

2016 ANNUAL REPORT

Built to last

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The test of time



In an industry experiencing continued consolidation and ever-changing market conditions, what remains certain in the midst of uncertainty?

OdysseyRe

With a history dating back more than a century and the supportive ownership of Fairfax for the last 20 years, we have built a business that is designed to stand the test of time.

The continuity of our team and the consistency of our business approach, which emphasizes a patient, long-term view, provide a wellspring of enduring strength and stability.

You can count on us to be here tomorrow.

OdysseyRe. Built to Last.

Letter from the CEO

Dear Friends, Business Partners and Colleagues,

OdysseyRe celebrated 20 years as a Fairfax Company in style by delivering exceptional underwriting results for the fifth consecutive year. Since 2012 our combined ratio has averaged 86% and, over the last 5 years, we have generated \$1.6 billion in underwriting profits. Getting older never felt so good!

For the full year 2016, OdysseyRe recorded gross premiums written of \$2.4 billion, a combined ratio of 88.9% and net underwriting profits of \$230 million. Our solid performance was broad-based, with every one of our five Divisions and 23 of our 33 business units recording underwriting profits. Continued favorable prior year loss emergence across all of our business segments drove our underwriting earnings as margins on current business continue to be eroded by prolonged soft market conditions.

As a Fairfax Company, we have built a business that is designed to stand the test of time.

During 2016 we expanded our product offerings and made additional investments in talent and technology. In our reinsurance operations, we successfully transitioned our underwriting leadership in Latin America and we generated growth in a number of areas around the world including motor, A&H and crop. Hudson, our U.S. specialty insurance operation, continued its expansion efforts by adding new products and making strategic hires in crop, liability, professional liability, commercial auto and surety. Newline, our London-based insurance operation, is working on a number of exciting new initiatives to expand our product and territorial reach outside the U.S., the latest example being the establishment of a branch office in Cologne to increase our presence in Germany. For more information about our operations, please see our Operations Overview on page 8. Regional narratives for our reinsurance and insurance businesses begin on page 10.

Built to Last

As a Fairfax Company, we have built a business that is designed to stand the test of time. The foundation of our Company is rock solid and the structure of our organization only gets stronger with each passing year. Diversification, discipline and quality service remain at the heart of our business philosophy. These central tenets, tirelessly embraced by our workforce, have provided strength and stability to our clients and business partners throughout our history and will continue to do so long into the future.

The loyalty and dedication of our staff has also been vital to the strength and stability of our Company. The senior leadership of OdysseyRe... profit center heads, key underwriters and senior operational staff... have worked together for a very long time. The continuity of our team, the preservation of our culture and the consistency of our business approach have been, and will remain, important parts of our value proposition to clients.



Building a durable and successful (re)insurance company requires patience not only in underwriting, but in investing as well. In the years since the 2008 global financial crisis, we have been extremely cautious in our investment posture, sacrificing short-term yield and portfolio growth to protect against the risk of another economic downturn and deflation. While global deflationary pressures have diminished, rising interest rates and strong equity markets, especially after the U.S. presidential election, have taken a toll on our investment performance. As a result, net income for the year declined to \$161 million compared to \$299 million the previous year. We finished 2016 with \$10.2 billion of assets and \$3.8 billion of shareholders' equity, which is down by 3% from the prior year as shareholder dividends modestly exceeded net income.

These are challenging times for any underwriting organization. Rates in many sectors are severely depressed. Rising commission levels, widening coverage and lax underwriting have made the market environment even more toxic. Unfortunately, we have seen this race to the bottom before and it never ends well. Andy Barnard, President of Fairfax's worldwide (re)insurance operations and OdysseyRe's former CEO, offered this incisive perspective on the market two decades ago:

"The environment today is awash in capital and, with few exceptions, flush with reported profits. Traditional barriers and definitions are eroding, and the closed world of reinsurance is being encroached upon from all directions. The pressures to pursue unhealthy business will increase, and the temptations to underprice exposures will mount. We will not compromise our future for the short term, but will remain focused on underwriting profitability and building long-term strength and value for our clients."

– Andrew Barnard, President & CEO, OdysseyRe's 1997 Annual Report

Andy's words echo today. The market in the late 90s was eerily similar to what we have been experiencing the last few years. Fortunately the values and principles that carried us then continue to serve us well now.

Letter from the CEO (continued)

As we look forward, assuming the market remains soft in the near term, growth opportunities will be harder to come by. In standard property and casualty lines, we will be cautious about deploying more capital and resources until we see a fundamental correction in pricing and terms. In specialty lines... crop, motor, A&H, surety, credit, niche casualty, and affinity products... where underwriting results are less volatile and pricing conditions vary locally, we see potential for disciplined growth. With an extensive network of 33 profit centers operating from 35 offices in 13 countries around the world, we have the distribution and the capabilities to make the most of what this market has to offer.

Finally, the spirit and culture of giving in our Company is very strong. Each year we donate a portion of our profits to charities that operate in the communities where our employees live and work. Based on our 2016 results, we have earmarked an additional \$1.6 million for the OdysseyRe Foundation and its business affiliates. 2017 marks the Foundation's 10th anniversary. Since it was formed in 2007, we have pledged more than \$37 million and donated to more than 300 charities globally.

In closing, on behalf of everyone at OdysseyRe, I would like to express my gratitude to our valued clients and business partners. We would not be here today without your loyalty and support. Thank you for your business and for the trust you place in us.

To Fairfax, Prem Watsa and Andy Barnard, thank you for your leadership, guidance and unwavering support. Your commitment to us, and by extension to our clients and business partners, has been vital in building our Company's enduring strength and stability.

To my 958 colleagues around the world, congratulations on another excellent year. Thank you for your hard work and loyalty, which are essential to our long-term growth and success. When we work collaboratively as a team, we can accomplish anything. Our future is bright and I look forward to continuing our journey for many years to come.



Brian D. Young
President & Chief Executive Officer



our mission

We are an underwriting company that aspires to be a world-class reinsurer and specialty insurer, providing excellent security and high-quality service to our clients.

We seek to maintain a global business focus that emphasizes patient, profitable growth and ultimately supports Fairfax Financial Holdings' goal to achieve a 15% annual return over the long term.

We aim to meet this financial objective by:

- Maximizing underwriting profitability and growing invested assets
- Responding to clients' needs with local resources
- Delivering exceptional service to clients and colleagues alike
- Expanding our global reach through product and territorial diversification
- Possessing superior underwriting, claims and actuarial expertise
- Adapting to changing market conditions while maintaining a consistent, disciplined underwriting approach
- Investing in our employees and providing opportunities for growth within the organization to preserve our culture for the long term
- Embracing Fairfax Financial Holdings' values and guiding principles

We recognize that our prosperity and good fortune are dependent on our underwriting prowess and our clients' success; and when we succeed, those in the communities in which our employees live and work will benefit too.

At a glance

(U.S. \$ in millions)

GROSS PREMIUMS WRITTEN:

\$2,380.7

COMBINED RATIO:

88.9%

NET INCOME:

\$160.9

SHAREHOLDERS' EQUITY:

\$3,833.2

STATUTORY SURPLUS:

\$3,193.9

Odyssey Re Holdings Corp. and its subsidiaries, collectively referred to as OdysseyRe, is one of the world's leading providers of reinsurance and specialty insurance, with total assets of \$10.2 billion and \$3.8 billion in shareholders' equity as of December 31, 2016.

Reinsurance is primarily underwritten through Odyssey Reinsurance Company. Specialty insurance is underwritten through Hudson Insurance Company, Hudson Specialty Insurance Company, Hudson Excess Insurance Company, Newline Insurance Company Limited and Newline Syndicate 1218 at Lloyd's.

Odyssey Re Holdings Corp. is wholly-owned by Fairfax Financial Holdings Limited, a financial services holding company with total assets of \$43.4 billion and \$11.8 billion in shareholders' equity. Fairfax is traded on the Toronto Stock Exchange under the symbol FFH.

OdysseyRe is rated "A" (Excellent) by A.M. Best Company and "A-" (Strong) by Standard & Poor's.

A

(EXCELLENT)
A.M. BEST

A-

(STRONG)
STANDARD
& POOR'S



Financial highlights

ODYSSEY RE HOLDINGS CORP.

(U.S. \$ in millions)

	2016	2015	2014
Gross premiums written	\$ 2,380.7	\$ 2,404.0	\$ 2,739.5
Net premiums written	2,100.2	2,095.0	2,393.8
Net premiums earned	2,074.1	2,204.1	2,356.6
Net investment income	215.1	217.2	216.9
Operating income before income taxes ^a	367.2	535.5	543.1
Net realized investment (losses) gains	(201.9)	(116.5)	357.1
Income before income taxes	165.3	419.0	900.2
Net income	160.9	299.3	590.7
Total assets	10,182.5	10,396.4	11,021.6
Shareholders' equity	3,833.2	3,958.2	3,983.2
Underwriting income	229.5	331.9	357.4
Combined ratio	88.9%	84.9%	84.8%

^a Represents income before income taxes excluding net realized investment gains and losses.

GROSS PREMIUMS WRITTEN BY DIVISION

(U.S. \$ in millions)

	2016	2015	2014
North America	\$ 654.6	\$ 624.2	\$ 769.1
Latin America	104.8	145.3	176.4
EuroAsia	460.2	464.3	538.2
London Market	244.3	262.0	272.1
U.S. Insurance	916.8	908.2	983.7
Total gross premiums written	\$ 2,380.7	\$ 2,404.0	\$ 2,739.5

operations overview

2016 GROSS PREMIUMS WRITTEN
\$2.4 BILLION

OdysseyRe is a globally diversified underwriter of property and casualty reinsurance and specialty insurance that operates through five Divisions: North America, Latin America, EuroAsia, London Market and U.S. Insurance.

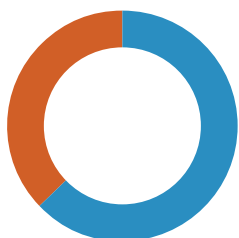


- NORTH AMERICA 27.5%
- LATIN AMERICA 4.4%
- EUROASIA 19.3%
- LONDON MARKET 10.3%
- U.S. INSURANCE 38.5%

“WRITING BUSINESS IN MORE THAN 100 TERRITORIES THROUGH A NETWORK OF 35 OFFICES LOCATED IN 13 COUNTRIES”

DIVERSIFICATION

Diversification is a critical focus of our business strategy as it provides portfolio stability and allows us to rapidly respond to business opportunities as they emerge around the world. We have 33 discrete business units organized along different product, territorial and distribution lines, with 18 of these focused on reinsurance and 15 dedicated to insurance markets.



- U.S. 62.9%
- NON-U.S. 37.1%

PROPERTY

Property accounted for 33% of gross premiums written compared to 35% in 2015. Catastrophe business represents 38% of our book and has been a major contributor to underwriting profitability during the last five years. Our property portfolio is heavily weighted to reinsurance as the margins are more attractive and we can adapt our portfolio profile more quickly in response to prevailing market conditions. Benign loss activity in recent years and excess capital have led to significant weakening in rates and broadening of coverage, making this sector less appealing today. In the current environment, we need to be more judicious in how we deploy our cat capacity.

CASUALTY

Casualty represented 36% of our global premiums compared to 35% of gross premiums written in 2015. Our casualty insurance business, which currently represents 66% of our global casualty portfolio, is a very diverse and stable book of business. We have been placing more emphasis on insurance as it gives us greater control of pricing and risk selection in today's challenging environment. While the casualty reinsurance market is very difficult and continues to consolidate, we are fortunate to have a core base of quality, long-term clients. We remain attuned to new opportunities, particularly in specialty lines, and are an attractive partner for willing buyers due to our expertise and lead market capabilities.



- PROPERTY 33.1%
- CASUALTY 35.6%
- SPECIALTY 31.3%

SPECIALTY

Specialty business, including crop, surety, credit, marine, aerospace, motor and accident & health, represented 31% of gross premiums written compared to 30% in 2015. This segment has been a growth area for us in recent years and we expect that to continue. The pricing cycles in specialty lines tend to be more localized and variable in terms of timing and thus bring additional geographic and product line diversification to our portfolio. These lines are less capital-intensive, making further expansion attractive, especially in the face of weakening margins in some of the traditional property and casualty lines.



