

EVEREST REINSURANCE HOLDINGS INC  
Form 10-K  
March 19, 2013

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C 20549  
FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the fiscal year ended December 31, 2012

Commission file number 1-14527  
EVEREST REINSURANCE HOLDINGS, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other  
jurisdiction  
of incorporation or  
organization)  
477 Martinsville Road

22-3263609  
(I.R.S Employer  
Identification No.)

Post Office Box 830  
Liberty Corner, New Jersey 07938-0830  
(908) 604-3000

(Address, including zip code, and telephone number, including area code, of registrant's principal executive office)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
5.40% Senior Notes Due 2014	NYSE
6.60% Long Term Notes Due 2067	NYSE
6.20% Trust Preferred Securities of Everest Re Capital Trust II guaranteed by Everest Reinsurance Holdings, Inc.	NYSE

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  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

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Yes                      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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes   X                      No

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 the 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. [   ]

Yes   X                      No

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	X	Smaller reporting company

(Do not check if smaller reporting company)

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

Yes                      No    X

The aggregate market value on June 30, 2012, the last business day of the registrant's most recently completed second quarter, of the voting stock held by non-affiliates of the registrant was zero.

At March 15, 2013, the number of shares outstanding of the registrant common shares was 1,000, all of which are owned by Everest Underwriting Group (Ireland) Limited, a wholly-owned direct subsidiary of Everest Re Group, Ltd.

The Registrant meets the conditions set forth in General Instruction I(1)(a) and (b) of Form 10-K and is therefore filing this form with the reduced disclosure format permitted by General Instruction I of Form 10-K.

EVEREST REINSURANCE HOLDINGS, INC.

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PART I

Unless otherwise indicated, all financial data in this document have been prepared using accounting principles generally accepted in the United States of America (“GAAP”). As used in this document, “Holdings” means Everest Reinsurance Holdings, Inc.; “Group” means Everest Re Group, Ltd.; “Holdings Ireland” means Everest Underwriting Group (Ireland) Limited; “Everest Re” means Everest Reinsurance Company and its subsidiaries (unless the context otherwise requires) and the “Company”, “we”, “us”, and “our” means Holdings and its subsidiaries (unless the context otherwise requires).

ITEM 1. BUSINESS

The Company.

Holdings, a Delaware corporation, is a wholly-owned subsidiary of Holdings Ireland. On December 30, 2008, Group contributed Holdings to its recently established Irish holding company, Holdings Ireland. Holdings Ireland is a direct subsidiary of Group and was established to serve as a holding company for the U.S. and Irish reinsurance and insurance subsidiaries. Group is a Bermuda holding company whose common shares are publicly traded in the U.S. on the New York Stock Exchange under the symbol “RE”. Group files an annual report on Form 10-K with the Securities and Exchange Commission (the “SEC”) with respect to its consolidated operations, including Holdings.

The Company’s principal business, conducted through its operating segments, is the underwriting of reinsurance and insurance in the U.S. and international markets. The Company had gross written premiums, in 2012, of \$3.6 billion, with approximately 71% representing reinsurance and 29% representing insurance. Stockholder’s equity at December 31, 2012 was \$3.5 billion. The Company underwrites reinsurance both through brokers and directly with ceding companies, giving it the flexibility to pursue business based on the ceding company’s preferred reinsurance purchasing method. The Company underwrites insurance principally through general agent relationships, brokers and surplus lines brokers. Holdings’ active operating subsidiaries, excluding Mt. McKinley Insurance Company (“Mt. McKinley”), which is in runoff, are each rated A+ (“Superior”) by A.M. Best Company (“A.M. Best”), a leading provider of insurer ratings that assigns financial strength ratings to insurance companies based on their ability to meet their obligations to policyholders.

Following is a summary of the Company’s operating subsidiaries:

- Everest Re, a Delaware insurance company and a direct subsidiary of Holdings, is a licensed property and casualty insurer and/or reinsurer in all states, the District of Columbia and Puerto Rico and is authorized to conduct reinsurance business in Canada, Singapore and Brazil. Everest Re underwrites property and casualty reinsurance for insurance and reinsurance companies in the U.S. and international markets. Everest Re has engaged in reinsurance transactions with Everest Reinsurance (Bermuda), Ltd. (“Bermuda Re”), Everest International Reinsurance, Ltd. (“Everest International”) and Everest Insurance Company of Canada (“Everest Canada”), which are affiliated companies, primarily driven by enterprise risk and capital management considerations under which business is ceded at market rates and terms. At December 31, 2012 Everest Re had statutory surplus of \$2.6 billion.
- Everest National Insurance Company (“Everest National”), a Delaware insurance company and a direct subsidiary of Everest Re, is licensed in 50 states and the District of Columbia and is authorized to write property and casualty insurance on an admitted basis in the jurisdictions in which it is licensed. The majority of Everest National’s business is reinsured by its parent, Everest Re.



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- Everest Indemnity Insurance Company (“Everest Indemnity”), a Delaware insurance company and a direct subsidiary of Everest Re, writes excess and surplus lines insurance business in the U.S. on a non-admitted basis. Excess and surplus lines insurance is specialty property and liability coverage that an insurer not licensed to write insurance in a particular jurisdiction is permitted to provide to insureds when the specific specialty coverage is unavailable from admitted insurers. Everest Indemnity is licensed in Delaware and is eligible to write business on a non-admitted basis in all other states, the District of Columbia and Puerto Rico. The majority of Everest Indemnity’s business is reinsured by its parent, Everest Re.
- Everest Security Insurance Company (“Everest Security”), a Georgia insurance company and a direct subsidiary of Everest Re, writes property and casualty insurance on an admitted basis in Georgia and Alabama. The majority of Everest Security’s business is reinsured by its parent, Everest Re.
- Mt. McKinley, a Delaware insurance company and a direct subsidiary of Holdings, was acquired by Holdings in September 2000 from The Prudential Insurance Company of America (“The Prudential”). In 1985, Mt. McKinley ceased writing new and renewal insurance and commenced a run-off operation to service claims arising from its previously written business. Effective September 19, 2000, Mt. McKinley and Bermuda Re entered into a loss portfolio transfer reinsurance agreement, whereby Mt. McKinley transferred, for arm’s length consideration, all of its net insurance exposures and reserves to Bermuda Re.
- Heartland Crop Insurance, Inc. (“Heartland”), a Kansas based managing general agent and a direct subsidiary of Holdings, was acquired on January 2, 2011. Heartland specializes in crop insurance, which is written mainly through Everest National.

Reinsurance Industry Overview.

