	$ 1,126,887
Less reclassification for (losses) realized in income	(921,437)	(10,317)	(911,120)
Net unrealized gains (losses) on investments	2,167,999	129,992	2,038,007
Change in value of cash flow hedge	438		438
Change in net unrealized gain on future policy benefit reserves	6,554		6,554
Change in underfunded pension liability	(3,427)		(3,427)
Foreign currency translation adjustments	169,261	(11,627)	180,888
Change in accumulated other comprehensive income (loss)	$ 2,340,825	$ 118,365	$ 2,222,460

The December 31 balance of each component of accumulated other comprehensive income (loss) for 2011, 2010 and 2009 are as follows:

Year Ended December 31

(U.S. dollars in thousands)	2011	2010	2009
Accumulated unrealized gains (losses) on investments, net of tax	$ 721,784	$ 238,751	$ (834,546)
OTTI losses recognized in other comprehensive income, net of tax	(199,988)	(228,107)	(353,013)
Accumulated foreign currency translation	77,554	104,254	53,301
Accumulated underfunded pension liability	(17,521)	(14,899)	(8,566)
Accumulated cash flow hedge	1,235	796	357
Total	$ 583,064	$ 100,795	$ (1,142,467)

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

21. Dividends

In 2011, four quarterly dividends of $0.11 per share were paid to all ordinary shareholders of record as of March 15, June 15, September 15 and December 15. In 2010, four quarterly dividends of $0.10 per share were paid to all ordinary shareholders of record as of March 15, June 15, September 15 and December 15. In 2009, four quarterly dividends of $0.10 per share were paid to all ordinary shareholders of record as of March 13, June 15, September 15 and December 15.

The Company paid dividends to Series C and Series E preference shareholders, and declared dividends to Series D preference shareholders, for the three years ended December 31, as follows:

Year Ended December 31 *(U.S. dollars in millions)*	**2011**	**2010**	**2009**
Series C preference ordinary shares	$ 5.3	$ 7.9	$ 23.2
Series D preference ordinary shares (1)	$	$	$
Series E preference ordinary shares	$ 66.2	$ 69.9	$ 65.0

(1) On December 16, 2011, the Company announced that the Board of Directors of XL-Cayman resolved to pay a dividend of $9.1084 per share on XL-Cayman s Series D Preference Ordinary Shares. The dividend was paid on January 17, 2012 to all shareholders of record as of January 3, 2012.

22. Taxation

Following completion of the redomestication of the Company, with effect from July 1, 2010, the Company is subject to income and capital gains tax in Ireland under applicable Irish law. Prior to July 1, 2010, the Company was resident for tax purposes in the Cayman Islands and in accordance with Cayman law, was not subject to any taxes in the Cayman Islands on either income or capital gains.

The Company s Bermuda subsidiaries are not subject to any income, withholding or capital gains taxes under current Bermuda law. In the event that there is a change such that these taxes are imposed, the Bermuda subsidiaries would be exempted from any such tax until March 2035 pursuant to the Bermuda Exempted Undertakings Tax Protection Act of 1966, and the Exempted Undertakings Tax Protection Amendment Act of 2011.

The Company s U.S. subsidiaries are subject to federal, state and local corporate income taxes and other taxes applicable to U.S. corporations. The provision for federal income taxes has been determined under the principles of the consolidated tax provisions of the IRS Code and Regulations thereunder.

The Company has operations in subsidiary and branch form in various other jurisdictions around the world, including but not limited to the U.K., Switzerland, Ireland, Germany, France, Canada, Brazil and various other countries in Latin America and Asia that are subject to relevant taxes in those jurisdictions.

Deferred income taxes have not been accrued with respect to certain undistributed earnings of foreign subsidiaries. If the earnings were to be distributed, as dividends or otherwise, such amounts may be subject to withholding taxation in the state of the paying entity. During 2010, the Company revised its capital strategy such that it is no longer able to positively assert that all earnings arising in the U.S. will be permanently reinvested in that jurisdiction and accordingly, a provision for withholding taxes arising in respect of U.S. earnings has been made. No withholding taxes are accrued with respect to the earnings of the Company s subsidiaries arising outside the U.S., as it is the intention that all such earnings will remain reinvested indefinitely.

The Company adopted the provisions of the final authoritative guidance on accounting for uncertainty in income taxes, on January 1, 2007. The Company did not recognize any liabilities for unrecognized tax benefits as a result of its implementation and has not recognized any liabilities in subsequent accounting periods. The Company s policy is to recognize any interest accrued related to unrecognized tax benefits as a component of interest expense and penalties in the tax charge. At December 31, 2011 and 2010, the Company has no accrued liabilities relating

to interest and penalties.

The Company has open examinations by tax authorities in Ireland (2006 to 2009), the U.K. (2007 to 2010), the U.S. (2006 to 2009), France (2008 and 2009), Germany (2006 to 2009), India (2008 to 2010), Canada (2007 to 2010) and Singapore (2008 and 2009). The Company believes that these examinations will be concluded within the next 24 months; however, it is not currently possible to estimate the outcome of these examinations.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

22. Taxation (Continued)

The Company has open tax years that are potentially subject to examinations by local tax authorities, in the following major tax jurisdictions: the U.S., 2010 and 2011; the U.K., 2009 to 2011; Switzerland, 2007 to 2011; Ireland, 2005 to 2011; Germany, 2010 and 2011; and France, 2007 to 2011.

The income tax provisions for the years ended December 31, 2011, 2010 and 2009 are as follows:

Year Ended December 31 *(U.S. dollars in thousands)*	**2011**	**2010**	**2009**
Current expense:			
U.S	$ 9,138	$ 40,413	$ 29,112
Non U.S	87,220	35,113	90,079
Total current expense	$ 96,358	$ 75,526	$ 119,191
Deferred expense (benefit):			
U.S	$ (5,550)	$ 18,225	$ (4,604)
Non U.S	(31,101)	68,986	5,720
Total deferred expense (benefit)	$ (36,651)	$ 87,211	$ 1,116
Total Tax Expense	$ 59,707	$ 162,737	$ 120,307

The weighted average expected tax provision has been calculated using the pre-tax accounting income (loss) in each jurisdiction multiplied by that jurisdiction s applicable statutory tax rate. The applicable statutory tax rates of the most significant jurisdictions contributing to the overall taxation of the Company are: Ireland 12.5% and 25%, Bermuda 0%, the U.S. 35%, the U.K. 26.5%, Switzerland 7.83% and 21.2%, Germany 15%, and France 34.43%. Reconciliation of the difference between the provision for income taxes and the expected tax provision at the weighted average tax rate for the years ended December 31, 2011, 2010 and 2009 is provided below:

(U.S. dollars in thousands)	**2011**	**2010**	**2009**
Expected tax provision at weighted average rate	$ (66,493)	$ 80,225	$ 129,136
Permanent differences:			
Non-taxable investment income (loss)	(14,246)	(10,176)	(5,715)
Non-taxable income (loss)	(3,265)	3,838	(91,968)
Prior year adjustments	(9,206)	16,594	(15,360)
State, local and foreign taxes	42,581	44,122	59,835
Valuation allowance	24,990	1,346	11,439
Allocated investment income	21,483	12,386	20,045
Stock options	5,840	3,323	6,222
Non-deductible expenses	12,901	11,079	6,673
Non-deductible goodwill impairment	57,069		
Non-taxable reserve release	(11,947)		
Total tax expense	$ 59,707	$ 162,737	$ 120,307

Taxes during 2011 varied significantly relative to the weighted average effective tax rate due to a combination of three key items; i) the impairment of goodwill which represented a loss to the company but was not deductible in certain relevant jurisdictions, ii) the distribution of

fourth quarter 2011 catastrophe losses between jurisdictions with the majority ultimately impacting low tax jurisdictions, and iii) the valuation allowances recorded against the tax impact of certain realized investment losses.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

22. Taxation (Continued)

Significant components of the Company s deferred tax assets and liabilities at December 31, 2011 and 2010 were as follows:

(U.S. dollars in thousands)	2011	2010
Deferred Tax Asset:		
Net unpaid loss reserve discount	$ 108,981	$ 105,313
Net unearned premiums	62,162	57,289
Compensation liabilities	35,830	42,347
Net operating losses	263,600	282,202
Investment adjustments	12,861	8,941
Pension	9,753	6,290
Bad debt reserve	10,829	10,502
Amortizable goodwill	10,732	
Net unrealized depreciation on investments	320	6,004
Stock options	13,842	15,052
Depreciation	4,072	7,131
Net realized capital losses	119,307	117,358
Deferred intercompany capital losses	117,892	142,300
Other	7,573	9,527
Deferred tax asset, gross of valuation allowance	$ 777,754	$ 810,256
Valuation allowance	497,236	514,467
Deferred tax asset, net of valuation allowance	$ 280,518	$ 295,789
Deferred Tax Liability:		
Net unrealized appreciation on investments	$ 96,797	$ 52,972
Deferred acquisition costs	20,103	19,601
Currency translation adjustments	8,062	11,115
Regulatory reserves	125,249	149,650
Untaxed Lloyd s result	8,340	16,028
Other	4,786	8,565
Deferred tax liability	$ 263,337	$ 257,931
Net Deferred Tax Asset	$ 17,181	$ 37,858

The deferred tax asset and liability balances presented above represent the gross deferred tax asset and liability balances across each tax jurisdiction. The deferred tax asset balances of $115.6 million and $143.5 million at December 31, 2011 and 2010, respectively, and deferred tax liability balances of $98.4 million and $105.7 million at December 31, 2011 and 2010, respectively, as disclosed on the consolidated balance sheets include netting of certain deferred tax assets and liabilities within a tax jurisdiction to the extent such netting is consistent with the regulations of the tax authorities in those jurisdictions.

The valuation allowance at December 31, 2011 and December 31, 2010 of $497.2 million and $514.5 million, respectively, related primarily to net operating loss carry forwards in Switzerland, net operating loss and capital loss carry forwards in Ireland, and net unrealized capital losses and realized capital loss carry forwards in the U.S. that may not be realized within a reasonable period. At December 31, 2011, the Company had realized capital loss carry forwards of approximately $340.8 million in the U.S. ($119.3 million tax effected). The 5 year limitation for the utilization of realized capital losses applies to this balance. Losses of $35.2 million will expire at the end of 2012 with another $305.6 million of realized capital losses expiring in future years through 2016. A valuation allowance ($119.3 million) has been established in respect of all of these realized capital losses. At December 31, 2011, the Company also had $336.8 million of losses arising from the sale of investments to a group company ($117.9 million tax effected), against which a valuation allowance of $117.9 million has been established.

These losses cannot be utilized to offset any future U.S. realized capital gains, and will not begin to expire, until the underlying assets have been sold to unrelated parties.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

22. Taxation (Continued)

At December 31, 2011, net operating loss carry forwards in the U.K. were approximately $96.5 million and have no expiration. A valuation allowance ($2.1 million) has been established in respect of $8.1 million of these U.K. losses given management s expectation that losses in specific U.K. entities will not be utilized in the future. At December 31, 2011, net operating loss carry forwards in Switzerland were approximately $881.2 million, of which $803.3 million will expire at the end of 2012 with the balance expiring in future years through 2018. A valuation allowance ($183.8 million) has been established in respect of all of the net operating losses which will expire in 2012 and in respect of a further $74.3 million of other Swiss losses. At December 31, 2011, net operating loss carry forwards in Ireland were approximately $189.5 million, with a further $158.0 million of capital losses carried forward. Although these Irish losses may be carried forward indefinitely, a valuation allowance ($53.1 million) has been established in respect of these Irish losses due to the uncertainty surrounding any future loss utilization.

Management has reviewed historical taxable income and future taxable income projections for its U.K. group and has determined that in its judgment substantially all of the U.K. net operating losses ($88.4 million) will more likely than not be realized as reductions of future taxable income within a reasonable period. Management will continue to evaluate income generated in future periods by the U.K. group in determining the reasonableness of its position. If management determines that future income generated by the U.K. group is insufficient to cause the realization of the net operating losses within a reasonable period, a valuation allowance would be required for the U.K. portion of the net deferred tax asset balance related to net operating losses in the amount of $22.2 million.

Management believes it is more likely than not that the tax benefit of the remaining net deferred tax assets will be realized.

Shareholders equity at December 31, 2011 and 2010 reflected tax benefits of nil and nil, respectively, related to compensation expense deductions for stock options exercised by the Company s U.S. subsidiaries.

23. Statutory Financial Data

The Company s ability to pay dividends is subject to certain regulatory restrictions on the payment of dividends by its subsidiaries. The payment of such dividends is limited by applicable laws and statutory requirements of the various countries in which the Company operates, including Bermuda, the U.S., Ireland and the U.K., among others. Statutory capital and surplus for the principal operating subsidiaries of the Company for the years ended December 31, 2011 and 2010 are summarized below. 2011 information is preliminary as many regulatory returns are due later in 2012 for many jurisdictions in which the Company does business, and accordingly, 2011 information summarized below is subject to revision.

	Bermuda (1)		U.S. (2)		U.K., Europe and Other	
(U.S. dollars in thousands)	2011	2010	2011	2010	2011	2010
Required statutory capital and surplus	$ 4,923,801	$ 4,687,988	$ 637,799	$ 640,834	$ 1,132,821	$ 1,141,884
Actual statutory capital and surplus (3)	$ 9,140,393	$ 9,159,021	$ 2,093,694	$ 2,273,711	$ 3,197,220	$ 3,211,204

(1) Required statutory capital and surplus represents 100% BSCR level for principal Bermuda operating subsidiaries.
(2) Required statutory capital and surplus represents 100% RBC level for principal U.S. operating subsidiaries.
(3) Statutory assets in Bermuda include investments in other U.S. and international subsidiaries reported separately herein.

The difference between statutory financial statements and statements prepared in accordance with GAAP varies by jurisdiction, however, the primary difference is that statutory financial statements do not reflect deferred policy acquisition costs, deferred income tax net assets, intangible assets, unrealized appreciation on investments and any unauthorized/authorized reinsurance charges.

Certain statutory restrictions on the payment of dividends from retained earnings by the Company s subsidiaries are further detailed below.

Management has evaluated the principal operating subsidiaries ability to maintain adequate levels of statutory capital, liquidity and rating agency capital and believes they will be able to do so. In performing this analysis, management has considered the current statutory capital position of each of the principal operating subsidiaries as well as the ability of the holding company to allocate capital and liquidity around the group as and when needed.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

23. Statutory Financial Data (Continued)

Bermuda Operations

In early July 2008, the Insurance Amendment Act of 2008 was passed, which introduced a number of changes to the Bermuda Insurance Act 1978, such as allowing the Bermuda Monetary Authority (BMA) to prescribe standards for an enhanced capital requirement and a capital and solvency return that insurers and reinsurers must comply with. The Bermuda Solvency Capital Requirement (BSCR) employs a standard mathematical model that can relate more accurately the risks taken on by (re)insurers to the capital that is dedicated to their business. Insurers and reinsurers may adopt the BSCR model or, where an insurer or reinsurer believes that its own internal model better reflects the inherent risk of its business, an in-house model approved by the BMA. Class 4 (re)insurers, such as the Company, were required to implement the new capital requirements under the BSCR model beginning with fiscal years ending on or after December 31, 2009. The Company s capital requirements under the BSCR are highlighted in the table above. In addition to the BSCR based requirements, the BMA also prescribes minimum liquidity standards which must be met.

Under the Insurance Act 1978, amendments thereto and related regulations of Bermuda, the Company s Bermuda subsidiaries, XL Re Ltd and XL Insurance (Bermuda) Ltd, are prohibited from declaring or paying dividends of more than 25% of each of their prior year s statutory capital and surplus, or of more than 15% of its statutory capital, unless the Company filed with the Bermuda Monetary Authority a signed affidavit by at least two members of the Company s Board of Directors and the Company s Principal Representative attesting that a dividend in excess of this amount would not cause the company to fail to meet its relevant margins. At December 31, 2011 and 2010, the maximum dividend that the Bermuda operating entities could pay, without a signed affidavit, having met minimum levels of statutory capital and surplus and liquidity requirements, was approximately $1.3 billion and $1.3 billion, respectively.