● REINSURANCE 54.4%
● INSURANCE 45.6%

REINSURANCE

Underwritten primarily through our flagship company, Odyssey Reinsurance Company, we write a global reinsurance portfolio of \$1.3 billion through a branch and representative office network of 14 offices in 10 countries. Reinsurance results were excellent producing a global combined ratio of 85.5% compared to 81.5% in 2015.

INSURANCE

Specialty insurance is underwritten in the U.S. through Hudson Insurance Group and outside the U.S. through Newline Group. Global gross premiums written generated by our insurance operations were \$1.1 billion, and the net combined ratio was 93.7%, compared to 90.2% in 2015. We expect our insurance portfolio to drive growth and be a major contributor to our overall profitability for the foreseeable future.



Combined ratio

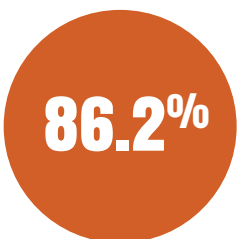
2016 UNDERWRITING RESULTS

OdysseyRe reported a net combined ratio of 88.9% for 2016. All five operating Divisions recorded underwriting profits for the year, as did both insurance and reinsurance activities. During the last five years, we have maintained a combined ratio below 90% and have generated \$1.6 billion in underwriting profits. The underwriting result is largely driven by favorable loss emergence from prior years. Loss reserves developed favorably for the ninth consecutive year.

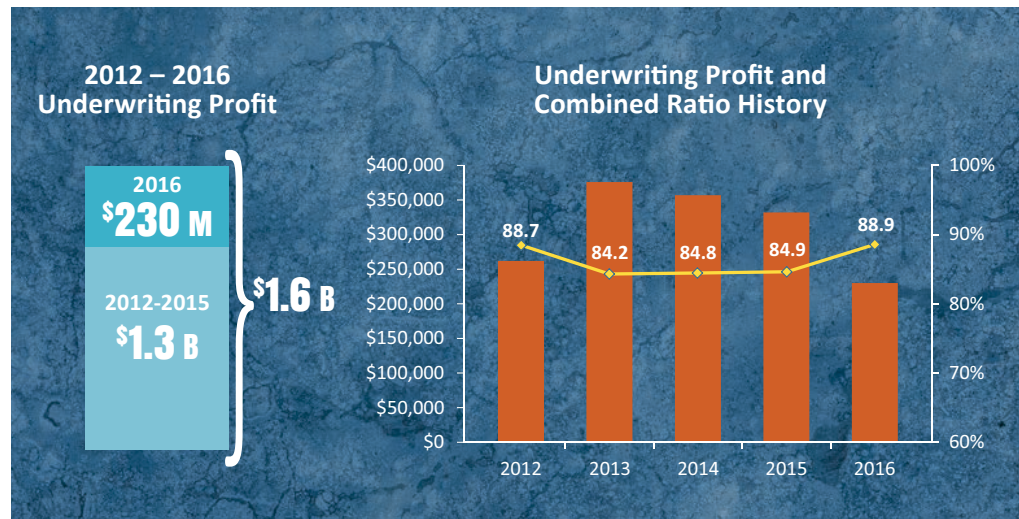
Reserve releases in 2016 were \$265 million, reducing the combined ratio by 12.8 points, compared to 10.5 points the previous year. Favorable development was recorded in all operating Divisions. Nearly 62% of the releases in 2016 were due to decreases in non-property cat loss reserves, compared to 72% in 2015. Property cat losses for 2016 were \$13 million greater than expectations and impacted the combined ratio by 0.6 points, compared to 2015 when property cat losses were \$119 million less than expectations, benefitting the combined ratio by 5.4 points.



Underwriting profits



Five-year average combined ratio



Reinsurance

PRODUCT OFFERING

TREATY

PROPERTY
(ASSUMED & RETRO)

CASUALTY

SURETY & TRADE CREDIT

MARINE & AVIATION

MOTOR/AUTO

ACCIDENT & HEALTH

AGRICULTURE

TERRORISM

CYBER LIABILITY

FACULTATIVE

CASUALTY
(U.S. AND LATIN AMERICA
ONLY)

PROPERTY
(LATIN AMERICA ONLY)

TERRORISM

ENERGY

Reinsurance is primarily underwritten through Odyssey Reinsurance Company. Our operations include a global network of 14 branch and representative offices across five regions:

- North America
- Latin America
- Europe, Middle East and Africa (EMEA)
- AsiaPacific
- London

Each region is comprised of talented, dedicated teams of underwriters, actuaries, auditors, claims professionals and catastrophe modelers. We pride ourselves on our consistent, long-term underwriting approach, well-defined risk appetite and commitment to providing quality service. We strive to be not just another balance sheet commodity, but a credible source of guidance and market leadership.

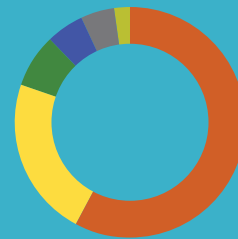
During 2016 we continued to make investments in talent to deepen our bench strength and expand our product offerings. Promoting from within is also very important to us as we value our culture and want to preserve it. The narratives that follow provide an overview of operational highlights and an in-depth view of our business in each region.

2016 GROSS PREMIUMS WRITTEN

\$1.3
BILLION

2016 COMBINED RATIO

85.5%



● NORTH AMERICA	50.6%
● LATIN AMERICA	8.1%
● EMEA	24.0%
● ASIAPACIFIC	11.5%
● LONDON	5.8%

● PROPERTY	58.0%
● CASUALTY	22.3%
● MOTOR/AUTO	7.6%
● MARINE & AVIATION	5.2%
● SURETY & TRADE CREDIT	4.9%
● AGRICULTURE	2.0%



OFFICE LOCATIONS

STAMFORD

300 First Stamford Place
Stamford, CT 06902
USA
Tel. +1 203 977 8000

BEIJING

Tel. +86 10 6618 2171

CHICAGO

Tel. +1 312 596 0226

LONDON

Tel. +44 020 7090 1800

MEXICO CITY

Tel. +52 55 5662 8660

MIAMI

Tel. +1 305 722 8401

MONTREAL

Tel. +1 514 488 6652

NEW YORK

Tel. +1 212 978 2700

PARIS

Tel. +33 1 49 26 1000

SÃO PAULO

Tel. +55 11 3512 6923

SINGAPORE

Tel. +65 6438 3806

STOCKHOLM

Tel. +46 8 598 115 00

TOKYO

Tel. +81 3 3261 2570

TORONTO

Tel. +1 416 862 0162

We pride ourselves on our consistent, long-term underwriting approach, well-defined risk appetite and commitment to providing quality service.

Reinsurance

NORTH AMERICA



Brian D. Quinn
Chief Executive Officer

OdysseyRe's North America team offers treaty and facultative reinsurance to a wide range of clients in the United States and Canada. Our treaty facilities are based in Stamford, with additional offices in Toronto and Montreal. Our casualty facultative underwriters operate from our offices in New York and Chicago. Product lines include property, casualty, surety, marine, aviation, agriculture and accident & health.

Highlights in 2016 include the appointment of Michael Fleming as the new head of our surety unit. We also added staff to support our growing A&H unit, which successfully completed its first full year of operation.

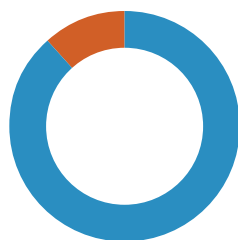
Once again, North America's 2016 full-year results exceeded expectations, with a combined ratio of 89.4% on \$654.6 million of gross premiums written. Key drivers remain disciplined underwriting, moderating underlying loss trends and favorable prior year development. While catastrophe activity was slightly lower than expectations, our results include losses from Fort McMurray, the largest catastrophe event in Canadian history, and Hurricane Matthew.

The continuation of solid results was matched by equally persistent market headwinds. In short, the contrast between our results and trading conditions could not be more stark, as positive bottom line numbers mask difficult fundamentals. Fortunately, our North America operation is well-positioned to meet the challenges ahead.

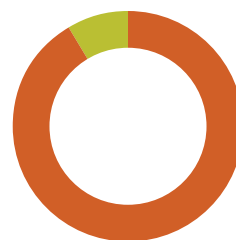
We pride ourselves in our specialist approach wherein each product line is headed by an experienced and knowledgeable underwriter with deep expertise and a lengthy, historical perspective. Whether we are managing a long-term client relationship or developing an immediate solution to a specific issue, our underwriting team is in familiar territory. By product line we know the ins and outs of the business, and where appropriate, can apply lessons of the past. We also treat our clients' problems as if they were our own, and are committed to listening, understanding, and providing feedback and alternative solutions.

Our philosophy of being "Built to Last" requires not only applied expertise, but also of critical importance is our ability to adapt to change. Traditional (re)insurance coverages increasingly occupy a landscape being transformed by technology and evolving customer buying habits. We embrace new product developments and welcome opportunities to partner with forward-thinking clients and prospects so we can collaboratively address these future challenges with innovative solutions.

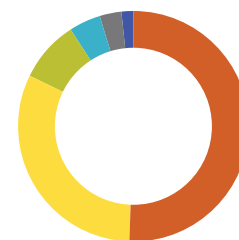
NORTH AMERICA
2016 GROSS PREMIUMS
WRITTEN
\$654.6
MILLION



● U.S. 88.5%
● CANADA 11.5%



● TREATY 91.5%
● CASUALTY FACULTATIVE 8.5%



● PROPERTY 50.6%
● CASUALTY 31.8%
● FACULTATIVE 8.5%
● ACCIDENT & HEALTH 4.4%
● SURETY 3.1%
● MARINE 1.6%

Reinsurance

LATIN AMERICA



Philippe E. Mallier
Chief Executive Officer

OdysseyRe's roots in Latin America date back nearly 20 years. What started off as a small, property facultative reinsurance operation in Mexico City, has grown into a Division that was built diligently, and patiently, over time. Today, our team in Latin America is 40-strong and possesses underwriting expertise that is second to none. Our product offerings include treaty reinsurance for property, casualty, surety, marine, aviation and agriculture, as well as facultative reinsurance for property, machinery & equipment, terrorism, energy, agriculture, general liability, professional liability and directors & officers liability.

Our strong foothold in the region is due in part to our team's in-depth understanding of the Latin American culture and a willingness to share our expertise. From our offices in Mexico City, Miami and São Paulo, Brazil, we proudly serve clients located in all countries throughout Latin America and the Caribbean. Providing clients and brokers with reinsurance solutions to meet their needs across all lines and demonstrating the highest standards of service at all times are our primary objectives.

Latin America once again reported strong year-end results in 2016 with a combined ratio of 82.7%, which was our sixth consecutive year below 85.0%. Gross premiums written totaled \$104.8 million. Net premiums written fell by 14.9%, which was primarily due to soft market conditions and the negative impact of foreign exchange rates across our regions. We saw growth in surety throughout 2016 and expanded our facultative reinsurance product offerings to include terror as well as accident & health.

In May we announced two leadership appointments: Andy Dickson as chief underwriting officer for treaty and Rogelio Diaz as chief underwriting officer for facultative and agro business. Both of these were promotions from within our Division, demonstrating our rich pool of talent and our commitment to preserving our culture. With Andy located in Miami and Rogelio in Mexico City, we will grow our business and continue to invest in our employees with expanded training and by hiring young talented professionals with strong analytical skills.

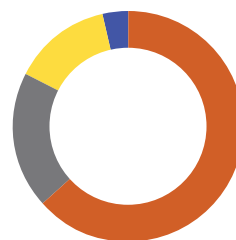
Listening to our clients regarding their exposures, assessing risk and offering tailor-made reinsurance solutions that met specific needs were fundamental to our success in 2016. Our Latin America Division is "Built to Last" and we look forward to serving our clients and business partners for many years to come.