Reinsurance is an arrangement in which an insurance company, the reinsurer, agrees to indemnify another insurance or reinsurance company, the ceding company, against all or a portion of the insurance risks underwritten by the ceding company under one or more insurance contracts. Reinsurance can provide a ceding company with several benefits, including a reduction in its net liability on individual risks or classes of risks, catastrophe protection from large and/or multiple losses and/or a reduction in operating leverage as measured by the ratio of net premiums and reserves to capital. Reinsurance also provides a ceding company with additional underwriting capacity by permitting it to accept larger risks and write more business than would be acceptable relative to the ceding company’s financial resources. Reinsurance does not discharge the ceding company from its liability to policyholders; rather, it reimburses the ceding company for covered losses.

There are two basic types of reinsurance arrangements: treaty and facultative. Treaty reinsurance obligates the ceding company to cede and the reinsurer to assume a specified portion of a type or category of risks insured by the ceding company. Treaty reinsurers do not separately evaluate each of the individual risks assumed under their treaties, instead, the reinsurer relies upon the pricing and underwriting decisions made by the ceding company. In facultative reinsurance, the ceding company cedes and the reinsurer assumes all or part of the risk under a single insurance contract. Facultative reinsurance is negotiated separately for each insurance contract that is reinsured. Facultative reinsurance, when purchased by ceding companies, usually is intended to cover individual risks not covered by their reinsurance treaties because of the dollar limits involved or because the risk is unusual.

Both treaty and facultative reinsurance can be written on either a pro rata basis or an excess of loss basis. Under pro rata reinsurance, the ceding company and the reinsurer share the premiums as well as the losses and expenses in an agreed proportion. Under excess of loss reinsurance, the reinsurer indemnifies the ceding company against all or a specified portion of losses and expenses in excess of a specified dollar amount, known as the ceding company’s retention or reinsurer’s attachment point, generally subject to a negotiated reinsurance contract limit.





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In pro rata reinsurance, the reinsurer generally pays the ceding company a ceding commission. The ceding commission generally is based on the ceding company's cost of acquiring the business being reinsured (commissions, premium taxes, assessments and miscellaneous administrative expense and may contain profit sharing provisions, whereby the ceding commission is adjusted based on loss experience). Premiums paid by the ceding company to a reinsurer for excess of loss reinsurance are not directly proportional to the premiums that the ceding company receives because the reinsurer does not assume a proportionate risk. There is usually no ceding commission on excess of loss reinsurance.

Reinsurers may purchase reinsurance to cover their own risk exposure. Reinsurance of a reinsurer's business is called a retrocession. Reinsurance companies cede risks under retrocessional agreements to other reinsurers, known as retrocessionaires, for reasons similar to those that cause insurers to purchase reinsurance: to reduce net liability on individual or classes of risks, protect against catastrophic losses, stabilize financial ratios and obtain additional underwriting capacity.

Reinsurance can be written through intermediaries, generally professional reinsurance brokers, or directly with ceding companies. From a ceding company's perspective, the broker and the direct distribution channels have advantages and disadvantages. A ceding company's decision to select one distribution channel over the other will be influenced by its perception of such advantages and disadvantages relative to the reinsurance coverage being placed.

### Business Strategy.

The Company's business strategy is to sustain its leadership position within targeted reinsurance and insurance markets, provide effective management throughout the property and casualty underwriting cycle and thereby achieve an attractive return for its stockholder. The Company's underwriting strategies seek to capitalize on its i) financial strength and capacity, ii) global franchise, iii) stable and experienced management team, iv) diversified product and distribution offerings, v) underwriting expertise and disciplined approach, vi) efficient and low-cost operating structure and vii) effective enterprise risk management practices.

The Company offers treaty and facultative reinsurance and admitted and non-admitted insurance. The Company's products include the full range of property and casualty reinsurance and insurance coverages, including marine, aviation, surety, errors and omissions liability ("E&O"), directors' and officers' liability ("D&O"), medical malpractice, other specialty lines, accident and health ("A&H") and workers' compensation.

The Company's underwriting strategies emphasize underwriting profitability over premium volume. Key elements of this strategy include careful risk selection, appropriate pricing through strict underwriting discipline and adjustment of the Company's business mix in response to changing market conditions. The Company focuses on reinsuring companies that effectively manage the underwriting cycle through proper analysis and pricing of underlying risks and whose underwriting guidelines and performance are compatible with its objectives.

The Company's underwriting strategies emphasize flexibility and responsiveness to changing market conditions, such as increased demand or favorable pricing trends. The Company believes that its existing strengths, including its broad underwriting expertise, U.S. and international presence, strong financial ratings and substantial capital, facilitate adjustments to its mix of business geographically, by line of business and by type of coverage, allowing it to participate in those market opportunities that provide the greatest potential for underwriting profitability. The Company's insurance operations complement these strategies by accessing business that is not available on a reinsurance basis. The Company carefully monitors its mix of business across all operations to avoid unacceptable geographic or other risk concentrations.



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## Capital Transactions.

The Company's business operations are in part dependent on its financial strength and financial strength ratings, and the market's perception of its financial strength. The Company's stockholder's equity was \$3,478.6 million and \$2,941.4 million at December 31, 2012 and 2011, respectively. The Company possesses significant financial flexibility with access to the debt markets and, through its ultimate parent, equity markets, as a result of its perceived financial strength, as evidenced by the financial strength ratings as assigned by independent rating agencies. The Company's capital position remains strong, commensurate with its financial ratings and the Company has ample liquidity to meet its financial obligations for the foreseeable future.

On October 14, 2011, Group and Holdings renewed the shelf registration statement on Form S-3ASR with the SEC, as a Well Known Seasoned Issuer. This shelf registration statement can be used by Group to register common shares, preferred shares, debt securities, warrants, share purchase contracts and share purchase units; by Holdings to register debt securities and by Everest Re Capital Trust III ("Capital Trust III") to register trust preferred securities.

On March 19, 2009, Group announced the commencement of a cash tender offer for any and all of the 6.6% fixed to floating rate long term subordinated notes. Upon expiration of the tender offer, the Company had reduced its outstanding debt by \$161.4 million.

On March 15, 2010, the \$200.0 million principal amount of 8.75% senior notes matured, and was paid off in cash.

## Financial Strength Ratings.

The following table shows the current financial strength ratings of the Company's operating subsidiaries as reported by A.M. Best, Standard & Poor's Financial Services, LLC ("Standard & Poor's") and Moody's Investors Services, Inc. ("Moody's"). These ratings are based upon factors of concern to policyholders and should not be considered an indication of the degree or lack of risk involved in a direct or indirect equity investment in an insurance or reinsurance company.