U.S. Property and Casualty Operations

Unless permitted by the New York Superintendent of Insurance, the Company s lead property and casualty subsidiary in the United States (XLRA) may not pay dividends to shareholders in an aggregate amount in any twelve month period that exceeds the lesser of 10 percent of XLRA s statutory policyholders surplus or 100 percent of its adjusted net investment income, as defined. The New York State insurance law also provides that any distribution that is a dividend may only be paid out of statutory earned surplus. At December 31, 2011, and 2010, XLRA had statutory earned surplus of $59.7 million and $184.3 million, respectively. At December 31, 2011, XLRA s statutory policyholders surplus was $2.1 billion, and accordingly, the maximum amount of dividends XLRA can declare and pay in 2012, without prior regulatory approval, is $59.7 million. At December 31, 2011 and 2010, none of the seven property and casualty subsidiaries of XLRA had a statutory earned deficit.

International Operations

The Company s international subsidiaries prepare statutory financial statements based on local laws and regulations. Some jurisdictions impose complex regulatory requirements on insurance companies while other jurisdictions impose fewer requirements. In some countries, the Company must obtain licenses issued by governmental authorities to conduct local insurance business. These licenses may be subject to reserves and minimum capital and solvency tests. Jurisdictions may impose fines, censure, and/or impose criminal sanctions for violation of regulatory requirements. The majority of the actual statutory capital outside of the U.S. and Bermuda is held in Ireland ($1.5 billion at December 31, 2011) and the U.K. ($1.1 billion at December 31, 2011). Dividends from the U.K. and Ireland are limited to the equivalent of retained earnings. As a part of the restructuring that established XL Re (Europe), the Company is required to notify the regulator in order to reduce capital levels below $1.5 billion in Ireland.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

24. Computation of Earnings Per Ordinary Share and Ordinary Share Equivalent

The following table sets forth the computation of basic and diluted earnings per share:

Year Ended December 31 *(U.S. dollars in thousands, except per share amounts)*	**2011**	**2010**	**2009**
Basic earnings per ordinary share and ordinary share equivalents:			
Net income attributable to XL Group plc.	$ (474,760)	$ 603,550	$ 74,991
Less: preference share dividends (1)		(34,694)	(80,200)
Add: gain on redemption of the Redeemable Series C preference ordinary shares		16,616	211,816
Net income (loss) attributable to ordinary shareholders	$ (474,760)	$ 585,472	$ 206,607
Weighted average ordinary shares outstanding	312,896	336,283	340,612
Basic earnings per ordinary share & ordinary share equivalents outstanding	$ (1.52)	$ 1.74	$ 0.61
Diluted earnings per ordinary share and ordinary share equivalents:			
Weighted average ordinary shares outstanding basic	$ 312,896	$ 336,283	$ 340,612
Impact of share based compensation and certain conversion features		1,426	354
Weighted average ordinary shares outstanding diluted	$ 312,896	$ 337,709	$ 340,966
Diluted earnings per ordinary share & ordinary share equivalents outstanding	$ (1.52)	$ 1.73	$ 0.61
Dividends per ordinary share	$ 0.44	$ 0.40	$ 0.40

(1) During the first quarter of 2011, the Redeemable Series C preference ordinary shares were reclassified as Non-controlling interest Redeemable Series C preference ordinary shares and Series E preference ordinary shares were reclassified as Non-controlling interest in equity of consolidated subsidiaries on the Company s consolidated balance sheet as a result of changes in ownership structure arising as part of the Company s redomestication of the ultimate parent holding company to Ireland as of July 1, 2010. Accordingly, preference share dividends declared are recorded as Non-controlling interests rather than as Preference share dividends within the consolidated statements of income from July 1, 2010 onwards. See Note 1, Basis of Preparation and Consolidation for additional details. During the third quarter of 2011, all outstanding Redeemable Series C preference ordinary shares were repurchased and canceled.

For the years ended December 31, 2011 and 2010, ordinary shares available for issuance under share based compensation plans of 16.9 million and 12.8 million, respectively, were not included in the calculation of diluted earnings per share because the assumed exercise or issuance of such shares would be anti-dilutive.

25. Related Party Transactions

At December 31, 2011 and 2010, the Company owned minority stakes in three and four, respectively, independent investment management companies (Investment Manager Affiliates) that are actively managing client capital and seeking growth opportunities. The Company sold its stake in Finisterre in the third quarter of 2011. For further information regarding this sale see Note 6(b), Investment Affiliates Operating Affiliates. The Company seeks to develop relationships with specialty investment management organizations, generally acquiring an equity interest in the business. The Company also invests in certain of the funds and limited partnerships and other legal entities managed by these affiliates and through these funds and partnerships pays management and performance fees to the Company s Investment Manager Affiliates.

In the normal course of business, the Company enters into certain quota share reinsurance contracts with a subsidiary of one of its other strategic affiliates, ARX Holding Corporation. During the years ended December 31, 2011, 2010 and 2009, these contracts resulted in reported net premiums written, net reported claims and reported acquisition costs as summarized below. Management believes that these transactions are conducted at market rates consistent with negotiated arms-length contracts.

ARX Holding Corporation:
Year Ended December 31

(U.S. dollars in thousands)	2011	2010	2009
Reported net premiums written	$ 65,347	$ 71,077	$ 44,097
Net losses incurred	$ 34,597	$ 33,098	$ 20,056
Reported acquisition costs	$ 25,268	$ 32,790	$ 19,079

In addition, the Company had entered into a reinsurance contract with another strategic affiliate, ITAU, which as outlined in Note 6, Investments in Affiliates, was sold during the second quarter of 2010. During the year ended December 31, 2009, the reinsurance contract resulted in reported net premiums of approximately $3.1 million, loss reserves of $1.2 million, and reported acquisition costs of $1.4 million.

XL GROUP PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

26. Unaudited Quarterly Financial Data

The following is a summary of the unaudited quarterly financial data for 2011 and 2010:

(U.S. dollars in thousands, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2011				
Net premiums earned property and casualty operations	$ 1,271,696	$ 1,306,125	$ 1,362,532	$ 1,386,759
Net premiums earned life operations	89,687	92,214	90,794	90,323
Underwriting profit (loss) property and casualty operations	(328,064)	67,049	(22,200)	(114,138)
Net income (loss) attributable to ordinary shareholders	(227,284)	225,663	42,398	(515,537)
Net income (loss) per ordinary share and ordinary share equivalent basic	$ (0.73)	$ 0.73	$ 0.14	$ (1.62)
Net income (loss) per ordinary share and ordinary share equivalent diluted	$ (0.73)	$ 0.69	$ 0.14	$ (1.62)
2010				
Net premiums earned property and casualty operations	$ 1,263,601	$ 1,216,313	$ 1,268,741	$ 1,282,482
Net premiums earned life operations	104,884	86,448	96,586	95,006
Underwriting profit property and casualty operations	(6,610)	94,673	64,666	109,765
Net income (loss) attributable to ordinary shareholders	127,996	191,811	77,543	188,122
Net income (loss) per ordinary share and ordinary share equivalent basic	$ 0.37	$ 0.56	$ 0.23	$ 0.58
Net income (loss) per ordinary share and ordinary share equivalent diluted	$ 0.37	$ 0.56	$ 0.23	$ 0.57

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

There have been no changes in accountants within the twenty-four months ending December 31, 2011.

ITEM 9A. CONTROLS AND PROCEDURES

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of the Company s management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of its disclosure controls and procedures pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures, as of the end of the period covered by this report, were effective to provide reasonable assurance that all material information relating to the Company required to be filed in this report has been made known to them in a timely fashion.

Management s Report on Internal Control Over Financial Reporting

The Company s management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) of the Securities Exchange Act of 1934, as amended.

The Company s internal control system was designed to provide reasonable assurance to the Company s management and board of directors regarding the preparation and fair presentation of published financial statements.

The Company s management assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2011. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework (the Framework). Based on its assessment, management concluded that, as of December 31, 2011, the Company s internal control over financial reporting is effective based on the Framework criteria.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The effectiveness of the Company s internal control over financial reporting as of December 31, 2011 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears in Item 15, Exhibits, Financial Statement Schedules.

Changes in Internal Control Over Financial Reporting

There have been no changes in internal control over financial reporting identified in connection with the Company s evaluation required pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Certain of the information required by this item relating to the executive officers of the Company may be found at the end of Part I under the heading Executive Officers of the Company. The balance of the information required by this item is omitted because a definitive proxy statement that involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A, and the information required by this item is incorporated by reference from that proxy statement.