LATIN AMERICA
2016 GROSS PREMIUMS
WRITTEN
\$104.8
MILLION



● TREATY 85.3%

● FACULTATIVE 14.7%



● PROPERTY 63.6%

● SURETY 19.1%

● CASUALTY 13.8%

● MARINE 3.5%

Reinsurance

EMEA



Isabelle Dubots-Lafitte
Chief Executive Officer

OdysseyRe offers reinsurance in Continental Europe, the Middle East and Africa (EMEA) from its offices in Paris and Stockholm. Our Paris-based underwriting team is responsible for writing property and casualty treaties in Western and Central Europe, the Middle East and Africa while the Stockholm office services the Nordic, Russian and Baltic markets.

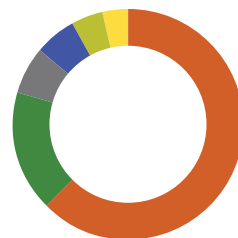
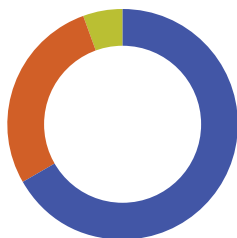
We are proud of our history and our culture, which emphasizes a patient, long-term business view and a commitment to excellent service. The vast majority of our 70 employees in the region have been with the Company for the past 20 years or longer, and many of our client relationships extend back decades.

Our 2016 year-end results were very strong despite intensified competition and increased pressure on pricing and terms. Gross premiums written totaled \$311.4 million, representing an increase of 3% from the prior year. We saw notable growth in certain markets, specifically Israel, Turkey, the Middle East and Africa. Property remains our major class representing 63% of our total volume. The balance of our portfolio is comprised of motor, credit & bond, marine, aerospace, crop and casualty treaty business.

Our strong results were driven by lower catastrophe losses and favorable loss development from prior years. The most sizeable cat event in 2016 was the Elvira floods in May and June, principally in France, Belgium and Germany. While the total industry loss was approximately \$3 billion, the impact on our results was not significant. With our geographic diversification throughout EMEA and a very stable client base, we produced a net combined ratio of 93.5%, which is in line with our 15-year average combined ratio of 93%.

During the past year we continued to build upon our capabilities by investing in talent, hiring new underwriters and actuaries who bring a fresh perspective and skillset to the business. In this challenging marketplace we remain firmly committed to understanding our clients' exposures and proactively providing solutions to meet their unique and ever-changing needs now and in the years to come.

EMEA
2016 GROSS PREMIUMS
WRITTEN
\$311.4
MILLION



EUROPE	66.8%
MIDDLE EAST	27.7%
AFRICA	5.5%

PROPERTY	62.7%
MOTOR	17.0%
CREDIT & BOND	6.6%
MARINE & AEROSPACE	5.9%
CROP	4.4%
CASUALTY	3.4%

Reinsurance

ASIAPACIFIC



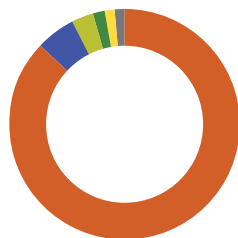
Lucien Pietropoli
Chief Executive Officer

OdysseyRe's AsiaPacific team underwrites treaty reinsurance from Singapore with the support of two representative offices in Beijing and Tokyo. Beijing, which was established in the fourth quarter of 2015, has completed its first full year and our local presence has increased our profile and provided new business opportunities. Our geographical focus includes China, Japan, South Korea, Indonesia, Hong Kong and other countries within Asia.

Our full-year 2016 results were solid as we reported gross premiums written of \$148.8 million, which represents a decrease of 8.1% from the prior year. This was driven by tough market conditions and a negative impact from foreign exchange rates. Despite those headwinds, we achieved a net combined ratio of 72.1%, which is a significant improvement over the 98.6% we recorded in 2015. Property continues to be our dominant class of business and represents 87% of our gross premiums written. Motor, credit & bond, marine, aerospace and casualty treaty business comprise the balance of our business portfolio.

While our resources and capabilities are valued by our clients and business partners, one thing is very clear: our strength is in our people. The underwriting expertise and exceptional service we offer has enabled us to maintain many long-lasting client relationships. This, along with our underwriting discipline, which emphasizes patient, profitable growth, will continue to guide our future, ensuring that we remain a strong, viable and trusted reinsurance partner for many years to come.

ASIAPACIFIC
2016 GROSS PREMIUMS
WRITTEN
\$148.8
MILLION



PROPERTY	87.2%
MARINE & AEROSPACE	5.3%
CROP	3.1%
MOTOR	1.8%
CASUALTY	1.4%
CREDIT & BOND	1.2%

Reinsurance

LONDON



Carl A. Overy
Chief Executive Officer

OdysseyRe's London branch, which operates as part of the Company's London Market Division, underwrites property, casualty, marine and aerospace treaty reinsurance. As well as serving the reinsurance needs of clients based in the London Market, including Lloyd's, the London branch's remit is global in scope allowing access to business where we have particular expertise.

Gross premiums written in 2016 were \$75.0 million, which represented a decrease of 6.5% from the prior year. The decrease reflects the increased competition and reduced prices we saw across 2016 and our disciplined response. With another benign catastrophe year combined with favorable prior year reserve releases, we produced a combined ratio of 47.7%, representing a profit of \$37.2 million. This compares to an underwriting profit of \$31.0 million in 2015, and highlights our focus on underwriting profitability as well as the strength of our reserves.

Our reputation for expertise and service with our clients and brokers continues to provide profitable opportunities, allowing us to grow our international marine, terrorism and U.K. motor portfolios in recent years. This, combined with our already significant presence in the property catastrophe and property retro markets, provides a well-diversified platform enabling us to meet our clients' reinsurance needs as well as take advantage of opportunities when they arise. These strengths ensure we are "Built to Last" beyond tomorrow.

LONDON
2016 GROSS PREMIUMS
WRITTEN
\$75.0
MILLION



PROPERTY	49.2%
MARINE & AEROSPACE	35.5%
MOTOR	9.8%
CASUALTY	5.5%



*We are not another
faceless capital
provider; we are
committed to
providing a credible
source of guidance and
market leadership.*

Insurance

2016 GROSS PREMIUMS
WRITTEN

\$1.1
BILLION

2016 COMBINED RATIO

93.7%

Specialty insurance is underwritten via Hudson Insurance Group in the U.S. and through Newline Group internationally.

Hudson offers a broad range of property and casualty insurance products to corporations, professional firms and individuals via retailers, wholesalers and program administrators. With 17 offices in the U.S. and an office in Vancouver, Canada, Hudson underwrites specialty primary and excess insurance on an admitted and non-admitted basis. Hudson is widely known for serving market niches that require highly specialized claims and underwriting capabilities. In 2016, Hudson launched a new Commercial Umbrella & Excess facility and is well positioned to respond to changing market conditions and seize opportunities that will provide for future growth.

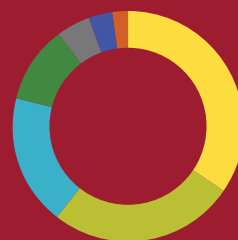
Newline's suite of casualty products is offered through two underwriting platforms, Newline Syndicate 1218 and Newline Insurance Company Limited. The Syndicate transacts business at its underwriting box at Lloyd's, with administrative support at Newline's London office. Service companies, located in Singapore, Melbourne and Malaysia, provide local, customized service and act as "coverholders" for Newline Syndicate, with full binding authority. Newline Syndicate also participates in the Lloyd's China platform in Shanghai. Newline Insurance Company Limited established a branch office in Cologne, Germany during the fourth quarter of 2016.

We continue to invest heavily in talent and technology across our insurance operations in an effort to expand our capabilities, streamline business processes and enhance our service offerings to clients and business partners.

The narratives that follow provide an in-depth view of our insurance business in the U.S. and around the world.



● U.S. 84.4%
● NON-U.S. 15.6%



● SPECIALTY LIABILITY 34.6%
● CROP 26.0%
● PROFESSIONAL LIABILITY 18.3%
● COMMERCIAL AUTO/MOTOR 10.9%
● SURETY 4.7%
● MARINE & AEROSPACE 3.4%
● SPECIALTY PROPERTY 2.1%



PRODUCT OFFERING

WITHIN THE U.S.

- COMMERCIAL AUTO
- COMMERCIAL UMBRELLA
& EXCESS
- CROP
- GENERAL LIABILITY/PACKAGE
- MANAGEMENT LIABILITY
- MEDICAL MALPRACTICE
- PERSONAL UMBRELLA
- PROFESSIONAL LIABILITY
- SPECIALTY PROPERTY & ENERGY
- SURETY

OUTSIDE THE U.S.

- CARGO & SPECIE
- CRIME
- DIRECTORS & OFFICERS
- LIABILITY
- MEDICAL MALPRACTICE
- PROFESSIONAL LIABILITY
- SPACE

We are investing in talent and technology in an effort to expand our capabilities, streamline business processes and enhance our service offerings to clients and business partners.

Insurance

U.S. ONLY



Christopher L. Gallagher
 Chief Executive Officer
 Hudson Insurance Company
 Hudson Specialty Insurance Company
 Hudson Excess Insurance Company

Hudson Insurance Group is a leading provider of specialty insurance in the United States. Based in New York City, with 17 additional offices located throughout the U.S. and in Vancouver, Canada, specialty primary and excess insurance is underwritten on an admitted basis through Hudson Insurance Company and on a non-admitted basis through Hudson Specialty Insurance Company and Hudson Excess Insurance Company.

Widely known for serving market niches that require highly specialized claims and underwriting capabilities, we focus on creating high-value solutions that give our business partners, producers and policyholders a safe harbor for the risks they face.

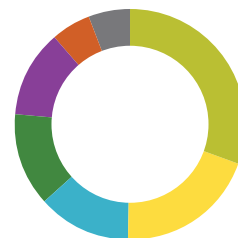
We offer a diverse range of property and casualty products and programs to corporations, professional firms and individuals through retailers, wholesalers and program administrators. Our nine underwriting units include Commercial Auto, Crop, Financial Products, General Liability & Package, Healthcare Liability, Professional Liability, Specialty Property & Energy, Surety and Tribal.

Hudson delivered excellent results in 2016, with gross premiums written reported at \$916.8 million and a net combined ratio of 93.2%. This compares to gross premiums written of \$908.2 million and a net combined ratio of 91.0% in 2015. Most of our business segments contributed to our solid underwriting performance and especially pleasing was the performance of our Crop and Surety operations, which continue to show improved profitability for the second consecutive year.

Noteworthy developments for 2016 include the launch of our new Commercial Umbrella & Excess facility in Stamford, which expands the products we offer to our wholesale business partners. We continued to make significant investments in technology and talent across the Company, especially in Risk Management and Surety. We also rebranded our fleet trucking operations under the Hudson banner and streamlined transportation risk management services under Napa River Insurance Services, Inc. With these enhancements we are well-positioned for continued growth in this sector.

With exceptional financial strength and a history that dates back to 1918, Hudson is certainly "Built to Last." We have demonstrated our ability to adapt to changing market conditions and be responsive to our clients' ever-changing needs. Hudson's expanded in-house underwriting capabilities, deep industry knowledge and experienced, talented professionals are essential to our success. Our business model allows us to focus on particular products and industry segments so that we can deliver creative, personalized products and services tailored to meeting our clients' exact needs, time and time again.