All of the below-mentioned ratings are continually monitored and revised, if necessary, by each of the rating agencies. The ratings presented in the following table were in effect as of February 28, 2013.

The Company believes that its ratings, in general, are important to its operations because they provide the Company's customers and investors with an independent assessment of the Company's underlying financial strength using a scale that provides for relative comparisons. Strong financial ratings are particularly important for reinsurance companies. Ceding companies must rely on their reinsurers to pay covered losses well into the future. As a result, a highly rated reinsurer is generally preferred.

Operating Subsidiary:	A.M. Best	Standard & Poor's	Moody's
Everest Re	A+ (Superior)	A+ (Strong)	Aa3 (Excellent)
Everest National	A+ (Superior)	A+ (Strong)	Not Rated
Everest Indemnity	A+ (Superior)	Not Rated	Not Rated
Everest Security	A+ (Superior)	Not Rated	Not Rated
Mt. McKinley	Not Rated	Not Rated	Not Rated

A.M. Best states that the “A+” (“Superior”) rating is assigned to those companies which, in its opinion, have a superior ability to meet their ongoing insurance policy and contract obligations based on A.M. Best’s comprehensive quantitative and qualitative evaluation of a company’s balance sheet strength, operating performance and business profile. Standard & Poor’s states that the “A+” rating is assigned to those insurance companies which, in its opinion, have strong financial security characteristics with respect to their ability to pay under its insurance policies and contracts in accordance with their terms. Moody’s states that insurance companies rated “Aa” offer excellent financial security. Together with the “Aaa” rated companies, “Aa” rated companies constitute what are generally known as high-grade companies, with “Aa” rated companies generally having somewhat larger long-term risks. On January 24, 2012, Moody’s affirmed the rating of Everest Re but changed the outlook on the ratings from stable to negative reflecting their opinion of

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the likely direction of the ratings over the medium term (12 to 18 months). Management will continue to work with Moody's over this time to address their concerns but it is not possible to predict the potential outcome. Management does not believe that a potential one notch downgrade would have a material adverse affect on the Company's business.

Subsidiaries other than Everest Re may not be rated by some or any rating agencies because such ratings are not considered essential by the individual subsidiary's customers or because of the limited nature of the subsidiary's operations. In particular, Mt. McKinley is not rated because it is in run-off status.

**Debt Ratings.**

The following table shows the debt ratings by A.M. Best, Standard & Poor's and Moody's of the Holdings' senior notes due October 15, 2014, long term notes due May 1, 2067 and Everest Re Capital Trust II's ("Capital Trust II") trust preferred securities due March 29, 2034, all of which are considered investment grade. Debt ratings are the rating agencies' current assessment of the credit worthiness of an obligor with respect to a specific obligation.

	A.M. Best	Standard & Poor's	Moody's
Senior Notes	a- (Strong)	A- (Strong)	A3 (Good)
Long Term Notes	bbb (Adequate)	BBB (Adequate)	Baa1 (Adequate)
Trust Preferred Securities	bbb+ (Adequate)	BBB (Adequate)	Baa1 (Adequate)

A debt rating of "a-" is assigned by A.M. Best where the issuer, in A.M. Best's opinion, has a strong ability to meet the terms of the obligation. A.M. Best assigns a debt rating in the "bbb" range where the issuer, in A.M. Best's opinion, has adequate ability to meet the terms of the obligation. Standard & Poor's assigns a debt rating in the "A" range to issuers that exhibit strong capacity and willingness to meet its financial commitments on obligations as they come due. A debt rating in the "BBB" range is assigned by Standard & Poor's where the issuers exhibit adequate protection parameters although adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation. According to Moody's, a debt rating of "A3" is assigned to issues that are considered upper-medium-grade obligations and subject to low credit risk. Obligations rated "Baa1" are subject to moderate credit risk and are considered medium-grade and as such may possess certain speculative characteristics. On January 24, 2012, Moody's affirmed the ratings of the Company's debt but changed the outlook on the ratings from stable to negative reflecting their opinion of the potential direction of the ratings over the medium term (12 to 18 months). The Company will continue to work with Moody's over this time to address their concerns but it is not possible to predict the potential outcome. The Company does not believe that a one notch downgrade would have a material adverse affect on the Company's business.

**Competition.**

The worldwide reinsurance and insurance businesses are highly competitive, as well as cyclical by product and market. As such, financial results tend to fluctuate with periods of constrained availability, high rates and strong profits followed by periods of abundant capacity, low rates and constrained profitability. Competition in the types of reinsurance and insurance business that the Company underwrites is based on many factors, including the perceived overall financial strength of the reinsurer or insurer, ratings of the reinsurer or insurer by A.M. Best and/or Standard & Poor's, underwriting expertise, the jurisdictions where the reinsurer or insurer is licensed or otherwise authorized, capacity and coverages offered, premiums charged, other terms and conditions of the reinsurance and insurance business offered, services offered, speed of claims payment and reputation and experience in lines written. Furthermore, the market impact from these competitive factors related to reinsurance and insurance is generally not consistent across lines of business, domestic and international geographical areas and distribution

channels.

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The Company competes in the U.S. and international reinsurance and insurance markets with numerous global competitors. The Company's competitors include independent reinsurance and insurance companies, subsidiaries or affiliates of established worldwide insurance companies, reinsurance departments of certain insurance companies and domestic and international underwriting operations, including underwriting syndicates at Lloyd's. Some of these competitors have greater financial resources than the Company and have established long term and continuing business relationships, which can be a significant competitive advantage. In addition, the lack of strong barriers to entry into the reinsurance business and the potential for securitization of reinsurance and insurance risks through capital markets provide additional sources of potential reinsurance and insurance capacity and competition.

Worldwide insurance and reinsurance market conditions continued to be very competitive, particularly in the casualty lines of business. Generally, there was ample insurance and reinsurance capacity relative to demand. Competition and its effect on rates, terms and conditions vary widely by market and coverage yet continued to be most prevalent in the U.S. casualty insurance and reinsurance markets.

However, during the fourth quarter of 2012, the industry sustained significant losses from Superstorm Sandy and also sustained significant losses during 2011 from Australian floods, the New Zealand earthquake, the earthquake and tsunami in Japan, storms in the U.S., and the Thailand floods. It is too early to determine the longer term impact on market conditions as a result of these events. While the 2011 events have resulted in meaningful rate increases for catastrophe coverages in some global catastrophe prone regions, particularly areas impacted by these losses, whether the magnitude of these 2012 and 2011 losses is sufficient to increase rates and improve market conditions for other lines of business remains to be seen.