ITEM 11. EXECUTIVE COMPENSATION

This item is omitted because the information required by this item is incorporated by reference from a definitive proxy statement that involves the election of directors that will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

This item is omitted because the information required by this item is incorporated by reference from a definitive proxy statement that involves the election of directors that will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

This item is omitted because the information required by this item is incorporated by reference from a definitive proxy statement that involves the election of directors that will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

This item is omitted because the information required by this item is incorporated by reference from a definitive proxy statement that involves the election of directors that will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

Financial Statements, Financial Statement Schedules and Exhibits.

	Page
Report of Independent Registered Public Accounting Firm	222

1. Financial Statements

Included in Part II, Item 8 of this report.

2. Financial Statement Schedules

Included in Part IV of this report:

	Schedule Number	Page
Consolidated Summary of Investments Other than Investments in Related Parties, at December 31, 2011 and 2010	I	223
Condensed Financial Information of Registrant, at December 31, 2011 and for the years ended December 31, 2011, 2010 and 2009	II	225
Reinsurance, for the years ended December 31, 2011, 2010 and 2009	IV	228
Supplementary Information Concerning Property/Casualty (Re)Insurance Operations for the years ended December 31, 2011, 2010 and 2009	VI	229

Other Schedules have been omitted as they are not applicable to the Company.

3. Exhibits

In reviewing the agreements included as exhibits to this Annual Report on Form 10-K, please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about the Company or the other parties to the agreements. The agreements contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other parties to the applicable agreement and:

- should not in all instances be treated as categorical statements of fact, but rather as a way of allocating the risk to one of the parties if those statements prove to be inaccurate;
- have been qualified by disclosures that were made to the other party in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;
- may apply standards of materiality in a way that is different from what may be viewed as material to you or other investors; and
- were made only as of the date of the applicable agreement or such other date or dates as may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time.

Exhibit	Description
3.1	Memorandum and Articles of Association of XL Group plc, incorporated by reference to Exhibit 3.1 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
3.2	Certification of Incorporation of XL Group plc, incorporated by reference to Exhibit 3.2 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
3.3	Memorandum of Association of XLIT Ltd., incorporated by reference to Exhibit 14.19 of the Company s Registration Statement on Form S-3 (No. 333-177869), filed on November 9, 2011.
3.4	Articles of Association of XLIT Ltd., incorporated by reference to Exhibit 14.20 of the Company s Registration Statement on Form S-3 (No. 333-177869), filed on November 9, 2011.
4.1	Excerpts from the Minutes of a Meeting of a Committee of the Board of Directors pursuant to Article 75 of XL Capital Ltd s Articles of Association held on March 15, 2007, incorporated by reference to Exhibit 4.2 to the Company s Current Report on Form 8-K (No. 1-10804) filed on March 15, 2007.
4.2	Indenture, dated as of January 23, 2003, between XL Capital Ltd and U.S. Bank National Association, as Trustee, incorporated by reference to Exhibit 4.1 to the Company s Amendment No. 1 to Registration Statement on Form S-3 (No. 333-101288) filed on January 23, 2003.
4.3	Indenture, dated as of June 2, 2004, between XL Capital Ltd and The Bank of New York, as Trustee, incorporated by reference to Exhibit 4.1 to the Company s Registration Statement on Form S-3 (No. 333-116245) filed on June 7, 2004.
4.4	First Supplemental Indenture, dated as of August 23, 2004, to the Indenture, dated as of June 2, 2004, between XL Capital Ltd and The Bank of New York, as Trustee, incorporated by

	reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 23, 2004.
4.5	Form of 5.25% Senior Note due 2014 (included in Exhibit 4.3 hereto), incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 23, 2004.
4.6	Second Supplemental Indenture, dated as of November 12, 2004, to the Indenture, dated as of June 2, 2004, between XL Capital Ltd and The Bank of New York, as Trustee, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on November 15, 2004.
4.7	Form of 6.375% Senior Note due 2024 (included in Exhibit 4.6 hereto), incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on November 15, 2004.

4.8	Third Supplemental Indenture, dated as of December 9, 2005, to the Indenture, dated as of June 2, 2004, between XL Capital Ltd and The Bank of New York, as trustee, incorporated by reference to Exhibit 4.2 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 12, 2005.
4.9	Fourth Supplemental Indenture, dated May 7, 2007, to the Indenture, dated as of June 2, 2004, between XL Capital Ltd, and The Bank of New York, as trustee, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on May 7, 2007.
4.10	Form of 6.25% Senior Note due 2027 (included in Exhibit 4.9 hereto), incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on May 7, 2007.
4.11	Form of XL Group plc Ordinary Share Certificate, incorporated by reference to Exhibit 4.5 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
4.12*	Excerpts from the Authorizing Resolutions of the Board of Directors of XL Capital Ltd, dated October 27, 2006.
4.13	Indenture, dated as of January 10, 2002, among XL Capital Finance (Europe) plc, XL Capital Ltd and State Street Bank and Trust Company, incorporated by reference to Exhibit 4.16(a) to the Company s Current Report on Form 8-K (No. 1-10804) filed on January 14, 2002.
4.14	Form of XL Capital Financial (Europe) plc Debt Security, incorporated by reference to Exhibit 4.14 to the Company s Current Report on Form 8-K (No. 1-10804) filed on January 14, 2002.
4.15	Excerpts from the Authorizing Resolutions of the Board of Directors of XL Capital Finance (Europe) plc, dated January 7, 2002, incorporated by reference to Exhibit 4.16(b) to the Company s Current Report on Form 8-K (No. 1-10804) filed on January 14, 2002.
4.16	Excerpts from the Authorizing Resolutions of the Special Finance Committee of XL Capital Ltd, dated July 3, 2003, incorporated by reference to Exhibit 99.11 to the Company s Quarterly Report on Form 10-Q (No. 1-10804) filed on August 14, 2003.
4.17	Form of 5.25% Senior Note due 2011 (included in Exhibit 4.8 hereto), incorporated by reference to Exhibit 4.8 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 12, 2005.
4.18	Fifth Supplemental Indenture, dated August 5, 2008, to the Indenture, dated as of June 2, 2004, between XL Capital Ltd and The Bank of New York Mellon, as trustee, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.19	Purchase Contract Agreement, dated August 5, 2008, between Xl Capital Ltd and The Bank of New York Mellon, as Purchase Contract Agent, incorporated by reference to Exhibit 4.2 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.20	Pledge Agreement, dated August 5, 2008, by and among XL Capital Ltd and the Bank of New York Mellon, as Collateral Agent, Custodial Agent, Securities Intermediary and Purchase Contract Agent, incorporated by reference to Exhibit 4.3 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.21	Form of Normal Units Certificate (included in Exhibit 4.19 hereto), incorporated by reference to Exhibit 4.5 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.22	Form of Stripped Units Certificate (included in Exhibit 4.19 hereto), incorporated by reference to Exhibit 4.6 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.23	Form of 8.25% Senior Note due 2021 (included in Exhibit 4.18 hereto), incorporated by reference to Exhibit 4.7 to the Company s Current Report on Form 8-K (No. 1-10804) filed on August 6, 2008.
4.24	Sixth Supplemental Indenture, dated as of June 30, 2010, to the Indenture, dated as of June 2, 2004, and the Fifth Supplemental Indenture, date as of August 5, 2008, between XL Capital Ltd, XL Group plc, as guarantor and the Bank of New York Mellon, as trustee, incorporated by reference to Exhibit 4.3 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.