HUDSON INSURANCE GROUP
2016 GROSS PREMIUMS
WRITTEN
\$916.8
MILLION



- HUDSON INSURANCE COMPANY 74.6%
- HUDSON SPECIALTY INSURANCE COMPANY 25.4%

- CROP 30.8%
- SPECIALTY LIABILITY 19.7%
- PROFESSIONAL LINES 13.1%
- COMMERCIAL AUTO 12.9%
- GENERAL LIABILITY & PACKAGE 12.2%
- SPECIALTY PROPERTY & ENERGY 5.7%
- SURETY 5.6%



OFFICE LOCATIONS

NEW YORK

100 William Street
New York, NY 10038
USA
Tel. +1 212 978 2800

ATLANTA

Tel. +1 678 331 4200

AVON

Tel. +1 203 977 6400

CALABASAS

Tel. +1 818 449 3111

CHICAGO

Tel. +1 312 596 0222

CORONA

Tel. +1 951 278 5648

FORT WASHINGTON

Tel. +1 212 978 2717

INDIANAPOLIS

Tel. +1 317 582 0073

KANSAS CITY

Tel. +1 816 778 0708

LAKE MARY

Tel. +1 407 710 1880

MINEOLA

Tel. +1 212 384 0100

MORRISTOWN

Tel. +1 212 384 0125

NAPA

Tel. +1 707 225 3300

OVERLAND PARK

Tel. +1 913 345 1515

SAN FRANCISCO

Tel. +1 415 423 1333

STAMFORD

Tel. +1 203 977 8000

VANCOUVER

Tel. +1 604 449 5360

WESTLAKE

Tel. +1 440 925 1995

Insurance

OUTSIDE THE U.S.



Carl A. Overy
 Chief Executive Officer
 Newline Syndicate 1218
 Newline Insurance
 Company Limited

Operating as the specialty insurance arm of OdysseyRe’s London Market Division, Newline Group is comprised of Newline Syndicate 1218 at Lloyd’s and Newline Insurance Company Limited. Headquartered in London with 114 professionals serving clients around the world, Newline Group offers a suite of products on a direct and facultative basis. Our product offerings include public liability, employers liability, products liability, commercial crime, bankers blanket bond, professional liability, directors and officers liability, medical malpractice, satellite, cargo and specie.

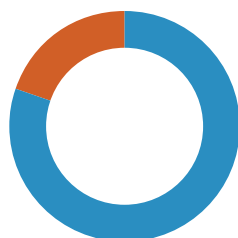
Newline’s territorial focus is predominantly the U.K., Continental Europe, Australia, Asia Pacific and Canada. Our global reach is provided through offices in London, Melbourne, Singapore, Shanghai (as part of Lloyd’s China) and Labuan, Malaysia. In addition, we established an office in Cologne, Germany in the fourth quarter of 2016. This new branch provides Newline with a foothold in Europe and will provide greater penetration within Germany and Eastern Europe.

Gross premiums written in 2016 were \$169.3 million, down from \$181.7 million in 2015. The decrease in business volume was driven by increasing competition, the non-renewal of a large Italian medical malpractice policy and the negative impact of foreign exchange movements. We partially offset these reductions with growth in our liability portfolio. Market conditions remain challenging, but notwithstanding this, Newline generated a combined ratio of 96.4%, which we attribute to our prudent risk selection, efficient deployment of capacity and strong historical reserving.

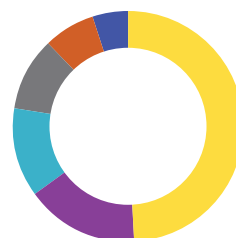
Distribution and being closer to our clients has been, and continues to be, very important. This is demonstrated by our continued expansion overseas by establishing local offices in key territories. We expect this will provide a solid base for future growth as and when market conditions improve.

2016 also marked Newline’s 20th anniversary. We have had an excellent run over the past two decades and are excited about our future as we continue to build a business to last for many years to come.

NEWLINE GROUP
2016 GROSS PREMIUMS
WRITTEN
\$169.3
MILLION



- NEWLINE SYNDICATE AT LLOYD'S 80.3%
- NEWLINE INSURANCE COMPANY LIMITED 19.7%



- LIABILITY 49.2%
- FINANCIAL INSTITUTIONS 15.9%
- PROFESSIONAL LIABILITY 12.5%
- MEDICAL MALPRACTICE 10.4%
- DIRECTORS & OFFICERS 7.2%
- SPACE & MARINE CARGO 4.8%



OFFICE LOCATIONS

LONDON

Corn Exchange
55 Mark Lane
London EC3R 7NE
England
Tel. +44 020 7090 1700

COLOGNE

Tel. +49.221.9669.4512

LABUAN

Tel. +60 87 442899

MANCHESTER

Tel. +44 0161 638 9350

MELBOURNE

Tel. +61 03 9999 1901

SINGAPORE

Tel. +65 6212 1290

SHANGHAI

Newline Underwriting Division
at Lloyd's
Tel. +86 021 6162 8200

We are well-positioned to respond to changing market conditions and seize opportunities that will provide for future growth.

Executive leadership

ODYSSEY RE HOLDINGS CORP.

BOARD OF DIRECTORS

⁽¹⁾ Compensation Committee

⁽²⁾ Audit Committee

Andrew A. Barnard ⁽¹⁾

*Chairman of the Board,
President and
Chief Operating Officer*
Fairfax Insurance Group

Brandon W. Sweitzer ⁽¹⁾⁽²⁾

*Dean, School of Risk
Management*
St. John's University School
of Risk Management

Peter S. Clarke ⁽²⁾

*Vice President and
Chief Risk Officer*
Fairfax Financial Holdings
Limited

Brian D. Young

*President and
Chief Executive Officer*
Odyssey Re Holdings Corp.

David J. Bonham ⁽²⁾

*Vice President and
Chief Financial Officer*
Fairfax Financial Holdings
Limited

Paul C. Rivett

President
Fairfax Financial Holdings
Limited

OFFICERS

Brian D. Young

*President and
Chief Executive Officer*

Michael G. Wacek

*Executive Vice President and
Chief Risk Officer*

Jan Christiansen

*Executive Vice President and
Chief Financial Officer*

Peter H. Lovell

*Senior Vice President,
General Counsel and
Corporate Secretary*

EXECUTIVE TEAM

Alane R. Carey

*Executive Vice President
Director of Global Marketing*

Philippe E. Mallier

*Chief Executive Officer
Latin America*

Brian D. Quinn

*Chief Executive Officer
North America*

Isabelle Dubots-Lafitte

*Chief Executive Officer
Europe, Middle East & Africa*

Carl A. Overy

*Chief Executive Officer
London Market*

Jeffrey M. Rubin

*Senior Vice President
Director of Global Claims*

Christopher L. Gallagher

*Chief Executive Officer
U.S. Insurance*

Lucien Pietropoli

*Chief Executive Officer
AsiaPacific*

Elizabeth A. Sander

*Executive Vice President
and Chief Actuary*



Independent Auditor's Report

To the Board of Directors of Odyssey Re Holdings Corp.:

We have audited the accompanying consolidated financial statements of Odyssey Re Holdings Corp. and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2016 and December 31, 2015, and the related consolidated statements of operations, comprehensive income, shareholders' equity and cash flows for each of the three years ended December 31, 2016.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Odyssey Re Holdings Corp. and its subsidiaries at December 31, 2016 and December 31, 2015 and the results of their operations and their cash flows for the three years ended December 31, 2016 in accordance with accounting principles generally accepted in the United States of America.

/s/ PricewaterhouseCoopers LLP

New York, New York
March 3, 2017

ODYSSEY RE HOLDINGS CORP.
CONSOLIDATED BALANCE SHEETS

	December 31,	
	2016	2015
	(In thousands, except share and per share amounts)	
ASSETS		
Investments and cash:		
Fixed income securities, available for sale, at fair value (amortized cost \$855,017 and \$1,341,079, respectively)	\$ 958,664	\$ 1,539,393
Fixed income securities, held for trading, at fair value (amortized cost \$1,963,009 and \$2,703,028, respectively)	1,895,406	2,592,569
Preferred stocks, held for trading, at fair value (cost \$0 and \$88,874, respectively)	—	54,155
Equity securities:		
Common stocks, available for sale, at fair value (cost \$135,896 and \$150,903, respectively)	154,457	191,443
Common stocks, held for trading and fair value options, at fair value (cost \$1,130,448 and \$1,396,476, respectively)	1,033,399	1,307,077
Common stocks, at equity	398,019	254,725
Short-term investments, held for trading, at fair value (amortized cost \$1,742,357 and \$708,749, respectively)	1,742,357	708,749
Cash and cash equivalents	604,861	460,267
Cash and cash equivalents held as collateral	218,660	200,717
Other invested assets	843,556	903,708
Total investments and cash	7,849,379	8,212,803
Accrued investment income	32,123	46,263
Premiums receivable	700,809	681,323
Reinsurance recoverable on paid losses	42,081	41,471
Reinsurance recoverable on unpaid losses	658,607	690,884
Prepaid reinsurance premiums	74,119	96,516
Funds held by reinsureds	129,949	125,380
Deferred acquisition costs	165,661	156,587
Federal and foreign income taxes receivable	400,782	207,371
Other assets	128,953	137,844
Total assets	\$ 10,182,463	\$ 10,396,442
LIABILITIES		
Unpaid losses and loss adjustment expenses	\$ 4,876,848	\$ 5,002,422
Unearned premiums	722,455	729,447
Reinsurance balances payable	149,178	157,633
Funds held under reinsurance contracts	56,734	42,297
Debt obligations	89,815	89,773
Other liabilities	454,254	416,678
Total liabilities	6,349,284	6,438,250
Commitments and Contingencies (Note 11)		
SHAREHOLDERS' EQUITY		
Non-controlling interest - preferred shares of subsidiaries	29,299	29,299
Common shares, \$10.00 par value; 60,000 shares authorized; 49,170 shares issued and outstanding	492	492
Additional paid-in capital	1,746,290	1,747,017
Accumulated other comprehensive income, net of deferred income taxes	67,581	151,164
Retained earnings	1,989,517	2,030,220
Total shareholders' equity	3,833,179	3,958,192
Total liabilities and shareholders' equity	\$ 10,182,463	\$ 10,396,442

See accompanying notes to consolidated financial statements.

ODYSSEY RE HOLDINGS CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
REVENUES			
Gross premiums written	\$ 2,380,747	\$ 2,403,985	\$ 2,739,511
Ceded premiums written	280,570	309,000	345,678
Net premiums written	2,100,177	2,094,985	2,393,833
(Increase) decrease in net unearned premiums	(26,081)	109,085	(37,256)
Net premiums earned	2,074,096	2,204,070	2,356,577
Net investment income	215,073	217,160	216,851
Net realized investment (losses) gains:			
Realized investment (losses) gains	(185,688)	(51,388)	461,009
Other-than-temporary impairment losses	(16,227)	(65,120)	(103,887)
Total net realized investment (losses) gains	(201,915)	(116,508)	357,122
Total revenues	<u>2,087,254</u>	<u>2,304,722</u>	<u>2,930,550</u>
EXPENSES			
Losses and loss adjustment expenses	1,171,825	1,185,774	1,283,997
Acquisition costs	431,417	449,083	478,060
Other underwriting expenses	241,329	237,303	237,121
Other expense, net	74,559	8,131	18,534
Interest expense	2,801	5,463	12,659
Total expenses	<u>1,921,931</u>	<u>1,885,754</u>	<u>2,030,371</u>
Income before income taxes	<u>165,323</u>	<u>418,968</u>	<u>900,179</u>
Federal and foreign income tax provision (benefit):			
Current	28,508	228,267	222,267
Deferred	(24,093)	(108,593)	87,228
Total federal and foreign income tax provision	4,415	119,674	309,495
Net income	<u>\$ 160,908</u>	<u>\$ 299,294</u>	<u>\$ 590,684</u>

See accompanying notes to consolidated financial statements.