Overall, the Company believes that current marketplace conditions, particularly for catastrophe coverages, provide profit opportunities for it given its strong ratings, distribution system, reputation and expertise. The Company continues to employ its strategy of targeting business that offers the greatest profit potential, while maintaining balance and diversification in its overall portfolio.

Employees.

As of February 1, 2013, the Company employed 644 persons. Management believes that employee relations are good. None of the Company's employees are subject to collective bargaining agreements, and the Company is not aware of any current efforts to implement such agreements.

Available Information.

The Company's Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports are available free of charge through the Company's internet website at <http://www.everestgroup.com> as soon as reasonably practicable after such reports are electronically filed with the SEC.

ITEM 1A. RISK FACTORS

In addition to the other information provided in this report, the following risk factors should be considered when evaluating us. If the circumstances contemplated by the individual risk factors materialize, our business, financial condition and results of operations could be materially and adversely affected and our ability to service our debt, our debt ratings and our ability to issue new debt could decline significantly.

RISKS RELATING TO OUR BUSINESS

Fluctuations in the financial markets could result in investment losses.

Prolonged and severe disruptions in the public debt and equity markets, such as occurred during 2008, could result in significant realized and unrealized losses in our investment portfolio. For the year ended December 31, 2008, we incurred \$489.2 million of realized investment losses and \$276.5 million of unrealized investment losses. Although financial markets have significantly improved since 2008, they could deteriorate in the future. Such declines in the financial markets could result in significant realized and unrealized losses on investments and could have a material adverse impact on our results of operations, equity, business and insurer financial strength and debt ratings.



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Our results could be adversely affected by catastrophic events.

We are exposed to unpredictable catastrophic events, including weather-related and other natural catastrophes, as well as acts of terrorism. Any material reduction in our operating results caused by the occurrence of one or more catastrophes could inhibit our ability to pay dividends or to meet our interest and principal payment obligations. Subsequent to April 1, 2010, we define a catastrophe as an event that causes a loss on property exposures before reinsurance of at least \$10.0 million, before corporate level reinsurance and taxes. Prior to April 1, 2010, we used a threshold of \$5.0 million. By way of illustration, during the past five calendar years, pre-tax catastrophe losses, net of contract specific reinsurance but before cessions under corporate reinsurance programs, were as follows:

Calendar year: (Dollars in millions)	Pre-tax catastrophe losses
2012	\$ 235.8
2011	798.4
2010	267.1
2009	23.9
2008	202.4

Our losses from future catastrophic events could exceed our projections.

We use projections of possible losses from future catastrophic events of varying types and magnitudes as a strategic underwriting tool. We use these loss projections to estimate our potential catastrophe losses in certain geographic areas and decide on the purchase of retrocessional coverage or other actions to limit the extent of potential losses in a given geographic area. These loss projections are approximations, reliant on a mix of quantitative and qualitative processes, and actual losses may exceed the projections by a material amount, resulting in a material adverse effect on our financial condition and results of operations.

If our loss reserves are inadequate to meet our actual losses, our net income would be reduced or we could incur a loss.

We are required to maintain reserves to cover our estimated ultimate liability of losses and loss adjustment expenses (“LAE”) for both reported and unreported claims incurred. These reserves are only estimates of what we believe the settlement and administration of claims will cost based on facts and circumstances known to us. In setting reserves for our reinsurance liabilities, we rely on claim data supplied by our ceding companies and brokers and we employ actuarial and statistical projections. The information received from our ceding companies is not always timely or accurate, which can contribute to inaccuracies in our loss projections. Because of the uncertainties that surround our estimates of loss and LAE reserves, we cannot be certain that ultimate losses and LAE payments will not exceed our estimates. If our reserves are deficient, we would be required to increase loss reserves in the period in which such deficiencies are identified which would cause a charge to our earnings and a reduction of capital. By way of illustration, during the past five calendar years, the reserve re-estimation process resulted in a decrease to our pre-tax net income in all of the years:

Calendar year: (Dollars in millions)	Effect on pre-tax net income
2012	\$ 12.3 decrease

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2011	14.8	decrease
2010	62.8	decrease
2009	70.0	decrease
2008	142.0	decrease

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The difficulty in estimating our reserves is significantly more challenging as it relates to reserving for potential asbestos and environmental (“A&E”) liabilities. At year end 2012, 5.4% of our gross reserves were comprised of A&E reserves. A&E liabilities are especially hard to estimate for many reasons, including the long delays between exposure and manifestation of any bodily injury or property damage, difficulty in identifying the source of the asbestos or environmental contamination, long reporting delays and difficulty in properly allocating liability for the asbestos or environmental damage. Legal tactics and judicial and legislative developments affecting the scope of insurers’ liability, which can be difficult to predict, also contribute to uncertainties in estimating reserves for A&E liabilities.

The failure to accurately assess underwriting risk and establish adequate premium rates could reduce our net income or result in a net loss.

Our success depends on our ability to accurately assess the risks associated with the businesses on which the risk is retained. If we fail to accurately assess the risks we retain, we may fail to establish adequate premium rates to cover our losses and LAE. This could reduce our net income and even result in a net loss.

In addition, losses may arise from events or exposures that are not anticipated when the coverage is priced. In addition to unanticipated events, we also face the unanticipated expansion of our exposures, particularly in long-tail liability lines. An example of this is the expansion over time of the scope of insurers’ legal liability within the mass tort arena, particularly for A&E exposures discussed above.

Decreases in pricing for property and casualty reinsurance and insurance could reduce our net income.

The worldwide reinsurance and insurance businesses are highly competitive, as well as cyclical by product and market. These cycles, as well as other factors that influence aggregate supply and demand for property and casualty insurance and reinsurance products, are outside of our control. The supply of (re)insurance is driven by prevailing prices and levels of capacity that may fluctuate in response to a number of factors including large catastrophic losses and investment returns being realized in the insurance industry. Demand for (re)insurance is influenced by underwriting results of insurers and insureds, including catastrophe losses, and prevailing general economic conditions. If any of these factors were to result in a decline in the demand for (re)insurance or an overall increase in (re)insurance capacity, our net income could decrease.

If rating agencies downgrade the ratings of our insurance subsidiaries, future prospects for growth and profitability could be significantly and adversely affected.