4.25	First Amendment, dated as of June 30, 2010, to the Pledge Agreement, dated August 5, 2008, by and among XL Capital Ltd, XL Company Switzerland GmbH and The Bank of New York Mellon, as Collateral Agent, Custodial Agent and Securities Intermediary and Purchase Contract Agent, incorporated by reference to Exhibit 4.2 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
4.26	First Amendment, dated as of June 30, 2010, to the Purchase Contract Agreement, dated August 5, 2008, between the Registrant, XL Capital Ltd, XL Company Switzerland GmbH and The Bank of New York Mellon, as Purchase Contract Agent, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
4.27	Supplemental Indenture, dated as of June 30, 2010, to the Indenture, dated as of January 10, 2002, among XL Capital Finance (Europe) plc, XL Capital Ltd, XL Company Switzerland GmbH and State Street Bank and Trust Company, incorporated by reference to Exhibit 4.4 to the Company s Current Report on Form 8-K12B (No. 1-10804) filed on July 1, 2010.
4.28	Form of XL Capital Ltd Global Series E Preference Share Certificate, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on March 15, 2007.
4.29*	Form of XLIT Ltd. Global Series D Preference Ordinary Share Certificate.
10.1+	1991 Performance Incentive Plan (as amended and restated effective March 7, 2003), incorporated by reference to Appendix B to the Company s Definitive Proxy Statement on Schedule 14A (No. 1-10804) filed on April 4, 2003.
10.2+	1991 Performance Incentive Program (as amended and restated effective April 29, 2005), incorporated by reference to Appendix C to the Company s Definitive Proxy Statement on Schedule 14A (No. 1-10804) filed on March 24, 2005.
10.3+	1991 Performance Incentive Program (as amended and restated effective February 27, 2009), incorporated by reference to Appendix B to the Company s Definitive Proxy Statement on Schedule 14A (No. 1-10804) filed on March 9, 2009.
10.4+	1991 Performance Incentive Program (as amended and restated effective April 30, 2010), incorporated by reference to Exhibit 10.1 to the Company s Quarterly Report on Form 10-Q (No. 1-10804) for the period ended June 30, 2010.
10.5+	Amended and Restated Directors Stock & Option Plan, incorporated by reference to Appendix C to the Company s Definitive Proxy Statement on Schedule 14A (No. 1-10804) filed on April 4, 2003.
10.6+	Amended and Restated Directors Stock & Option Plan, effective as of January 1, 2009, incorporated by reference to Appendix C to the Company s Definitive Proxy Statement on Schedule 14A (No. 1-10804) filed on March 9, 2009.
10.7+	Amended and Restated Directors Stock & Option Plan, effective as of April 30, 2010, incorporated by reference to Exhibit 10.2 to the Company s Quarterly Report on Form 10-Q (No. 1-10804) for the period ended June 30, 2010.
10.8+	Employment Agreement, dated as of September 29, 2006, between XL Capital Ltd and Sarah E. Street, incorporated by reference to Exhibit 10.1 to the Company s quarterly report on Form 10-Q for the period ended September 30, 2006 (No. 1-10804).
10.9+	Form of Non-Statutory Stock Option Agreement (One-Time Vesting), incorporated by reference to Exhibit 10.45 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.10+	Form of Non-Statutory Stock Option Agreement (Incremental Vesting), incorporated by reference to Exhibit 10.5 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804)
10.11+	Form of Non-Statutory Stock Option Agreement (Incremental Vesting), incorporated by reference to Exhibit 10.5 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.12+	Form of Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.6 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.13+	Form of Restricted Stock Agreement, incorporated by reference to Exhibit 10.7 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.14+	Form of Non-Statutory Stock Option Agreement (Renewal Form), incorporated by reference to Exhibit 10.8 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).

10.15+	Form of Non-Statutory Stock Option Agreement (Non-Employee Director Renewal Form), incorporated by reference to Exhibit 10.9 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).

10.16+	Form of Directors Restricted Stock Agreement, incorporated by reference to Exhibit 10.10 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.17+	Form of Performance Restricted Stock Agreement, incorporated by reference to Exhibit 10.11 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.18+	Form of Performance Restricted Stock Unit Agreement, incorporated by reference to Exhibit 10.12 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.19+	Form of Performance Unit Agreement, incorporated by reference to Exhibit 10.8 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.20+	Form of Performance Unit Agreement, incorporated by reference to Exhibit 10.9 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.21+	Form of Restricted Stock Unit Agreement, incorporated by reference to Exhibit 10.13 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.22+	Form of Restricted Stock Unit Agreement, incorporated by reference to Exhibit 10.6 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.23+	Form of Restricted Stock Unit Agreement (for U.S. taxpayers based in Bermuda), incorporated by reference to Exhibit 10.7 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.24+	Form of Director Stock Option Agreement, incorporated by reference to Exhibit 10.14 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2004 (No. 1-10804).
10.25	Insurance Letters of Credit Master Agreement between XL Mid Ocean Reinsurance Ltd and Citibank, N.A., dated May 19, 1993, incorporated by reference to Exhibit 10.33 to Amendment No. 2 to the Registration Statement on Form S-1 of Mid Ocean Limited (No. 333-63298) filed on June 25, 1993.
10.26	Second Amended and Restated Agreement for the Sale and Purchase of Winterthur International, dated as of February 15, 2001, between Winterthur Swiss Insurance Company and XL Insurance (Bermuda) Ltd (formerly XL Insurance Ltd), incorporated by reference to Exhibit 99(a) to the Company s Current Report on Form 8-K (No. 1-10804) filed August 9, 2001.
10.27	Amendment Agreement, dated July 19, 2002, between Winterthur Swiss Insurance Company and XL Insurance (Bermuda) Ltd, incorporated by reference to Exhibit 10.58 to the Company s Annual Report on Form 10-K for the year ended December 31, 2002 (No. 1-10804).
10.28	Pledge Agreement, dated as of December 18, 2001, made by XL Investments Ltd, XL Re Ltd, XL Insurance (Bermuda) Ltd and XL Europe Ltd, as Grantors, in favor of Citibank, N.A., as Bank, incorporated by reference to Exhibit 10.54 to the Company s Annual Report on Form 10-K for the year ended December 31, 2001 (No. 1-10804).
10.29	Amendment No. 1, dated as of June 24, 2002, to the Pledge Agreement, dated December 18, 2001, made by XL Investments Ltd, XL Re Ltd, XL Insurance (Bermuda) Ltd, and XL Europe Ltd, as Grantors, in favor of Citibank, N.A., as Bank, incorporated by reference to Exhibit 10.67 to the Company s Quarterly Report on Form 10-Q for the period ended September 30, 2003 (No. 1-10804).
10.30	Replacement Capital Covenant, dated March 15, 2007, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on March 15, 2007.
10.31	Service Agreement Relative to Sureties, Letters of Guarantees and International Stand-By Letters of Credit, dated April 25, 2003, between Société Le Mans Re and Credit Lyonnais, incorporated by reference to Exhibit 10.62 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2003 (No. 1-10804).
10.32	First Renewal, dated November 27, 2000, between Le Mans Re and BNP Paribas, to the Reinsurance Stand-By Letter of Credit Agreement, dated October 7, 1999, incorporated by reference to Exhibit 10.63 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2003 (No. 1-10804).

10.33	Master Commutation, Release and Restructuring Agreement by and among XL Capital Ltd, XL Insurance (Bermuda) Ltd, XL Reinsurance America Inc., X.L. Global Services, Inc., XL Services (Bermuda) Ltd and X.L. America, Inc., Security Capital Assurance Ltd (SCA), certain of SCA s subsidiaries and certain financial institutions who have entered into various credit default swaps with affiliates of SCA, dated as of July 28, 2008, as amended, incorporated by reference to Exhibit 10.10 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.34+	Employment Agreement, dated as of March 14, 2008 by and between XL Capital Ltd and Michael S. McGavick, incorporated by reference to Exhibit 10.1 to the Company s Quarterly Report on Form 10-Q for the period ended March 30, 2008 (No. 1-10804).
10.35+	Agreement and Release, dated November 29, 2011, between XL Group plc and David B. Duclos, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on December 1, 2011 (No. 1-10804).
10.36+	Consulting Agreement, dated November 29, 2011, between XL Group plc, XL Specialty Insurance Company, Inc. and David B. Duclos, incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K filed on December 1, 2011 (No. 1-10804).
10.37	Consulting Agreement, dated as of April 24, 2009, between XL Capital Ltd and Brian O Hara, incorporated by reference to Exhibit 10.3 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.38+	2008 Form of Employment Agreement between XL Capital Ltd and certain Executive Officers, incorporated by reference to Exhibit 10.4 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.39+	2008 Form of Amendment to Employment Agreement between XL Capital Ltd and certain Executive Officers (amended in response to Internal Revenue Code Section 457A), incorporated by reference to Exhibit 10.5 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1- 10804).
10.40+	2009 Form of Employment Agreement between XL Capital Ltd and certain Executive Officers, incorporated by reference to Exhibit 10.6 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.41+	Amended Employment Agreement, dated as of April 25, 2008, by and between XL Capital Ltd, X.L. Global Services, Inc. and James H. Veghte (amended in response to Internal Revenue Code Section 409A), incorporated by reference to Exhibit 10.7 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.42+	Amendment to Employment Agreement, dated as of December 2008, between XL Capital Ltd and Michael S. McGavick (amended in response to Internal Revenue Code Section 457A), incorporated by reference to Exhibit 10.9 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (No. 1-10804).
10.43+	Agreement and Release between XL Capital Ltd and Brian W. Nocco, dated as of November 3, 2009, incorporated by reference to Exhibit 10.1 to the Company s Quarterly Report on Form 10-Q for the period ended September 30, 2009 (No. 1-10804).
10.44+	Amendment to Employment Agreement, dated as of December 16, 2009, by and between XL Capital Ltd and Sarah E. Street, incorporated by reference to Exhibit 10.52 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009 (No. 1-10804).
10.45+	Form of Letter Agreement, dated December 15, 2009, relating to Employment Agreements between XL Capital Ltd and certain Executive Officers, incorporated by reference to Exhibit 10.52 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009 (No. 1-10804).
10.46	Insurance Letters of Credit Master Agreement, dated November 11, 2009, between XL Insurance (Bermuda) Ltd and Citibank Europe plc, incorporated by reference to Exhibit 10.52 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009 (No. 1-10804).
10.47	Pledge Agreement, dated November 11, 2009, between XL Re Ltd and XL Insurance (Bermuda) Ltd, as Pledgors, and Citibank Europe plc, as Pledgee, incorporated by reference to Exhibit 10.52 to the Company s Annual Report on Form