ODYSSEY RE HOLDINGS CORP.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
Net income	\$ 160,908	\$ 299,294	\$ 590,684
OTHER COMPREHENSIVE (LOSS) INCOME, BEFORE TAX			
Unrealized net (depreciation) appreciation on securities arising during the period	(53,043)	(291,276)	193,946
Reclassification adjustment for net realized investment (gains) losses included in net income	(48,910)	(34,436)	37,683
Foreign currency translation adjustments.....	(24,166)	(27,086)	23,313
Benefit plan liabilities	(2,440)	(1,447)	(23,473)
Other comprehensive (loss) income , before tax.....	(128,559)	(354,245)	231,469
TAX BENEFIT (PROVISION)			
Unrealized net depreciation (appreciation) on securities arising during the period	18,546	101,702	(67,725)
Reclassification adjustment for net realized investment gains (loss) included in net income	17,118	12,053	(13,189)
Foreign currency translation adjustments.....	8,458	9,480	(8,160)
Benefit plan liabilities	854	506	8,216
Total tax benefit (provision).....	44,976	123,741	(80,858)
Other comprehensive (loss) income, net of tax	(83,583)	(230,504)	150,611
Comprehensive income.....	\$ 77,325	\$ 68,790	\$ 741,295

See accompanying notes to consolidated financial statements.

ODYSSEY RE HOLDINGS CORP.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

	Years Ended December 31,		
	2016	2015	2014
(In thousands, except common share amounts)			
NON-CONTROLLING INTEREST - PREFERRED SHARES OF SUBSIDIARIES			
Balance, beginning and end of year	\$ 29,299	\$ 29,299	\$ 29,299
PREFERRED SHARES (par value)			
Balance, beginning of year	—	—	3
Series A and B preferred shares redemptions	—	—	(3)
Balance, end of year	—	—	—
COMMON SHARES (par value)			
Balance, beginning of year	492	477	535
Common shares capital contributions	—	15	155
Common shares capital redemptions	—	—	(213)
Balance, end of year	492	492	477
ADDITIONAL PAID-IN CAPITAL			
Balance, beginning of year	1,747,017	1,639,236	587,994
Common shares capital contributions	—	124,985	1,291,012
Net change due to stock option exercises and restricted share awards	(727)	(17,204)	753
Series A and B preferred shares redemptions	—	—	(7,868)
Common shares capital redemptions	—	—	(232,655)
Balance, end of year	1,746,290	1,747,017	1,639,236
ACCUMULATED OTHER COMPREHENSIVE INCOME, NET OF DEFERRED INCOME TAXES			
Balance, beginning of year	151,164	381,668	231,057
Unrealized net (depreciation) appreciation on securities, net of reclassification adjustments	(66,289)	(211,957)	150,715
Foreign currency translation adjustments	(15,708)	(17,606)	15,153
Benefit plan liabilities	(1,586)	(941)	(15,257)
Balance, end of year	67,581	151,164	381,668
RETAINED EARNINGS			
Balance, beginning of year	2,030,220	1,932,537	2,881,846
Net income	160,908	299,294	590,684
Dividends to preferred shareholders and non-controlling interest	(1,611)	(1,611)	(2,188)
Dividends to common shareholder	(200,000)	(200,000)	—
Loss on redemption of Series A and Series B preferred shares ...	—	—	(218)
Capital redemptions on common shares	—	—	(1,537,587)
Balance, end of year	1,989,517	2,030,220	1,932,537
TOTAL SHAREHOLDERS' EQUITY	<u>\$ 3,833,179</u>	<u>\$ 3,958,192</u>	<u>\$ 3,983,217</u>
COMMON SHARES OUTSTANDING			
Balance, beginning of year	49,170	47,668	53,440
Repurchased and retired	—	—	(21,327)
Shares issued	—	1,502	15,555
Balance, end of year	49,170	49,170	47,668

See accompanying notes to consolidated financial statements.

ODYSSEY RE HOLDINGS CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	\$ 160,908	\$ 299,294	\$ 590,684
Adjustments to reconcile net income to net cash provided by operating activities:			
(Increase) decrease in premiums receivable and funds held, net of reinsurance	(26,572)	49,546	(13,045)
Increase (decrease) in unearned premiums and prepaid reinsurance premiums, net...	26,792	(98,730)	39,834
Increase (decrease) in unpaid losses and loss adjustment expenses, net of reinsurance.....	10,496	(130,140)	(6,768)
(Increase) decrease in current and deferred federal and foreign income taxes, net	(148,440)	(177,416)	222,137
(Increase) decrease in deferred acquisition costs	(11,419)	27,077	(6,787)
Change in other assets and liabilities, net.....	41,937	(25,032)	(35,786)
Net realized investment losses (gains).....	201,915	116,508	(357,122)
Bond discount amortization, net.....	(4,183)	(2,985)	(16,768)
Amortization of compensation plans	14,655	13,440	10,008
Net cash provided by operating activities	<u>266,089</u>	<u>71,562</u>	<u>426,387</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Maturities of fixed income securities, available for sale.....	63,890	3,445	5,918
Sales of fixed income securities, available for sale	501,833	158,077	148,923
Purchases of fixed income securities, available for sale	(5,330)	(8,203)	(48,925)
Sales of equity securities, available for sale.....	584	172,436	123,970
Purchases of equity securities, available for sale.....	(95,254)	(156,786)	(17,999)
Net settlements of other invested assets	(9,944)	310,631	155,548
Purchases of other invested assets.....	(112,762)	(157,199)	(152,629)
Net change in cash and cash equivalents held as collateral.....	(11,280)	(12,429)	16,758
Sales of trading securities	5,345,260	1,957,778	3,316,403
Purchases of trading securities	(5,748,858)	(2,406,470)	(3,896,636)
Net purchases of fixed assets	(10,680)	(10,760)	(10,871)
Acquisition of net assets of a business	—	(9,300)	(7,779)
Net cash used in investing activities	<u>(82,541)</u>	<u>(158,780)</u>	<u>(367,319)</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Common shares capital contributions	—	125,000	202,248
Capital redemptions on common shares	—	—	(196,242)
Repayment of debt obligations	—	—	(50,000)
Repayment of debt obligations upon maturity.....	—	(125,000)	—
Purchase of restricted shares	(15,382)	(30,625)	(9,088)
Dividends paid to preferred shareholders	(1,611)	(1,611)	(2,188)
Dividends paid to common shareholder.....	(2)	—	—
Net cash used in financing activities	<u>(16,995)</u>	<u>(32,236)</u>	<u>(55,270)</u>
Effect of exchange rate changes on cash and cash equivalents.....	<u>(21,959)</u>	<u>(31,994)</u>	<u>(35,317)</u>
Increase (decrease) in cash and cash equivalents.....	144,594	(151,448)	(31,519)
Cash and cash equivalents, beginning of year	460,267	611,715	643,234
Cash and cash equivalents, end of year	<u>\$ 604,861</u>	<u>\$ 460,267</u>	<u>\$ 611,715</u>
Supplemental disclosures of cash flow information:			
Interest paid.....	\$ 2,741	\$ 6,685	\$ 12,162
Income taxes paid	\$ 152,842	\$ 298,026	\$ 87,374
Non-cash activity:			
Dividends paid to common shareholder	\$ 199,998	\$ 200,000	\$ —
Receipt of securities for issuance of common shares	\$ —	\$ —	\$ 200,660
Distribution of securities for redemption of common shares	\$ —	\$ —	\$ 685,958
Distribution of securities for redemption of preferred shares	\$ —	\$ —	\$ 8,090

See accompanying notes to consolidated financial statements.

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization

Odyssey Re Holdings Corp., a Delaware corporation (together with its subsidiaries, the “Company” or “OdysseyRe”; on a stand-alone basis, “ORH”), is an underwriter of reinsurance, providing a full range of property and casualty products on a worldwide basis, and an underwriter of specialty insurance, primarily in the United States and through the Lloyd’s of London (“Lloyd’s”) marketplace. ORH owns all of the common shares of Odyssey Reinsurance Company (“ORC”), its principal operating subsidiary, which is domiciled in the state of Connecticut. ORC directly or indirectly owns all of the common shares of the following subsidiaries:

- Hudson Insurance Company (“Hudson”) and its subsidiaries:
 - Hudson Specialty Insurance Company (“Hudson Specialty”);
 - Hudson Excess Insurance Company (“Hudson Excess”); and
 - Napa River Insurance Services, Inc.
- Clearwater Select Insurance Company (“Clearwater Select”);
- Newline Holdings U.K. Limited and its subsidiaries (collectively, “Newline”):
 - Newline Underwriting Management Limited, which manages Newline Syndicate (1218), a member of Lloyd’s;
 - Newline Insurance Company Limited (“NICL”); and
 - Newline Corporate Name Limited (“NCNL”), which provides capital for and receives distributed earnings from Newline Syndicate (1218).

Fairfax Financial Holdings Limited (“Fairfax”), a publicly traded financial services holding company based in Canada, ultimately owns 100% of the common shares of ORH and 100% of the preferred shares of ORH’s subsidiaries.

In the fourth quarter of 2014, Fairfax reorganized and aligned the ownership of the Company under a single Fairfax intermediate holding company in the United States, Odyssey US Holdings Inc. (“OUSHI”). To facilitate the reorganization, ORH redeemed from various Fairfax entities i) all of its outstanding preferred shares (253,599 Series A shares and 70,000 Series B shares) for \$8.1 million in cash and marketable securities, ii) 10,627 of its outstanding common shares for \$882.2 million in cash and marketable securities and iii) 10,700 of its outstanding common shares for \$888.3 million in notes issued by ORH payable to Fairfax (US) Inc. (“Fairfax (US)”), which is Fairfax’s top-tier U.S. holding company. All of the remaining outstanding common shares of ORH were distributed in a tax-free spin-off culminating in the ownership of all of ORH’s common stock under OUSHI, a subsidiary of Fairfax (US). After borrowing \$400.0 million from Fairfax, OUSHI contributed \$400.0 million to ORH and agreed to assume ORH’s \$888.3 million note payable to Fairfax (US) in exchange for 15,518 shares of ORH’s common stock. In connection with this transaction, Fairfax (US) agreed to release ORH from all obligations relating to the \$888.3 million note. ORH’s shareholders’ equity decreased by \$490.3 million as a result of these transactions.

Dividends and returns of capital from the Company are expected to be the source of funds for servicing OUSHI’s debt obligations owed to various Fairfax entities.

2. Summary of Significant Accounting Policies

(a) *Basis of Presentation.* The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany transactions have been eliminated.

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The preparation of consolidated financial statements in conformity with GAAP requires the Company to make estimates and assumptions that could differ materially from actual results affecting the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. The Company considers its accounting policies that are most dependent on the application of estimates and assumptions as critical accounting estimates, which are defined as estimates that are both i) important to the portrayal of the Company's financial condition and results of operations and ii) require the Company to exercise significant judgment. These estimates, by necessity, are based on assumptions about numerous factors.

The Company reviews its critical accounting estimates and assumptions on a quarterly basis, including: the estimate of reinsurance premiums and premium related amounts; establishing deferred acquisition costs; goodwill and intangible impairment evaluations; an evaluation of the adequacy of reserves for unpaid losses and loss adjustment expenses; review of its reinsurance and retrocession agreements; estimates related to income taxes, including an analysis of the recoverability of deferred income tax assets; and an evaluation of its investment portfolio, including a review for other-than-temporary declines in estimated fair value.

(b) *Investments.* The majority of the Company's investments in fixed income securities and common stocks are categorized as "available for sale" or "held for trading" and are recorded at their estimated fair value based on quoted market prices (see Note 3). Most investments in common stocks of affiliates are carried at the Company's proportionate share of the equity of those affiliates. Short-term investments, which are classified as "held for trading" and which have a maturity of one year or less from the date of purchase, are carried at fair value. The Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Cash equivalents include certificates of deposits totaling \$11.3 million and \$10.6 million as of December 31, 2016 and 2015, respectively. Investments in limited partnerships and investment funds have been reported in other invested assets. Other invested assets also include trust accounts relating to the Company's benefit plans and derivative securities, all of which are carried at fair value. The Company routinely evaluates the carrying value of its investments in common stocks of affiliates and in partnerships and investment funds. In the case of limited partnerships and investment funds, the carrying value is generally established on the basis of the net valuation criteria as determined by the managers of the investments. Such valuations could differ significantly from the values that would have been available had markets existed for the securities. Investment transactions are recorded on their trade date, with balances pending settlement reflected in the consolidated balance sheets as a component of other assets or other liabilities.