Our active insurance company subsidiaries currently hold financial strength ratings assigned by third-party rating agencies which assess and rate the claims paying ability and financial strength of insurers and reinsurers. Our active subsidiaries carry an “A+” (“Superior”) rating from A.M. Best. Everest Re and Everest National hold an “A+” (“Strong”) rating from Standard & Poor’s. Everest Re holds an “Aa3” (“Excellent”) rating from Moody’s. Financial strength ratings are used by client companies and agents and brokers that place the business as an important means of assessing the financial strength and quality of reinsurers. A downgrade or withdrawal of any of these ratings might adversely affect our ability to market our insurance products and could have a material and adverse effect on future prospects for growth and profitability.

On January 24, 2012, Moody’s affirmed the ratings of Everest Re but changed the outlook on the ratings from stable to negative reflecting their opinion of the likely directions of the ratings over the medium term (12 to 18 months). We will continue to work with Moody’s over this time to address their concerns but it is not possible to predict the potential outcome.

On March 13, 2009, Standard & Poor's downgraded its ratings of Everest Re and Everest National one level to "A+". It is possible that a further downgrade will occur in the future if we do not continue to meet the evolving criteria expected of our current rating. In that regard, several of the rating agencies are in the process of modifying their approaches to evaluating enterprise risk management and its impact on ratings. Therefore, we cannot predict the outcome of this reassessment or its potential impact upon our ratings.

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Consistent with market practice, much of our treaty reinsurance business allows the ceding company to terminate the contract or seek collateralization of our obligations in the event of a rating downgrade below a certain threshold. The termination provision would generally be triggered if a rating fell below A.M. Best Company's A- rating level, which is three levels below Everest Re's current rating of A+. To a lesser extent, Everest Re also has modest exposure to reinsurance contracts that contain provisions for obligatory funding of outstanding liabilities in the event of a rating agency downgrade. Those provisions would also generally be triggered if Everest Re's rating fell below A.M. Best's A- rating level.

The failure of our insureds, intermediaries and reinsurers to satisfy their obligations to us could reduce our income.

In accordance with industry practice, we have uncollateralized receivables from insureds, agents and brokers and/or rely on agents and brokers to process our payments. We may not be able to collect amounts due from insureds, agents and brokers, resulting in a reduction to net income.

We are subject to credit risk of reinsurers in connection with retrocessional arrangements because the transfer of risk to a reinsurer does not relieve us of our liability to the insured. In addition, reinsurers may be unwilling to pay us even though they are able to do so. The failure of one or more of our reinsurers to honor their obligations to us in a timely fashion would impact our cash flow and reduce our net income and could cause us to incur a significant loss.

If we are unable or choose not to purchase reinsurance and transfer risk to reinsurers, our net income could be reduced or we could incur a net loss in the event of unusual loss experience.

We are generally less reliant on the purchase of reinsurance than many of our competitors, in part because of our strategic emphasis on underwriting discipline and management of the cycles inherent in our business. We try to separate our risk taking process from our risk mitigation process in order to avoid developing too great a reliance on reinsurance. We generally purchase reinsurance from other third parties only when we expect a net benefit. The percentage of business that we reinsure may vary considerably from year to year, depending on our view of the relationship between cost and expected benefit for the contract period.

We have entered into affiliated whole account quota share reinsurance agreements for 2002 through 2012 and entered into a new quota share agreement for 2013 with Bermuda Re. We believe that the terms, conditions and pricing of the quota share agreements reflect arm's length market conditions. In addition, we entered into a loss portfolio transfer agreement with Bermuda Re on October 1, 2008. These affiliated reinsurance arrangements allow us to more effectively leverage our capital, expertise, distribution platform and market presence than our stand alone capital position would otherwise allow.

Percentage of ceded written premiums to gross  
written premiums

	2012	2011	2010	2009	2008
Unaffiliated	6.3%	5.0%	7.4%	6.0%	6.0%
Affiliated	46.3%	45.8%	41.1%	42.0%	36.2%

Our affiliated quota share agreements reflect general reinsurance market terms and conditions and are negotiated on an arms' length basis. As a result, there can be no assurance that these arrangements will continue beyond 2013. If the quota shares are not renewed, we may have to reduce our premium volume and we may be more exposed to reductions in net income from large losses.



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Our industry is highly competitive and we may not be able to compete successfully in the future.

Our industry is highly competitive and subject to pricing cycles that can be pronounced. We compete globally in the United States and international reinsurance and insurance markets with numerous competitors. Our competitors include independent reinsurance and insurance companies, subsidiaries or affiliates of established worldwide insurance companies, reinsurance departments of certain insurance companies and domestic and international underwriting operations, including underwriting syndicates at Lloyd's. Some of these competitors have greater financial resources than we do and have established long term and continuing business relationships throughout the industry, which can be a significant competitive advantage. In addition, the lack of strong barriers to entry into the reinsurance business and the potential for securitization of reinsurance and insurance risks through capital markets provide additional sources of potential reinsurance and insurance capacity and competition.

We are dependent on our key personnel.

Our success has been, and will continue to be, dependent on our ability to retain the services of existing key executive officers and to attract and retain additional qualified personnel in the future. The loss of the services of any key executive officer or the inability to hire and retain other highly qualified personnel in the future could adversely affect our ability to conduct business. Generally, we consider key executive officers to be those individuals who have the greatest influence in setting overall policy and controlling operations: Chairman and Chief Executive Officer, Joseph V. Taranto (age 63), President, Dominic J. Adesso (age 59) and Executive Vice President and Chief Financial Officer, Craig Howie (age 49). We currently have employment contracts with Mr. Taranto and Mr. Adesso. Mr. Taranto's contract was filed with the SEC and provides for terms of employment ending on December 31, 2013. Mr. Adesso's contract was filed with the SEC and provides for terms of employment ending December 31, 2016.

Our investment values and investment income could decline because they are exposed to interest rate, credit and market risks.

A significant portion of our investment portfolio consists of fixed income securities and smaller portions consist of equity securities and other investments. Both the fair market value of our invested assets and associated investment income fluctuate depending on general economic and market conditions. For example, the fair market value of our predominant fixed income portfolio generally increases or decreases inversely to fluctuations in interest rates. The market value of our fixed income securities could also decrease as a result of a downturn in the business cycle, that causes the credit quality of such securities to deteriorate. The net investment income that we realize from future investments in fixed income securities will generally increase or decrease with interest rates.

Interest rate fluctuations also can cause net investment income from fixed income investments that carry prepayment risk, such as mortgage-backed and other asset-backed securities, to differ from the income anticipated from those securities at the time of purchase. In addition, if issuers of individual investments are unable to meet their obligations, investment income will be reduced and realized capital losses may arise.