	10-K for the year ended December 31, 2009 (No. 1-10804).
10.48	Amendment No. 1, dated November 23, 2009, to Pledge Agreement dated November 11, 2009 between XL Re Ltd and XL Insurance (Bermuda) Ltd, as Pledgors, and Citibank Europe plc, as Pledgee, incorporated by reference to Exhibit 10.52 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009 (No. 1-10804).
10.49	Amendment No. 2, dated December 23, 2009, to Pledge Agreement dated November 11, 2009 between XL Re Ltd and XL Insurance (Bermuda) Ltd, as Pledgors, and Citibank Europe plc, as Pledgee, incorporated by reference to Exhibit 10.57 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009 (No. 1-10804).
10.50+	Form of Indemnification Agreement, dated July 1, 2010, by and between XL Capital Ltd and certain directors and executive officers of the Company, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K12B filed on July 1, 201 (No. 1-10804).
10.51+	Deed Poll Indemnity, dated July 1, 2010, by XL Capital Ltd, incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K12B filed on July 1, 2010 (No. 1-10804).
10.52+	Employment Agreement, dated as of May 6, 2010, between XL Capital Ltd and Irene M. Esteves, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on May 6, 2010 (No. 1-10804).
10.53+	Supplemental Deferred Compensation Plan, amended and restated effective as of January 1, 2007, incorporated by reference to Exhibit 10.3 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.54+	2009 Cash Long Term Program, amended and restated as of April 30, 2010, incorporated by reference to Exhibit 10.4 to the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (No. 1-10804).
10.55	Aircraft Time Sharing Agreement, dated February 22, 2011, between Michael S. McGavick and X.L. America, Inc, incorporated by reference to Exhibit 10.63 to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10.56	Credit Agreement, dated as of March 25, 2011, between XL Group plc, XL Group Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Account Parties, XL Group plc, XL Group Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd and XL Life Ltd, as Guarantors, the Lenders party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and The Bank of New York Mellon, as Collateral Agent, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on March 28, 2011 (No. 1-10804).
10.57	Pledge Agreement, dated as of March 25, 2011, between XL Group plc, XL Group Ltd., X.L. America, Inc., Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Pledgors, JPMorgan Chase Bank, N.A., as Administrative Agent, and The Bank of New York Mellon, as Collateral Agent, incorporated by reference to Exhibit 10.3 to the Company s Current Report on Form 8-K filed on March 28, 2011 (No. 1-10804).
10.58+	XL Services UK Limited Profit Sharing Scheme, incorporated by reference to Exhibit 4.3 to the Company s Registration Statement on Form S-8 filed on May 11, 2011 (No. 333-174138).
10.59+	Employment Agreement, dated as of June 18, 2011, by and between XL Group plc, X.L. Global Services, Inc. and Peter R. Porrino, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on June 21, 2011.
10.60	Indenture, dated September 30, 2011, among XL Group plc, XL Group Ltd. (n/k/a XLIT Ltd.) and Wells Fargo Bank, National Association, as Trustee, incorporated by reference to Exhibit 4.1 to the Company s Current Report on Form 8-K filed on September 30, 2011 (No. 1-10804).
10.61	First Supplemental Indenture, dated September 30, 2011 to the Indenture dated September 30, 2011 among XL Group plc, XL Group Ltd. (n/k/a XLIT Ltd.) and Wells Fargo Bank, National Association, as Trustee, incorporated by reference to Exhibit 4.2 to the Company s Current Report on Form 8-K filed on September 30, 2011 (No. 1-10804).
10.62	Form of 5.75% Senior Note due 2021, incorporated by reference to Exhibit 4.2 to the Company s Current Report on

	Form 8-K filed on September 30, 2011 (No. 1-10804).
10.63	Secured Credit Agreement, dated as of December 9, 2011, between XL Group plc, XLIT Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Account Parties, XL Group plc, XLIT Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd and XL Life Ltd, as Guarantors, the Lenders party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and The Bank of New York Mellon, as Collateral Agent, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on December 12, 2011.
10.64	Unsecured Credit Agreement, dated as of December 9, 2011, between XL Group plc, XLIT Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Account Parties, XL Group plc, XLIT Ltd., X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd and XL Life Ltd, as Guarantors, the Lenders party thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent, incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K filed on December 12, 2011.
10.65	Amendment, dated as of December 9, 2011, to the Credit Agreement, dated as of March 25, 2011, between XL Group plc, XLIT Ltd. (formerly XL Group Ltd.), X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Account Parties, XL Group plc, XLIT Ltd. (formerly XL Group Ltd.), X.L. America, Inc., XL Insurance (Bermuda) Ltd, XL Re Ltd and XL Life Ltd, as Guarantors, the Lenders party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and The Bank of New York Mellon, as Collateral Agent, incorporated by reference to Exhibit 10.3 to the Company s Current Report on Form 8-K filed on December 12, 2011.
10.66	Pledge Agreement, dated as of December 9, 2011, between XL Group plc, XLIT Ltd., X.L. America, Inc., Insurance (Bermuda) Ltd, XL Re Ltd, XL Re Europe Limited, XL Insurance Company Limited, XL Insurance Switzerland Ltd and XL Life Ltd, as Pledgors, JPMorgan Chase Bank, N.A., as Administrative Agent, and The Bank of New York Mellon, as Collateral Agent, incorporated by reference to Exhibit 10.4 to the Company s Current Report on Form 8-K filed on December 12, 2011.
10.67+*	Form of Letter Agreement between XL Global Services, Inc. and/or XL Group plc and certain executive officers.
10.68	Subscription Agreement, dated as of December 5, 2006, among XL Capital Ltd, Stoneheath Re and Goldman Sachs International, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 11, 2006.
10.69	Excess of Loss Reinsurance Agreement, dated as of December 12, 2006, by and among XL Insurance (Bermuda) Ltd, XL Insurance Switzerland, XL Europe Limited, XL Insurance Company Limited, XL Re Latin America Ltd, XL Insurance Argentina S.A. Compania de Seguros, XL Insurance Company Ltd, XL Re Ltd, XL Re Europe Limited, Vitodurum Reinsurance Company, Underwriting Members of Lloyd s Syndicate #1209 and Stoneheath Re, incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 12, 2006.
10.70	Securities Issuance Agreement, dated as of December 12, 2006, between XL Capital Ltd and Stoneheath Re, incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 12, 2006.
10.71	Trust Agreement, dated as of December 12, 2006 among the Asset Swap Counterparty, The Ceding Insurers and XL Capital Ltd as Beneficiaries and Stoneheath Re, as Guarantor and Beneficiary and The Bank of New York, as Trustee, incorporated by reference to Exhibit 10.3 to the Company s Current Report on Form 8-K (No. 1-10804) filed on December 12, 2006.
31*	Rule 13a-14(a)/15d-14(a) Certifications.
32*	Section 1350 Certifications.
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document

101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document

* Filed herewith

** These interactive data files are furnished herewith and deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Act of 1933, as amended, and otherwise are not subject to liability under those sections.