Investment income, which is reported net of applicable investment expenses, is recorded as earned. Realized investment gains or losses are determined on the basis of average cost. The Company records, in investment income, its proportionate share of income or loss, including realized gains or losses, for those securities for which the equity method of accounting is utilized, which include most common stocks of affiliates, limited partnerships and investment funds. Due to the timing of when financial information is reported by equity investees and received by the Company, including limited partnerships and investment funds, results attributable to these investments are generally reported by the Company on a one month or one quarter lag. Unrealized appreciation and depreciation related to trading securities is recorded as realized investment gains or losses in the consolidated statements of operations.

The net amount of unrealized appreciation or depreciation on the Company's available for sale investments, net of applicable deferred income taxes, is reflected in shareholders' equity in accumulated other comprehensive income. A decline in the fair value of an available for sale investment below its cost or amortized cost that is deemed other-than-temporary is recorded as a realized investment loss in the consolidated statements of operations, resulting in a new cost or amortized cost basis for the investment. Other-than-temporary declines in the carrying values of investments recorded in accordance with the equity method of accounting are recorded in net investment income in the consolidated statements of operations.

(c) *Premium Revenue Recognition.* Reinsurance assumed premiums written and related costs are based upon reports received from ceding companies. When reinsurance assumed premiums written have not been reported by the ceding company they are estimated, at the individual contract level, based on historical patterns and experience from the ceding company and judgment of the Company. Subsequent adjustments to premiums written, based on actual results or revised estimates from the ceding company, are recorded in the period in which they become known. Reinsurance assumed premiums written related to proportional treaty business are established on a basis that is consistent with the coverage periods under the terms of the underlying insurance contracts. Reinsurance assumed premiums written related to excess of loss and facultative reinsurance business

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

are recorded over the coverage term of the contracts, which is generally one year. Unearned premium reserves are established for the portion of reinsurance assumed premiums written that are to be recognized over the remaining contract period. Unearned premium reserves related to proportional treaty contracts are computed based on reports received from ceding companies, which show premiums written but not yet earned. Premium adjustments made over the life of the contract are recognized as earned premiums based on the applicable contract period to which they apply. Insurance premiums written are based upon the effective date of the underlying policy and are generally earned on a pro rata basis over the policy period, which is usually one year. A reserve for uncollectible premiums is established when deemed necessary. The Company has established a reserve for potentially uncollectible premium receivable balances of \$10.2 million and \$9.6 million as of December 31, 2016 and 2015, respectively, which has been netted against premiums receivable.

The cost of reinsurance purchased by the Company (reinsurance premiums ceded) is reported as prepaid reinsurance premiums and amortized over the contract period in proportion to the amount of reinsurance protection provided. The ultimate amount of premiums, including adjustments, is recognized as premiums ceded, and amortized over the applicable contract period to which they apply. Premiums earned are reported net of reinsurance ceded premiums earned in the consolidated statements of operations. Amounts paid by the Company for retroactive reinsurance that meet the conditions for reinsurance accounting are reported as reinsurance receivables to the extent those amounts do not exceed the associated liabilities. If the liabilities exceed the amounts paid, reinsurance receivables are increased to reflect the difference, and the resulting gain is deferred and amortized over the estimated settlement period. If the amounts paid for retroactive reinsurance exceed the liabilities, the related liabilities are increased or the reinsurance receivable is reduced, or both, at the time the reinsurance contract is effective, and the excess is charged to net income. Changes in the estimated amount of liabilities relating to the underlying reinsured contracts are recognized in net income in the period of the change. Assumed and ceded reinstatement premiums represent additional premiums related to reinsurance coverages, principally catastrophe excess of loss contracts, which are paid when the incurred loss limits have been utilized under the reinsurance contract and such limits are reinstated. Premiums written and earned premiums related to a loss event are estimated and accrued as earned. The accrual is adjusted based upon any change to the ultimate losses incurred under the contract.

(d) *Deferred Acquisition Costs.* Acquisition costs, which are reported net of costs recovered under ceded contracts, consist of commissions and brokerage expenses incurred on insurance and reinsurance business written, and premium taxes on direct insurance written, and are deferred and amortized over the period in which the related premiums are earned. Commission adjustments are accrued based on changes in premiums and losses recorded by the Company in the period in which they become known. Deferred acquisition costs are limited to their estimated realizable value based on the related unearned premium, which considers anticipated losses and loss adjustment expenses and estimated remaining costs of servicing the business, all based on historical experience. The realizable value of the Company's deferred acquisition costs is determined without consideration of investment income.

Included in acquisition costs in the consolidated statements of operations are amortized deferred acquisition costs of \$418.2 million, \$437.4 million and \$479.3 million for the years ended December 31, 2016, 2015 and 2014, respectively.

(e) *Goodwill and Intangible Assets.* The Company accounts for goodwill and intangible assets as permitted or required by GAAP. A purchase price paid that is in excess of net assets arising from a business combination is recorded as an asset ("goodwill") and is not amortized. Intangible assets with finite lives are amortized over the estimated useful life of the asset. Intangible assets with indefinite useful lives are not amortized. Goodwill and intangible assets are analyzed for impairment on an annual basis or more frequently if events or changes in circumstances indicate that the carrying amount may not be recoverable. If the goodwill or intangible asset is impaired, it is written down to its realizable value with a corresponding expense reflected in the consolidated statements of operations. For the year ended December 31, 2016, the Company impaired \$6.8 million of goodwill related to its acquisition of an agency producing financial products. For the year ended December 31, 2015, the Company impaired \$1.4 million of intangible assets with finite lives related to its acquisition of an agency producing surety business. The Company did not incur any impairment of its goodwill or intangible assets for the year ended December 31, 2014.

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table reflects the carrying amount of goodwill, intangible assets with indefinite lives and intangible assets with finite lives as of December 31, 2016 and 2015 (in thousands):

	Intangible Assets			Total
	Goodwill	Indefinite Lives	Finite Lives	
Balance, January 1, 2015	\$ 48,554	\$ 5,813	\$ 17,744	\$ 72,111
Acquired during 2015	10,498	—	950	11,448
Amortization during 2015	—	—	(5,476)	(5,476)
Impairment during 2015	—	—	(1,402)	(1,402)
Balance, December 31, 2015	59,052	5,813	11,816	76,681
Acquired during 2016	—	—	—	—
Amortization during 2016	—	—	(5,093)	(5,093)
Impairment during 2016	(6,795)	—	—	(6,795)
Balance, December 31, 2016	<u>\$ 52,257</u>	<u>\$ 5,813</u>	<u>\$ 6,723</u>	<u>\$ 64,793</u>

The Company acquired \$5.7 million of intangible assets with finite lives during the year ended December 31, 2014. The Company amortized \$4.6 million during the year ended December 31, 2014 related to its intangible assets with finite lives.

The following table provides the estimated amortization expense related to intangible assets for the succeeding three years (in thousands):

	Years Ended December 31,		
	2017	2018	2019
Amortization of intangible assets	\$ 3,675	\$ 2,522	\$ 526

Intangible assets with finite lives will be fully amortized as of December 31, 2019.

(f) *Unpaid losses and loss adjustment expenses.* The reserves for losses and loss adjustment expenses are estimates of amounts needed to pay reported and unreported claims and related loss adjustment expenses. The estimates are based on assumptions related to the ultimate cost to settle such claims. The inherent uncertainties of estimating reserves are greater for reinsurers than for primary insurers due to the diversity of development patterns among different types of reinsurance contracts and the necessary reliance on ceding companies for information regarding reported claims. As a result, there can be no assurance that the ultimate liability will not exceed amounts reserved, with a resulting adverse effect on the Company.

The reserves for unpaid losses and loss adjustment expenses are based on the Company's evaluations of reported claims and individual case estimates received from ceding companies for reinsurance business or the estimates advised by the Company's claims adjusters for insurance business. The Company utilizes generally accepted actuarial methodologies to determine reserves for losses and loss adjustment expenses on the basis of historical experience and other estimates. The reserves are reviewed continually during the year and changes in estimates in losses and loss adjustment expenses are reflected as an expense in the consolidated statements of operations in the period the adjustment is made. Reinsurance recoverables on unpaid losses and loss adjustment expenses are reported as assets. A reserve for uncollectible reinsurance recoverables is established based on an evaluation of each reinsurer or retrocessionaire and historical experience. The Company uses tabular reserving for workers' compensation indemnity loss reserves, which are considered to be fixed and determinable, and discounts such reserves using an interest rate of 3.5% and the Life Table for Total Population: United States, 2009.

(g) *Deposit Assets and Liabilities.* The Company may enter into assumed and ceded reinsurance contracts that contain certain loss limiting provisions and, as a result, do not meet the risk transfer provisions of GAAP. These contracts are deemed as either transferring only significant timing risk or only significant underwriting risk or transferring neither significant timing nor underwriting risk and are accounted for using the deposit accounting method, under which revenues and expenses from reinsurance contracts are not recognized as written premium and incurred losses. Instead, the profits or losses from these contracts are recognized net, as other income or other expense over the contract or contractual settlement periods.

For such contracts, the Company initially records the amount of consideration paid as a deposit asset or received as a deposit liability. Revenue or expense is recognized over the term of the contract, with any deferred

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

amount recorded as a component of assets or liabilities until such time it is earned. The ultimate asset or liability under these contracts is estimated, and the asset or liability initially established, which represents consideration received, is increased or decreased over the term of the contract. The change during the period is recorded in the Company's consolidated statements of operations, with increases and decreases in the ultimate asset or liability shown in other expense, net. As of December 31, 2016 and 2015, the Company had reflected \$7.0 million and \$7.2 million in other assets and \$0.3 million and less than \$0.1 million in other liabilities, respectively, related to deposit contracts. In cases where cedants retain the consideration on a funds held basis, the Company records those assets in other assets, and records the related investment income on the assets in the Company's consolidated statements of operations as investment income.

(h) *Income Taxes.* The Company records deferred income taxes to provide for the net tax effect of temporary differences between the carrying values of assets and liabilities in the Company's consolidated financial statements and their tax bases. Such differences relate principally to deferred acquisition costs, unearned premiums, unpaid losses and loss adjustment expenses, investments and tax credits. Deferred tax assets are reduced by a valuation allowance when the Company believes it is more likely than not that all or a portion of deferred taxes will not be realized. As of December 31, 2016 and 2015, a valuation allowance was not required.

The Company has elected to recognize accrued interest and penalties associated with uncertain tax positions as part of the income tax provision. As of December 31, 2016 and 2015, the Company has not recorded any interest or penalties.

(i) *Derivatives.* The Company utilizes derivative instruments to manage against potential adverse changes in the value of its assets and liabilities. Derivatives include total return swaps, interest rate swaps, forward currency contracts, U.S. Treasury bond forward contracts, CPI-linked derivative contracts, credit default swaps, call options and warrants and other equity and credit derivatives. In addition, the Company holds options on certain securities within its fixed income portfolio that allow the Company to extend the maturity date on fixed income securities or convert fixed income securities to equity securities. The Company categorizes these investments as trading securities, and changes in fair value are recorded as realized investment gains or losses in the consolidated statements of operations. All derivative instruments are recognized as either assets or liabilities on the consolidated balance sheet and are measured at their fair value. Gains or losses from changes in the derivative values are reported based on how the derivative is used and whether it qualifies for hedge accounting. For derivative instruments that do not qualify for hedge accounting, changes in fair value are included in realized investment gains and losses in the consolidated statements of operations. Margin balances required by counterparties in support of derivative positions are included in fixed income securities and short-term investments.