The majority of our fixed income securities are classified as available for sale and temporary changes in the market value of these investments are reflected as changes to our stockholder's equity. Our actively managed equity security portfolios are fair valued and any changes in fair value are reflected as net realized capital gains or losses. As a result, a decline in the value of our securities reduces our capital or could cause us to incur a loss.





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We have invested a portion of our investment portfolio in equity securities. The value of these assets fluctuates with changes in the markets. In times of economic weakness, the fair value of these assets may decline, and may negatively impact net income. We also invest in non-traditional investments which have different risk characteristics than traditional fixed income and equity securities. These alternative investments are comprised primarily of private equity limited partnerships. The changes in value and investment income/(loss) for these partnerships may be more volatile than over-the-counter securities.

The following table quantifies the portion of our investment portfolio that consists of fixed income securities, equity securities and investments that carry prepayment risk.

(Dollars in millions)	At December 31, 2012	%	of Total
Mortgage-backed securities			
Commercial	\$ 52.5	0.6	%
Agency residential	683.7	7.5	%
Non-agency residential	2.3	0.0	%
Other asset-backed	46.5	0.5	%
Total asset-backed	785.0	8.6	%
Other fixed income	4,746.4	52.3	%
Total fixed income, at market value	5,531.4	60.9	%
Fixed maturities, at fair value	41.5	0.5	%
Equity securities, at fair value	1,199.8	13.2	%
Other invested assets, at market value	420.7	4.6	%
Other invested assets, at fair value	1,068.7	11.8	%
Cash and short-term investments	813.3	9.0	%
Total investments and cash	\$ 9,075.5	100.0	%

(Some amounts may not reconcile due to rounding.)

We may experience foreign currency exchange losses that reduce our net income and capital levels.

Through our international operations, we conduct business in a variety of foreign (non-U.S.) currencies, principally the Canadian dollar and the Singapore dollar. Assets, liabilities, revenues and expenses denominated in foreign currencies are exposed to changes in currency exchange rates. Our functional currency is the U.S. dollar, and exchange rate fluctuations relative to the U.S. dollar may materially impact our results and financial position. In 2012, we wrote approximately 25.1% of our coverages in non-U.S. currencies; as of December 31, 2012, we maintained approximately 16.4% of our investment portfolio in investments denominated in non-U.S. currencies. During 2012, 2011 and 2010, the impact on our quarterly pre-tax net income from exchange rate fluctuations ranged from a loss of \$12.2 million to a gain of \$24.1 million.

We are subject to cybersecurity risks that could negatively impact our business operations.

We are dependent upon our information technology platform, including our processing systems, data and electronic transmissions in our business operations. Security breaches could expose us to the loss or misuse of our information, litigation and potential liability. In addition, cyber incidents that impact the availability, reliability, speed, accuracy or

other proper functioning of these systems could have a significant negative impact on our operations and possibly our results. An incident could also result in a violation of applicable privacy and other laws, damage our reputation, cause a loss of customers or give rise to monetary fines and other penalties, which could be significant. Management is not aware of a cybersecurity incident that has had a material impact on our operations.

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RISKS RELATING TO REGULATION

Insurance laws and regulations restrict our ability to operate and any failure to comply with those laws and regulations could have a material adverse effect on our business.

We are subject to extensive and increasing regulation under U.S., state and foreign insurance laws. These laws limit the amount of dividends that can be paid to us by our operating subsidiaries, impose restrictions on the amount and type of investments that we can hold, prescribe solvency, accounting and internal control standards that must be met and maintained and require us to maintain reserves. These laws also require disclosure of material inter-affiliate transactions and require prior approval of “extraordinary” transactions. Such “extraordinary” transactions include declaring dividends from operating subsidiaries that exceed statutory thresholds. These laws also generally require approval of changes of control of insurance companies. The application of these laws could affect our liquidity and ability to pay dividends, interest and other payments on securities, as applicable, and could restrict our ability to expand our business operations through acquisitions of new insurance subsidiaries. We may not have or maintain all required licenses and approvals or fully comply with the wide variety of applicable laws and regulations or the relevant authority’s interpretation of the laws and regulations. If we do not have the requisite licenses and approvals or do not comply with applicable regulatory requirements, the insurance regulatory authorities could preclude or temporarily suspend us from carrying on some or all of our activities or monetarily penalize us. These types of actions could have a material adverse effect on our business. To date, no material fine, penalty or restriction has been imposed on us for failure to comply with any insurance law or regulation.

As a result of the recent dislocation of the financial markets, Congress and the Presidential administration in the United States, are contemplating changes in the way the financial services industry is regulated. It is possible that insurance regulation will be drawn into this process, and that federal regulatory initiatives in the insurance industry could emerge. In addition, regulatory bodies in Europe are developing a new capital adequacy directive for insurers and reinsurers. The future impact of such initiatives, if any, on our operation, net income (loss) or financial condition cannot be determined at this time.

RISK RELATING TO OUR SECURITIES

Because of our holding company structure, our ability to pay dividends, interest and principal is dependent on our receipt of dividends, loan payments and other funds from our subsidiaries.

We are a holding company, whose most significant asset consists of the stock of our operating subsidiaries. As a result, our ability to pay dividends, interest or other payments on our securities in the future will depend on the earnings and cash flows of the operating subsidiaries and the ability of the subsidiaries to pay dividends or to advance or repay funds to us. This ability is subject to general economic, financial, competitive, regulatory and other factors beyond our control. Payment of dividends and advances and repayments from some of the operating subsidiaries are regulated by U.S., state and foreign insurance laws and regulatory restrictions, including minimum solvency and liquidity thresholds. Accordingly, the operating subsidiaries may not be able to pay dividends or advance or repay funds to us in the future, which could prevent us from paying dividends, interest or other payments on our securities.

ITEM  
1B. UNRESOLVED STAFF COMMENTS

None.

ITEM  
2. PROPERTIES

Everest Re's corporate offices are located in approximately 230,500 square feet of leased office space in Liberty Corner, New Jersey. The Company's other fourteen locations occupy a total of approximately 129,435 square feet, all of which are leased. Management believes that the above described office space is adequate for its current and anticipated needs.

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ITEM  
3. LEGAL PROCEEDINGS

In the ordinary course of business, the Company is involved in lawsuits, arbitrations and other formal and informal dispute resolution procedures, the outcomes of which will determine the Company's rights and obligations under insurance and reinsurance agreements. In some disputes, the Company seeks to enforce its rights under an agreement or to collect funds owing to it. In other matters, the Company is resisting attempts by others to collect funds or enforce alleged rights. These disputes arise from time to time and are ultimately resolved through both informal and formal means, including negotiated resolution, arbitration and litigation. In all such matters, the Company believes that its positions are legally and commercially reasonable. The Company considers the statuses of these proceedings when determining its reserves for unpaid loss and loss adjustment expenses.