\+ Management contract or compensatory plan or arrangement

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of XL Group plc:

In our opinion, the consolidated financial statements listed in the index appearing under Item 15 (1), present fairly, in all material respects, the financial position of XL Group plc and its subsidiaries at December 31, 2011 and 2010 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the index appearing under Item 15 (2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management s Report on Internal Control over Financial Reporting, Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedules, and on the Company s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 2(g) to the consolidated financial statements, the Company adopted new accounting guidance that changed the manner in which it accounts for other-than-temporary impairments of available for sale securities in 2009.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP
New York, New York
February 27, 2012

XL GROUP PLC

SCHEDULE I
CONSOLIDATED SUMMARY OF INVESTMENTS OTHER THAN INVESTMENTS IN RELATED PARTIES

At December 31, 2011

Type of Investment *(U.S. dollars in thousands)*	Cost or Amortized Cost (1)	Fair Value	Amount Presented in the Balance Sheet
Fixed Maturities:			
Bonds and notes:			
U.S. Government and Government-Related/Supported	$ 1,864,354	$ 1,990,983	$ 1,990,983
Corporate	10,212,083	10,462,515	10,462,515
Residential mortgage-backed securities Agency	5,189,473	5,379,406	5,379,406
Residential mortgage-backed securities Non-Agency	851,557	641,815	641,815
Commercial mortgage-backed securities	927,684	974,835	974,835
Collateralized debt obligations	843,553	658,602	658,602
Other asset-backed securities Government	995,903	986,356	986,356
U.S. States and political subdivisions of the States	1,698,573	1,797,378	1,797,378
Non-U.S. Sovereign Government, Supranational and Government-Related	3,188,535	3,298,135	3,298,135
Total fixed maturities (1)	$ 25,771,715	$ 26,190,025	$ 26,190,025
Equity Securities	$ 480,685	$ 468,197	$ 468,197
Short-term investments (1)	$ 359,378	$ 359,063	$ 359,063
Fixed maturities, held to maturity (1)	$ 2,668,978	$ 2,895,688	$ 2,668,978
Other investments	$ 849,511	$ 958,681	$ 985,262
Total investments other than investments in related parties	$ 30,130,267	$ 30,871,654	$ 30,671,525

(1) Investments in fixed maturities, short-term investments and held to maturity are shown at amortized cost.

XL GROUP PLC

SCHEDULE I
CONSOLIDATED SUMMARY OF INVESTMENTS OTHER THAN INVESTMENTS IN RELATED PARTIES (CONTINUED)

At December 31, 2010

Type of Investment *(U.S. dollars in thousands)*	Cost or Amortized Cost (1)	Fair Value	Amount Presented in the Balance Sheet
Fixed Maturities:			
Bonds and notes:			
U.S. Government and Government-Related/Supported	$ 2,499,079	$ 2,565,444	$ 2,565,444
Corporate	10,962,804	10,968,971	10,968,971
Residential mortgage-backed securities Agency	5,059,249	5,203,711	5,203,711
Residential mortgage-backed securities Non-Agency	1,257,474	1,021,823	1,021,823
Commercial mortgage-backed securities	1,135,075	1,172,507	1,172,507
Collateralized debt obligations	920,501	734,138	734,138
Other asset-backed securities Government	979,539	960,532	960,532
U.S. States and political subdivisions of the States	1,379,150	1,360,456	1,360,456
Non-U.S. Sovereign Government, Supranational and Government-Related	3,129,971	3,154,523	3,154,523
Total fixed maturities (1)	$ 27,322,842	$ 27,142,105	$ 27,142,105
Equity Securities	$ 56,737	$ 84,767	$ 84,767
Short-term investments (1)	$ 450,491	$ 450,681	$ 450,681
Fixed maturities, held to maturity (1)	$ 2,728,335	$ 2,742,626	$ 2,728,335
Other investments	$ 789,917	$ 883,409	$ 893,570
Total investments other than investments in related parties	$ 31,348,322	$ 31,303,588	$ 31,299,458

(1) Investments in fixed maturities, short-term investments and held to maturity are shown at amortized cost.

XL GROUP PLC

SCHEDULE II
CONDENSED FINANCIAL INFORMATION OF REGISTRANT
CONDENSED BALANCE SHEETS PARENT COMPANY ONLY

As at December 31, 2011 and 2010

(U.S. dollars in thousands)	2011	2010
Assets		
Cash and cash equivalents	$ 1,644	$ 2,816
Amounts due from subsidiaries	80,841	
Investments in subsidiaries on an equity basis	9,374,825	9,750,149
Other assets	3,797	901
Total assets	$ 9,461,107	$ 9,753,866
Liabilities		
Amounts due to subsidiaries (1)	$	$ 125,052
Accounts payable and accrued liabilities	19,145	1,857
Total liabilities	$ 19,145	$ 126,909
Commitments and Contingencies		
Shareholders Equity:		
Ordinary shares, 999,990,000 authorized, par value $0.01 Issued and outstanding: (2011, 315,645,796; 2010, 316,396,289)	$ 3,157	$ 3,165
Additional paid in capital	8,955,702	9,009,220
Accumulated other comprehensive Income (loss)	583,064	100,795
Retained earnings (deficit)	(99,961)	513,777
Total shareholders equity	$ 9,441,962	$ 9,626,957
Total liabilities and shareholders equity	$ 9,461,107	$ 9,753,866

XL GROUP PLC

SCHEDULE II
CONDENSED FINANCIAL INFORMATION OF REGISTRANT (CONTINUED)
STATEMENT OF INCOME AND COMPREHENSIVE INCOME PARENT COMPANY ONLY

For the Years Ended December 31, 2011, 2010 and 2009

(U.S. dollars in thousands)	XL Group plc		XLIT Ltd. (1)	
	Year Ended December 31, 2011	July 1 to December 31, 2010	January 1 to June 30, 2010	Year Ended December 31, 2009
Net investment income	$ 2	$	$ 44,636	$ 20,245
Realized investment gains (losses):				
Net realized gains (losses) on investments sold			25,177	(5,453)
Other-than-temporary impairments on investments			(11,670)	(8,468)
Other-than-temporary impairments on investments transferred to other comprehensive income			4	1,319
Total net realized gains (losses) on investments			13,511	(12,602)
Net realized and unrealized gains (losses) on derivative instruments			(4,087)	(8,830)
Equity in net earnings (losses) of subsidiaries (Dividends were $183,029 in 2011 $197,326 and $448,400 in 2010 and $2,091,474 in 2009)	(400,612)	275,629	384,311	310,490
Equity in net earnings of affiliates			2	1,221
Total revenues	$ (400,610)	$ 275,629	$ 438,373	$ 310,524
Operating expenses	74,422	9,930	48,256	107,211
Foreign exchange (gains) losses	(275)	34	1,003	(122)
Interest expense	3		51,431	122,662
Total expenses	$ 74,150	$ 9,964	$ 100,690	$ 229,751
Income (loss) before income tax	(474,760)	265,665	337,683	80,773
Provision for income tax			(202)	5,782
Net income (loss)	$ (474,760)	$ 265,665	$ 337,885	$ 74,991
Preference share dividends			(34,694)	(80,200)
Gain on redemption of Redeemable Series C preference ordinary shares			16,616	211,816
Net income (loss) attributable to ordinary shareholders	$ (474,760)	$ 265,665	$ 319,807	$ 206,607
Net income (loss)	$ (474,760)	$ 265,665	$ 337,885	$ 74,991
Impact of adoption of new authoritative OTTI guidance, net of taxes				(229,670)
Impact of adoption of new authoritative embedded derivative guidance, net of taxes		31,917		
Change in net unrealized gains (losses) on investment portfolio, net of tax	471,696	161,048	880,332	2,391,020
Change in OTTI losses recognized in other comprehensive income, net of tax	39,456	93,269	31,637	(123,343)

Change in underfunded pension liability	(2,622)	(6,186)	3,567	(3,427)
Change in value of cash flow hedge	439	219	220	438
Change in net unrealized gains (losses) on future policy benefit reserves			(3,714)	6,554
Foreign currency translation adjustments	(26,700)	159,261	(108,308)	180,888
Comprehensive income (loss)	$ 7,509	$ 705,193	$ 1,141,619	$ 2,297,451

(1) As part of the Redomestication on July 1, 2010, XL-Cayman became a wholly-owned subsidiary of XL-Ireland, and as such, certain of the above financial data with respect to periods prior to the Redomestication are not comparable for periods subsequent to the Redomestication.