(j) *Foreign Currency.* Foreign currency transaction gains or losses resulting from a change in exchange rates between the currency in which a transaction is denominated, or the original currency, and the functional currency are reflected in the consolidated statements of operations in the period in which they occur. The Company translates the financial statements of its foreign subsidiaries and branches that have functional currencies other than the U.S. dollar into U.S. dollars by translating balance sheet accounts at the balance sheet date exchange rate and income statement accounts at the rate at which the transaction occurs or the average exchange rate for each quarter. Translation gains or losses are recorded, net of deferred income taxes, as a component of accumulated other comprehensive income.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table presents the foreign exchange effect, net of the effects of foreign currency forward contracts purchased as an economic hedge against foreign exchange rate volatility and of tax, on specific line items in the Company's financial statements for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Statement of operations:			
Realized investment gains (losses):			
Foreign currency forward contracts gains	\$ 4,330	\$ 81,354	\$ 78,690
Other investment gains (losses)	41,940	(77,071)	(92,557)
Total realized investment gains (losses)	46,270	4,283	(13,867)
Net investment income	1,240	262	1,258
Other (expense) income, net	(52,084)	13,600	4,548
(Loss) income before income taxes	(4,574)	18,145	(8,061)
Total federal and foreign income tax (benefit) provision	(1,600)	6,351	(2,821)
Net (loss) income	(2,974)	11,794	(5,240)
Other comprehensive (loss) income, net of tax	(15,708)	(17,606)	15,153
Total effect on comprehensive (loss) income and shareholders' equity	<u>\$ (18,682)</u>	<u>\$ (5,812)</u>	<u>\$ 9,913</u>

(k) *Stock-Based Compensation Plans.* The Company reflects awards of restricted common stock of Fairfax to employees as a reduction to additional paid-in-capital when the shares are purchased and amortizes the award value through compensation expense over the related vesting periods.

(l) *Payments.* Payments of claims by the Company, as reinsurer, to a broker on behalf of a reinsured company are recorded in the Company's financial statements as a paid loss at the time the cash is disbursed and is treated as paid to the reinsured. Premiums due to the Company from the reinsured are recorded as receivables from the reinsured until the cash is received by the Company, either directly from the reinsured or from the broker.

(m) *Funds Held Balances.* "Funds held under reinsurance contracts" represents amounts due to reinsurers arising from the Company's receipt of a deposit from a reinsurer, or the withholding of a portion of the premiums due, in accordance with contractual terms, as a guarantee the reinsurer will meet its loss and other obligations. Interest generally accrues on withheld funds in accordance with contract terms. "Funds held by reinsured" represents amount due from a ceding company that withholds, in accordance with the contractual terms, a portion of the premium due the Company as a guarantee that the Company will meet its loss and other obligations.

(n) *Fixed Assets.* Fixed assets, with a net book value of \$25.9 million and \$26.5 million as of December 31, 2016 and 2015, respectively, are recorded at amortized cost and are included in other assets. Depreciation and amortization are generally computed on a straight-line basis over the following estimated useful lives:

Leasehold improvements	10 years or term of lease, if shorter
Electronic data processing equipment and furniture	5 years
Personal computers and software	3 years

Depreciation and amortization expense for the years ended December 31, 2016, 2015 and 2014 was \$9.8 million, \$9.6 million and \$9.0 million, respectively.

(o) *Contingent Liabilities.* Amounts are accrued for the resolution of claims that have either been asserted or are deemed probable of assertion if, in the opinion of the Company, it is both probable that a liability has been incurred and the amount of the liability can be reasonably estimated. In many cases it is not possible to determine whether a liability has been incurred or to estimate the ultimate or minimum amount of that liability until years after the contingency arises, in which case no accrual is made until that time. As of December 31, 2016 and 2015, no contingent liabilities have been recorded (see Note 11).

(p) *Recent Accounting Pronouncements.* The Financial Accounting Standards Board ("FASB") is the organization the primary purpose of which is to establish and improve GAAP within the United States. In May 2015, the FASB issued Accounting Standards Update ("ASU") 2015-09 "Financial Services - Insurance - Disclosures about Short-Duration Contracts," which requires additional disclosures in financial statements by insurance

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

entities regarding liabilities for unpaid claims and claim adjustment expenses, and changes in assumptions or methodologies for calculating such liabilities. ASU 2015-09 is effective for the Company for annual periods beginning after December 15, 2016.

In January 2016, the FASB issued ASU 2016-01 “Financial Instruments - Recognition and Measurement of Financial Assets and Financial Liabilities.” ASU 2016-01 generally requires that equity investments (excluding equity method investments) be measured at fair value with changes in fair value recognized in net income. Under existing GAAP, changes in fair value of available-for-sale equity investments are recorded in other comprehensive income. Given the current magnitude of our equity investments, the adoption of ASU 2016-01 could have a significant impact on the periodic net earnings reported in our Consolidated Statement of Earnings, although it likely will not significantly impact our comprehensive income or shareholders’ equity. ASU 2016-01 is effective for the Company for periods beginning after December 15, 2018, with the cumulative effect of the adoption made to the balance sheet as of the date of adoption. Thus, the adoption will result in a reclassification of the related accumulated unrealized appreciation currently included in accumulated other comprehensive income to retained earnings, with no impact on the Company’s shareholders’ equity.

In February 2016, the FASB issued ASU 2016-02 “Leases.” ASU 2016-02 requires a lessee to recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term, along with additional qualitative and quantitative disclosures. ASU 2016-02 is effective for the Company for annual periods beginning after December 15, 2019, with early adoption permitted. The Company is evaluating the effect this standard will have on its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13 “Financial Instruments - Credit Losses,” which provides for the recognition and measurement at the reporting date of all expected credit losses for financial assets that are not accounted for at fair value through net income, including investments in available-for-sale debt securities and loans, premiums receivable and reinsurance recoverable. The updated guidance amends the current other-than-temporary impairment model for available-for-sale debt securities by requiring the recognition of impairments relating to credit losses through an allowance account and limits the amount of credit loss to the difference between a security’s amortized cost basis and its fair value. This guidance also applies a new current expected credit loss model for determining credit-related impairments for financial instruments measured at amortized cost. ASU 2016-13 is effective for the Company for reporting periods beginning after December 15, 2020, with early adoption permitted. Management is currently evaluating the effect that this standard will have on the Company’s consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18 “Statement of Cash Flows (Topic 230): Restricted Cash.” ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts described as restricted cash or restricted cash equivalents. Disclosure will be required to reconcile such total to amounts on the balance sheet and to disclose the nature of the restrictions. ASU 2016-18 is effective for the Company for reporting periods after December 15, 2019, with early adoption permitted. The Company is evaluating the effect this standard will have on its consolidated financial statements.

(q) *Subsequent Events.* The Company has evaluated the significance of events occurring subsequent to December 31, 2016 with respect to disclosing the nature and expected impact of such events as of March 3, 2017, the date these consolidated financial statements were available to be issued.

3. Fair Value Measurements

The Company accounts for a significant portion of its financial instruments at fair value as permitted or required by GAAP.

Fair Value Hierarchy

The assets and liabilities recorded at fair value in the consolidated balance sheets are measured and classified in a three level hierarchy for disclosure purposes based on the observability of inputs available in the marketplace used to measure fair values. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). When the inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value

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measurement in its entirety. Gains and losses for assets and liabilities categorized within the Level 3 table below, therefore, may include changes in fair value that are attributable to both observable inputs (Levels 1 and 2) and unobservable inputs (Level 3). Financial assets and liabilities recorded in the consolidated balance sheets are categorized based on the inputs to the valuation techniques as follows:

Level 1: Level 1 financial instruments are financial assets and liabilities for which the values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Company has the ability to access. Market price data generally is obtained from exchange markets. The Company does not adjust the quoted price for such instruments. The majority of the Company's Level 1 investments are common stocks that are actively traded in a public market and short-term investments and cash equivalents, for which the cost basis approximates fair value.

Level 2: Level 2 financial instruments are financial assets and liabilities for which the values are based on quoted prices in markets that are not active, or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability. Level 2 inputs include the following:

- a) Quoted prices for similar assets or liabilities in active markets;
- b) Quoted prices for identical or similar assets or liabilities in non-active markets;
- c) Pricing models, the inputs for which are observable for substantially the full term of the asset or liability; and
- d) Pricing models, the inputs for which are derived principally from, or corroborated by, observable market data through correlation or other means, for substantially the full term of the asset or liability.

Assets and liabilities measured at fair value on a recurring basis and classified as Level 2 include government, corporate and municipal fixed income securities, which are priced using publicly traded over-the-counter prices and broker-dealer quotes. Observable inputs such as benchmark yields, reported trades, broker-dealer quotes, issuer spreads and bids are available for these investments. Preferred stocks are also classified as Level 2 and are priced using models that utilize underlying stock prices and volatility, credit spreads and SWAP curves. For determining the fair value of swaptions, which are classified as Level 2, the Company utilizes broker-dealer quotes that include observable interest rate yield curves and interest rate volatility. Also included in Level 2 are inactively traded convertible corporate debentures that are valued using a pricing model that includes observable inputs such as credit spreads and discount rates in the calculation.

Level 3: Level 3 financial instruments are financial assets and liabilities for which the values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These measurements include circumstances in which there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement in its entirety. Therefore, these inputs reflect the Company's own assumptions about the methodology and valuation techniques that a market participant would use in pricing the asset or liability.

For the year ended December 31, 2015, the Company transferred \$128.3 million of a Level 3 security to Level 2 after determining that the underlying invested assets of the investee had changed. For the years ended December 31, 2016 and 2014, no securities were transferred into or out of Level 3.

The Company uses valuation techniques to establish the fair value of Level 3 investments. During the years ended December 31, 2016, 2015 and 2014, the Company purchased \$356.1 million, \$238.9 million and \$223.1 million, respectively, of investments that are classified as Level 3. As of December 31, 2016 and 2015, the Company held \$911.7 million and \$939.8 million, respectively, of investments that are classified as Level 3. Level 3 investments include certain limited partnerships, classified as other invested assets on the consolidated balance sheets, based on the net asset values received from the general partners. Generally, these limited partnerships invest in securities that trade in active markets, and as a result, their net asset values reflect their fair values. The Company classifies such investments as Level 3 within the fair value hierarchy when the Company is required to provide the general partner with more than three months' notice prior to liquidation or redemption of the partnership interest. Level 3 investments also include CPI-linked derivative contracts, and certain bonds, preferred stocks and common stocks.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A review of fair value hierarchy classifications is conducted on a quarterly basis. Changes in the observability of valuation inputs may result in a reclassification for certain financial assets or liabilities. Reclassifications impacting Level 3 of the fair value hierarchy are generally reported as transfers in or out of the Level 3 category as of the beginning of the period in which the reclassifications occur. The Company has determined, after carefully considering the impact of recent economic conditions and liquidity in the credit markets on the Company's portfolio, that it should not re-classify any of its investments from Level 1 or Level 2 to Level 3 for the years ended December 31, 2016, 2015 or 2014. For the year ended December 31, 2016, \$0.9 million common stock – held for trading and fair value option was transferred from Level 1 to Level 2. There were no transfers of securities between Level 1 and Level 2 during the years ended December 31, 2015 and 2014.

The Company is responsible for determining the fair value of its investment portfolio by utilizing market driven fair value measurements obtained from active markets, where available, by considering other observable and unobservable inputs and by employing valuation techniques that make use of current market data. For the majority of the Company's investment portfolio, the Company uses quoted prices and other information from independent pricing sources to determine fair values.