Aside from litigation and arbitrations related to these insurance and reinsurance agreements, the Company is not a party to any other material litigation or arbitration.

ITEM  
4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Market Information and Holder of Common Stock.

As of December 31, 2012, all of the Company's common stock was owned by Holdings Ireland and was not publicly traded.

Dividend History and Restrictions.

The Company did not pay any dividends in 2012, 2011 and 2010. The declaration and payment of future dividends, if any, 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 and growth objectives, capital and surplus requirements of its operating subsidiaries, regulatory restrictions, rating agency considerations and other factors. As an insurance holding company, the Company is dependent on dividends and other permitted payments from its subsidiaries to pay cash dividends to its stockholder. The payment of dividends to Holdings by Everest Re is subject to limitations imposed by Delaware law. Generally, Everest Re may only pay dividends out of its statutory earned surplus, which was \$1.7 billion at December 31, 2012, and only after it has given 10 days prior notice to the Delaware Insurance Commissioner. During this 10-day period, the Commissioner may, by order, limit or disallow the payment of ordinary dividends if the Commissioner finds the insurer to be presently or potentially in financial distress. Further, the maximum amount of dividends that may be paid without the prior approval of the Delaware Insurance Commissioner in any twelve month period is the greater of (1) 10% of an insurer's statutory surplus as of the end of the prior calendar year or (2) the insurer's statutory net income, not including realized capital gains, for the prior calendar year. The maximum amount that is available for the payment of dividends by Everest Re in 2013 without prior regulatory approval is \$359.0 million.

Recent Sales of Unregistered Securities.

None.

ITEM  
6. SELECTED FINANCIAL DATA

Information for Item 6 is not required pursuant to General Instruction I(2) of Form 10-K.

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

The following is a discussion and analysis of our results of operations and financial condition. It should be read in conjunction with the Consolidated Financial Statements and accompanying notes thereto presented under ITEM 8, "Financial Statements and Supplementary Data".

Industry Conditions.

The worldwide reinsurance and insurance businesses are highly competitive, as well as cyclical by product and market. As such, financial results tend to fluctuate with periods of constrained availability, high rates and strong profits followed by periods of abundant capacity, low rates and constrained profitability. Competition in the types of reinsurance and insurance business that we underwrite is based on many factors, including the perceived overall financial strength of the reinsurer or insurer, ratings of the reinsurer or insurer by A.M. Best and/or Standard & Poor's, underwriting expertise, the jurisdictions where the reinsurer or insurer is licensed or otherwise authorized, capacity and coverages offered, premiums charged, other terms and conditions of the reinsurance and insurance business offered, services offered, speed of claims payment and reputation and experience in lines written. Furthermore, the market impact from these competitive factors related to reinsurance and insurance is generally not consistent across lines of business, domestic and international geographical areas and distribution channels.

We compete in the U.S. and international reinsurance and insurance markets with numerous global competitors. Our competitors include independent reinsurance and insurance companies, subsidiaries or affiliates of established worldwide insurance companies, reinsurance departments of certain insurance companies and domestic and international underwriting operations, including underwriting syndicates at Lloyd's. Some of these competitors have greater financial resources than we do and have established long term and continuing business relationships, which can be a significant competitive advantage. In addition, the lack of strong barriers to entry into the reinsurance business and the potential for securitization of reinsurance and insurance risks through capital markets provide additional sources of potential reinsurance and insurance capacity and competition.

Worldwide insurance and reinsurance market conditions continued to be very competitive, particularly in the casualty lines of business. Generally, there was ample insurance and reinsurance capacity relative to demand. Competition and its effect on rates, terms and conditions vary widely by market and coverage yet continued to be most prevalent in the U.S. casualty insurance and reinsurance markets.

However, during the fourth quarter of 2012, the industry sustained significant losses from Superstorm Sandy and also sustained significant losses during 2011 from Australian floods, the New Zealand earthquake, the earthquake and tsunami in Japan, storms in the U.S., and the Thailand floods. It is too early to determine the longer term impact on market conditions as a result of these events. While the 2011 events have resulted in meaningful rate increases for catastrophe coverages in some global catastrophe prone regions, particularly areas impacted by these losses, whether the magnitude of these 2012 and 2011 losses is sufficient to increase rates and improve market conditions for other lines of business remains to be seen.

Overall, we believe that current marketplace conditions, particularly for catastrophe coverages, provide profit opportunities for us given our strong ratings, distribution system, reputation and expertise. We continue to employ our strategy of targeting business that offers the greatest profit potential, while maintaining balance and diversification in our overall portfolio.





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## Financial Summary.

We monitor and evaluate our overall performance based upon financial results. The following table displays a summary of the consolidated net income (loss), ratios and stockholder's equity for the periods indicated:

(Dollars in millions)	Years Ended December 31,			Percentage Increase/(Decrease)			
	2012	2011	2010	2012/2011		2011/2010	
Gross written premiums	\$3,569.4	\$3,558.5	\$3,467.8	0.3	%	2.6	%
Net written premiums	1,691.6	1,754.0	1,788.7	-3.6	%	-1.9	%
<b>REVENUES:</b>							
Premiums earned	\$1,773.9	\$1,793.9	\$1,813.8	-1.1	%	-1.1	%
Net investment income	306.1	312.9	350.3	-2.2	%	-10.7	%
Net realized capital gains (losses)	391.7	(41.1 )	65.3		NM	-163.0	%
Other income (expense)	12.1	(11.7 )	12.1	-203.3	%	-197.3	%
Total revenues	2,483.9	2,053.9	2,241.5	20.9	%	-8.4	%
<b>CLAIMS AND EXPENSES:</b>							
Incurred losses and loss adjustment expenses	1,249.7	1,877.6	1,477.5	-33.4	%	27.1	%
Commission, brokerage, taxes and fees	310.7	338.7	335.1	-8.3	%	1.1	%
Other underwriting expenses	170.6	154.3	139.8	10.5	%	10.4	%
Corporate expense	8.8	6.1	5.9	44.3	%	3.5	%
Interest, fee and bond issue cost amortization expense	50.7	50.8	54.6	0.0	%	-6.9	%
Total claims and expenses	1,790.6	2,427.4	2,012.8	-26.2	%	20.6	%
INCOME (LOSS) BEFORE TAXES	693.3	(373.5 )	228.8		NM		NM
Income tax expense (benefit)	173.0	(170.7 )	(36.6 )	-201.4	%		NM
NET INCOME (LOSS)	\$520.3	\$(202.8 )	\$265.4		NM	-176.4	%
<b>RATIOS:</b>							
						Point Change	
Loss ratio	70.5	% 104.7	% 81.5	% (34.2	)	23.2	
Commission and brokerage ratio	17.5	% 18.9	% 18.5	% (1.4	)	0.4	
Other underwriting expense ratio	9.6	% 8.6	% 7.6	% 1.0		1.0	
Combined ratio	97.6	% 132.2	% 107.6	% (34.6	)	24.6	
<b>Balance sheet data:</b>							
		At December 31,			Percentage Increase/		
(Dollars in millions)	2012	2011	2010	2012/2011		2011/2010	
Total investments and cash	\$9,075.5	\$8,396.3	\$8,293.9	8.1	%	1.2	%
Total assets	15,088.0	14,349.2	13,845.7	5.1	%	3.7	%
Loss and loss adjustment expense reserves	8,143.1	8,290.6	7,652.3	-1.8	%	8.3	%
Total debt	818.2	818.1	868.1	0.0	%	-5.8	%