XL GROUP PLC

SCHEDULE II
CONDENSED FINANCIAL INFORMATION OF REGISTRANT (CONTINUED)
STATEMENT OF CASH FLOWS PARENT COMPANY ONLY
For the Years Ended December 31, 2011, 2010 and 2009

(U.S. dollars in thousands)	XL Group plc		XLIT Ltd. (1)	
	Year Ended December 31, 2011	July 1 to December 31, 2010	January 1 to June 30, 2010	Year Ended December 31, 2009
Net income (loss)	$ (474,760)	$ 265,665	$ 337,885	$ 74,991
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:				
Net realized (gains) losses on investments and derivative instruments			(9,423)	21,432
Equity in (earnings) loss of subsidiaries	400,612	(275,629)	(384,311)	(310,490)
Equity in net (income) of affiliates			(2)	(1,221)
Share based compensation	29,377	15,705	15,586	32,231
Amortization of premiums (discounts) on fixed maturities			(9,791)	221
Accretion of notes payable and debt			341	681
Accounts payable and accrued liabilities			(24,973)	(57,806)
Amounts due to (from) subsidiaries	(205,893)	125,052	(183,273)	(3,259,462)
Dividends received from subsidiaries	183,029	448,400	197,326	2,091,474
Other	22,804	7,914	30,936	17,432
Total adjustments	429,929	321,442	(367,584)	(1,465,508)
Net cash provided by (used in) operating activities	$ (44,831)	$ 587,107	$ (29,699)	$ (1,390,517)
Cash flows provided by (used in) investing activities:				
Proceeds from sale of fixed maturities and short-term investments	$	$	$ 369,752	$ 245,629
Proceeds from redemption of fixed maturities and short-term investments			575,326	2,860,755
Proceeds from sale of equity securities			238	
Purchases of fixed maturities and short term investments			(919,840)	(4,475,472)
Investment in subsidiaries	272,398		298,119	1,955,045
Investment in affiliates			5	1,743
Investment in limited partnerships			95	347
Net cash provided by (used in) investing activities	$ 272,398	$	$ 323,695	$ 588,047
Cash flows provided by (used in) financing activities:				
Proceeds from issuance of ordinary shares and exercise of stock options	$ 576,333	$ 1,182	$	$ 745,000
Repurchase of Series E preference ordinary shares			(94,157)	(104,718)
Dividends paid	(138,050)	(65,350)	(106,471)	(225,008)
Buybacks of ordinary shares	(667,022)	(520,184)	(1,840)	(626)
Repayment of debt				(745,000)
Net cash provided by (used in) financing activities	$ (228,739)	$ (584,352)	$ (202,468)	$ (330,352)
Net change in cash and cash equivalents	(1,172)	2,755	91,528	(1,132,822)

Cash and cash equivalents	beginning of period	2,816	61	600,993	1,733,815
Cash and cash equivalents	**end of period**	$ 1,644	$ 2,816	$ 692,521	$ 600,993

(1) As part of the Redomestication on July 1, 2010, XL-Cayman became a wholly-owned subsidiary of XL-Ireland, and as such, certain of the above financial data with respect to periods prior to the Redomestication are not comparable for periods subsequent to the Redomestication.

XL GROUP PLC

SCHEDULE IV REINSURANCE

For the Years Ended December 31, 2011, 2010 and 2009

(U.S. dollars in thousands)	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percentage of Amount Assumed to Net
2011					
Life reinsurance in force(1)	$	$ 559,676	$ 88,646,215	$ 88,086,538	100.6%
Premiums Earned:					
Property and casualty operations	$ 4,624,557	$ 1,477,000	$ 2,179,555	$ 5,327,112	40.9%
Life operations		32,308	395,326	363,018	108.9%
Total premiums earned:	$ 4,624,557	$ 1,509,308	$ 2,574,881	$ 5,690,130	45.3%
2010					
Life reinsurance in force(1)	$	$ 559,674	$ 100,908,397	$ 100,348,723	100.6%
Premiums Earned:					
Property and casualty operations	$ 4,535,626	$ 1,342,017	$ 1,837,528	$ 5,031,137	36.5%
Life operations		32,226	415,150	382,924	108.4%
Total premiums earned:	$ 4,535,626	$ 1,374,243	$ 2,252,678	$ 5,414,061	41.6%
2009					
Life reinsurance in force(1)	$	$ 565,048	$ 129,797,640	$ 129,232,592	100.4%
Premiums Earned:					
Property and casualty operations	$ 4,861,073	$ 1,586,968	$ 1,877,634	$ 5,151,739	36.4%
Life operations		41,275	596,376	555,101	107.4%
Total premiums earned:	$ 4,861,073	$ 1,628,243	$ 2,474,010	$ 5,706,840	43.4%

(1) Represents the sum face value outstanding of in force life reinsurance policies.

XL GROUP PLC

SCHEDULE VI
SUPPLEMENTARY INFORMATION
CONCERNING PROPERTY/CASUALTY (RE)INSURANCE OPERATIONS

For the Years Ended December 31, 2011, 2010 and 2009

(U.S. dollars in thousands)	Deferred Acquisition Costs	Reserves For Losses and Loss Expenses	Reserves for Unearned Premiums	Net Earned Premiums	Net Investment Income	Losses and Loss Expenses incurred related to		Net Paid Losses and Loss Expenses	Amortization of Deferred Acquisition Costs	Net Premiums Written
						Current Year	Prior Year			
2011(1)	$ 531,282	$ 20,613,901	$ 3,555,310	$ 5,327,112	$ 745,138	$ 4,363,258	$ (284,867)	$ 3,846,202	$ 786,093	$ 5,433,388
2010(1)	$ 498,385	$ 20,531,607	$ 3,469,934	$ 5,031,137	$ 803,358	$ 3,584,662	$ (372,862)	$ 3,470,509	$ 739,154	$ 4,999,588
2009(1)	$ 486,180	$ 20,823,524	$ 3,646,815	$ 5,151,739	$ 882,748	$ 3,453,577	$ (284,740)	$ 3,875,935	$ 775,869	$ 4,743,712

(1) The information presented above includes P&C Operations balances only.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: February 27, 2012

XL Group plc
(Registrant)

/s/ Michael S. McGavick

Name: Michael S. McGavick
Title: Chief Executive Officer and Director
XL Group plc

Date: February 27, 2012

/s/ Peter R. Porrino

Name: Peter R. Porrino
Title: Chief Financial Officer
XL Group plc

POWER OF ATTORNEY

We, the undersigned directors and executive officers of XL Group plc, hereby severally constitute Michael S. McGavick, Peter R. Porrino and Kirstin Gould, and each of them singly, our true and lawful attorneys with full power to them and each of them to sign for us, and in our names in the capacities indicated below, any and all amendments to the Annual Report on Form 10-K filed with the Securities and Exchange Commission, hereby ratifying and confirming our signatures as they may be signed by our said attorneys to any and all amendments to said Annual Report on Form 10-K.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signatures	Title	Date
/s/ Michael S. McGavick	Chief Executive Officer (Principal Executive Officer) and Director	February 27, 2012
Michael S. McGavick		
/s/ Peter R. Porrino	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	February 27, 2012
Peter R. Porrino		
/s/ Ramani Ayer	Director	February 27, 2012
Ramani Ayer		
/s/ Dale R. Comey	Director	February 27, 2012
Dale R. Comey		
/s/ Robert R. Glauber	Director and Chairman of the Board of Directors	February 27, 2012
Robert R. Glauber		
/s/ Herbert N. Haag	Director	February 27, 2012
Herbert N. Haag		
/s/ Suzanne B. Labarge	Director	February 27, 2012
Suzanne B. Labarge		
/s/ Joseph Mauriello	Director	February 27, 2012
Joseph Mauriello		
/s/ Eugene M. McQuade	Director	February 27, 2012
Eugene M. McQuade		
/s/ Clayton S. Rose	Director	February 27, 2012
Clayton S. Rose		
/s/ Sir John Vereker	Director	February 27, 2012
Sir John Vereker		