Total liabilities	11,609.3	11,407.8	10,717.9	1.8	%	6.6	%
Stockholder's equity	3,478.6	2,941.4	3,127.7	18.3	%	-6.0	%

(NM, not meaningful)

(Some amounts may not reconcile due to rounding)

#### Revenues.

Premiums. Gross written premiums increased by 0.3% to \$3,569.4 million in 2012 compared to \$3,558.5 million in 2011, reflecting an \$80.1 million increase in our insurance business, partially offset by a \$69.2 million decrease in our reinsurance business. The increase in insurance premiums was primarily due to the growth in crop and primary A&H medical stop loss insurance, partially offset by the termination and runoff of several large casualty programs. The decreases in reinsurance premiums was primarily due to the non-renewal of a large Florida quota share reinsurance contract and a \$27.7 million decline due to movement in foreign exchange rates, partially offset by increases in new business and rate increases on renewals, particularly for catastrophe exposed contracts. Net written premiums decreased by 3.6% to \$1,691.6 million in 2012 compared to \$1,754.0 million in 2011. The variance between the changes in gross and net written premiums was primarily attributable to the growth in the crop business, for which the Company uses a higher level of reinsurance. Premiums earned decreased by 1.1% to \$1,773.9 million in 2012 compared to

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\$1,793.9 million in 2011. The fluctuations in premiums earned in comparison to net written premiums were primarily attributable to changes in the mix of business, particularly crop insurance which has a different premiums earning pattern.

Gross written premiums increased by 2.6% to \$3,558.5 million in 2011 compared to \$3,467.8 million in 2010, reflecting a \$103.7 million increase in our insurance business, partially offset by a \$12.9 million decrease in our reinsurance business. The year over year increase in insurance premiums was primarily due to the acquisition of Heartland, which provided \$169.6 million of new crop insurance business, our recent initiative in primary medical stop loss insurance, which added \$54.0 million of premium and improved premium rates on our California workers' compensation business, partially offset by our reduced participation on a large casualty program. The decrease in reinsurance premiums was due to the continued reduction in U.S. casualty business, the loss of several large crop reinsurance contracts, as well as the planned reduction of catastrophe exposed business in certain territories, partially offset by higher reinstatement premiums, \$24.5 million resulting from catastrophe losses and favorable foreign exchange impact, year over year, of \$33.4 million. Net written premiums decreased by 1.9% to \$1,754.0 million in 2011 compared to \$1,788.7 million in 2010. The fluctuations in net written premiums relative to the change in gross written premiums were due to a combination of a higher percentage of premiums ceded under an affiliated quota share agreement and a lower level of ceded reinsurance in the Insurance segment due to the planned reduction in one casualty program. Premiums earned decreased 1.1% to \$1,793.9 million in 2011 compared to \$1,813.8 million in 2010. The change in net premiums earned is relatively consistent with the decline in net written premiums.

Net Investment Income. Net investment income decreased by 2.2% to \$306.1 million in 2012 compared with net investment income of \$312.9 million in 2011. Net pre-tax investment income, as a percentage of average invested assets was 3.7% in 2012 compared to 3.9% in 2011. The decline in income and yield was primarily the result of lower reinvestment rates for the fixed income portfolio, partially offset by additional dividend income from equity investments.

Net investment income decreased 10.7% to \$312.9 million in 2011 compared with net investment income of \$350.3 million in 2010, primarily due to a \$58.2 million decline in income from our fixed maturities, reflective of reducing our municipal bond exposures and declining reinvestment rates. These decreases were partially offset by an increase of \$19.5 million in income from equities due to our expanded public equity portfolio and emerging market debt mutual funds. Net pre-tax investment income, as a percentage of average invested assets, was 3.9% in 2011 compared to 4.4% in 2010. The variance in this yield was primarily the result of fluctuations in our limited partnership income.

Net Realized Capital Gains (Losses). Net realized capital gains were \$391.7 million, net realized capital losses were \$41.1 million and net realized capital gains were \$65.3 million in 2012, 2011 and 2010, respectively. Of the \$391.7 million, there were \$364.5 million of gains from fair value re-measurements and \$33.9 million of net realized capital gains from sales on our fixed maturity and equity securities, partially offset by \$6.6 million of other-than-temporary impairments on our available for sale fixed maturity securities. The net realized capital losses of \$41.1 million in 2011 were the result of \$16.7 million of losses from fair value re-measurements, \$14.5 million of other-than-temporary impairments on our available for sale fixed maturity securities and \$9.9 million of net realized capital losses from sales on our fixed maturity and equity securities. The net realized capital gains of \$65.3 million in 2010 were the result of \$93.8 million of gains of fair value re-measurements, partially offset by \$26.4 million of net realized capital losses from sales on our fixed maturity and equity securities and \$2.1 million of other-than-temporary impairments.

Other Income (Expense). We recorded other income of \$12.1 million, other expense of \$11.7 million and other income of \$12.1 million in 2012, 2011 and 2010, respectively. The changes were primarily due to fluctuations in currency exchange rates for the corresponding periods and fluctuations in the amortization of deferred gains on retroactive reinsurance agreements with affiliates.



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Claims and Expenses.

Incurred Losses and Loss Adjustment Expenses. The following table presents our incurred losses and loss adjustment expenses (“LAE”) for the periods indicated.

Current	Ratio %/	Years Ended December 31, Prior
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