The following tables present the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of December 31, 2016 and 2015 (in thousands):

	Fair Value Measurements as of December 31, 2016			
	Reported Fair Value	Level 1	Level 2	Level 3
Fixed income securities, available for sale:				
United States government, government agencies and authorities	\$ 7,930	\$ —	\$ 7,930	\$ —
States, municipalities and political subdivisions	891,125	—	891,125	—
Foreign governments	8,901	—	8,901	—
Corporate	50,708	1,629	49,079	—
Total fixed income securities, available for sale	958,664	1,629	957,035	—
Fixed income securities, held for trading:				
United States government, government agencies and authorities	189,672	—	189,672	—
States, municipalities and political subdivisions	960,243	—	960,243	—
Foreign governments	416,591	—	416,591	—
Corporate	328,900	—	107,702	221,198
Total fixed income securities, held for trading ..	1,895,406	—	1,674,208	221,198
Common stocks, available for sale	154,457	150,716	3,741	—
Common stocks, held for trading and fair value options	1,033,399	633,318	282,300	117,781
Short-term investments, held for trading.....	1,742,357	1,742,357	—	—
Cash equivalents.....	490,443	490,443	—	—
Derivatives	82,641	—	69,027	13,614
Other investments.....	571,389	—	12,257	559,132
Total assets measured at fair value	<u>\$ 6,928,756</u>	<u>\$ 3,018,463</u>	<u>\$ 2,998,568</u>	<u>\$ 911,725</u>
Derivative liabilities	<u>\$ 79,540</u>	<u>\$ —</u>	<u>\$ 79,540</u>	<u>\$ —</u>
Total liabilities measured at fair value.....	<u>\$ 79,540</u>	<u>\$ —</u>	<u>\$ 79,540</u>	<u>\$ —</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	Fair Value Measurements as of December 31, 2015			
	Reported Fair Value	Level 1	Level 2	Level 3
Fixed income securities, available for sale:				
United States government, government agencies and authorities	\$ 55,710	\$ —	\$ 55,710	\$ —
States, municipalities and political subdivisions	1,415,628	—	1,415,628	—
Foreign governments	9,090	—	9,090	—
Corporate	58,965	2,212	56,753	—
Total fixed income securities, available for sale	1,539,393	2,212	1,537,181	—
Fixed income securities, held for trading:				
United States government, government agencies and authorities	799,270	—	799,270	—
States, municipalities and political subdivisions	1,200,819	—	1,200,819	—
Foreign governments	248,127	—	248,127	—
Corporate	344,353	—	86,042	258,311
Total fixed income securities, held for trading ..	2,592,569	—	2,334,258	258,311
Convertible preferred stocks, held for trading	54,155	—	54,155	—
Common stocks, available for sale	191,443	187,980	3,463	—
Common stocks, held for trading and fair value options	1,307,077	661,740	558,152	87,185
Short-term investments, held for trading.....	708,749	681,905	26,844	—
Cash equivalents	254,337	254,337	—	—
Derivatives	167,425	—	106,400	61,025
Other investments	544,342	—	11,108	533,234
Total assets measured at fair value	\$ 7,359,490	\$ 1,788,174	\$ 4,631,561	\$ 939,755
Derivative liabilities	\$ 13,011	\$ —	\$ 13,011	\$ —
Total liabilities measured at fair value	\$ 13,011	\$ —	\$ 13,011	\$ —

The Company had cash collateral posted on its behalf by counterparties to derivative transactions in the amounts of \$4.7 million and \$18.6 million as of December 31, 2016 and 2015, respectively. The Company is not party to any counterparty netting transactions.

The following table provides a summary of changes in the fair value of Level 3 financial assets and liabilities for the years ended December 31, 2016 and 2015 (in thousands):

	Fixed Income Securities	Other Invested Assets	Equity Securities
Balance, January 1, 2015	\$ 271,322	\$ 471,916	\$ 216,628
Change in value related to securities sold	10	11,033	1,496
Change in value related to securities held	(46,483)	19,282	(12,256)
Purchases / advances	50,791	146,284	41,873
Settlements / paydowns	(17,329)	(54,256)	(32,248)
Transfers from Level 3 to Level 2	—	—	(128,308)
Balance, December 31, 2015	258,311	594,259	87,185
Change in value related to securities sold	(13,788)	16,806	(782)
Change in value related to securities held	(12,361)	255	11,156
Purchases / advances	211,832	79,046	65,212
Settlements / paydowns	(222,796)	(117,620)	(44,990)
Balance, December 31, 2016	\$ 221,198	\$ 572,746	\$ 117,781

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following tables present changes in value included in net income related to Level 3 assets for the years ended December 31, 2016, 2015, and 2014 (in thousands):

	Net Investment Income	Net Realized Capital Gains (Losses)	Currency Translation	Total
Year ended December 31, 2016				
Fixed income securities	\$ (2,842)	\$ (20,691)	\$ (2,616)	\$ (26,149)
Other invested assets	—	21,660	(4,599)	17,061
Equity securities.....	—	13,417	(3,043)	10,374
Total changes in value included in net income	<u>\$ (2,842)</u>	<u>\$ 14,386</u>	<u>\$ (10,258)</u>	<u>\$ 1,286</u>
Year ended December 31, 2015				
Fixed income securities	\$ (2,297)	\$ (42,662)	\$ (1,514)	\$ (46,473)
Other invested assets	—	33,349	(3,034)	30,315
Equity securities.....	—	(7,416)	(3,344)	(10,760)
Total changes in value included in net income	<u>\$ (2,297)</u>	<u>\$ (16,729)</u>	<u>\$ (7,892)</u>	<u>\$ (26,918)</u>
Year ended December 31, 2014				
Fixed income securities	\$ 89	\$ 62,237	\$ (1,285)	\$ 61,041
Other invested assets	—	(908)	(4,736)	(5,644)
Equity securities.....	—	16,982	(3,102)	13,880
Total changes in value included in net income	<u>\$ 89</u>	<u>\$ 78,311</u>	<u>\$ (9,123)</u>	<u>\$ 69,277</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table provides information on the valuation techniques, significant unobservable inputs and ranges for each major category of Level 3 assets measured at fair value on a recurring basis at December 31, 2016 and 2015 (in thousands):

Valuation Technique/Asset Type	As of December 31,		Significant Unobservable Inputs	Range	
	2016	2015		2016	2015
<u>Market Approach</u>					
Fixed income securities, held for trading	\$ 221,198	\$ 258,311	Risk premium for credit risk	6.0%-9.1%	6.0%-8.4%
CPI-linked derivatives (1)	13,614	61,025	Broker quotes		
Total valued using market approach	<u>234,812</u>	<u>319,336</u>			
<u>Income Approach</u>					
Common stock, held for trading	<u>14,652</u>	<u>11,551</u>	EV/EBITDA multiple	7.5x	7.5x
<u>Net Asset Value</u>					
Common stock, held for trading	63,845	42,117	Price/earning multiple	10x	10x
Partnerships, at fair value (2)	509,063	533,234	Time lag in receiving distributions		
Total valued using net asset value approach	<u>572,908</u>	<u>575,351</u>			
<u>Market Price to Book Value</u>					
Common stocks, fair value option (3)	39,284	33,517	Time lag in receiving book value of comparable companies		
<u>Par Value</u>					
Other investments	<u>50,069</u>	—	Transaction price		
Total - Level 3	<u>\$ 911,725</u>	<u>\$ 939,755</u>			

- (1) Valued using broker-dealer quotes that management has determined use market observable inputs except for the inflation volatility input which is not market observable.
- (2) Includes interest in thirteen and twelve limited partnerships, as of December 31, 2016 and 2015, respectively, that are carried as held for trading securities.
- (3) The Company evaluates observable price-to-book multiples of peer companies and applies such to the most recently available book value per share.

Fair Value Option

The fair value option (“FVO”) allows companies to irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and liabilities. Changes in the fair value of assets and liabilities for which the election is made are recognized in net income as they occur. The FVO election is permitted on an instrument-by-instrument basis at initial recognition of an asset or liability or upon the occurrence of an event that gives rise to a new basis of accounting for that instrument.

The Company elected the FVO for its investment in Advent Capital (Holdings) PLC (“Advent”) as, at the time of the election, Advent was publicly traded and its trading price was believed to be a better indicator of its value than an amount computed under the equity method. Fairfax and its subsidiaries currently own 100% of Advent’s common stock, of which the Company holds 17.0%. To determine the fair value of Advent, the Company evaluates observable price-to-book multiples of peer companies and applies such to Advent’s most recently available book value per share. As of December 31, 2016 and 2015, the Company’s interest in Advent was recorded at fair value of \$39.3 million and \$33.5 million, respectively, in common stocks held for trading and fair value options, with related changes in fair value recognized as a realized investment gain or loss in the period in which they occurred. The change in Advent’s fair value resulted in the recognition of a realized investment gain of \$5.8 million for the year ended December 31, 2016, a realized investment loss of \$8.9 million for the year ended December 31, 2015 and a realized investment gain of \$10.9 million for the year ended December 31, 2014. The value of the

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Company's interest in Advent as of December 31, 2016, calculated in accordance with the equity method of accounting, would have been \$31.4 million.

The Company owns Class C, G, H, J and Q common shares of HWIC Asia Fund ("HWIC Asia"), which is 100% owned by Fairfax and of which the Company owns 30.1% as of December 31, 2016. At the time of the purchase of each class of shares, the Company elected the FVO for these investments, as HWIC Asia is a multi-class investment company that reports its investments at fair value and provides a Net Asset Value on a monthly basis.

The carrying value of the Company's investment in the various HWIC Asia common share issues as of December 31, 2016 and 2015, which is included in common stocks held for trading and fair value option on the balance sheet, and the changes in fair value for each issue for the year then ended, are summarized below (in thousands):

	HWIC Asia Class C	HWIC Asia Class E	HWIC Asia Class G	HWIC Asia Class H	HWIC Asia Class J	HWIC Asia Class Q	Total
Fair value as of December 31, 2014	\$ 46,506	\$ 326,599	\$ 41,020	\$ 128,308	\$ —	\$ —	\$ 542,433
Purchases/(sales)	—	(23,230)	15,000	8	41,872	—	33,650
Change in fair value	(6,993)	(14,201)	941	(2,857)	683	—	(22,427)
Currency translation adjustment	—	(233)	—	15	(438)	—	(656)
Fair value as of December 31, 2015	39,513	288,935	56,961	125,474	42,117	—	553,000
Purchases/(sales)	—	(289,341)	17,000	—	—	20,212	(252,129)
Change in fair value	(4,113)	406	2,112	(12,937)	4,185	366	(9,981)
Currency translation adjustment	—	—	—	(288)	(2,125)	(909)	(3,322)
Fair value as of December 31, 2016	\$ 35,400	\$ —	\$ 76,073	\$ 112,249	\$ 44,177	\$ 19,669	\$ 287,568

HWIC Asia's fair value increased by \$21.8 million for the year ended December 31, 2014.

The Company did not elect the FVO for its other affiliated investments, as these affiliated investments were ultimately 100% owned by Fairfax and its subsidiaries, and fair values were deemed to be not readily obtainable.

As of December 31, 2016 and 2015, respectively, the Company has not elected the FVO for any of its liabilities.

4. Investments and Cash

A summary of the Company's available for sale investment portfolio as of December 31, 2016 and 2015, is as follows (in thousands):

	Cost or Amortized Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
2016				
Fixed income securities:				
United States government, government agencies and authorities	\$ 7,055	\$ 923	\$ 48	\$ 7,930
States, municipalities and political subdivisions	792,179	99,266	320	891,125
Foreign governments	7,466	1,435	—	8,901
Corporate	48,317	2,391	—	50,708
Total fixed income securities	855,017	104,015	368	958,664
Common stocks	135,896	25,463	6,902	154,457
Total	\$ 990,913	\$ 129,478	\$ 7,270	\$ 1,113,121

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

<u>2015</u>	<u>Cost or Amortized Cost</u>	<u>Gross Unrealized Appreciation</u>	<u>Gross Unrealized Depreciation</u>	<u>Fair Value</u>
Fixed income securities:				
United States government, government agencies and authorities	\$ 43,036	\$ 12,674	\$ —	\$ 55,710
States, municipalities and political subdivisions	1,233,198	182,564	134	1,415,628
Foreign governments	7,349	1,741	—	9,090
Corporate	57,496	1,469	—	58,965
Total fixed income securities	1,341,079	198,448	134	1,539,393
Common stocks	150,903	45,866	5,326	191,443
Total	<u>\$ 1,491,982</u>	<u>\$ 244,314</u>	<u>\$ 5,460</u>	<u>\$ 1,730,836</u>

Common stocks accounted for under the equity method of accounting were carried at \$398.0 million and \$254.7 million as of December 31, 2016 and 2015, respectively. Common stocks at equity had gross unrealized appreciation of \$8.5 million and \$0.4 million and gross unrealized depreciation of \$5.6 million and \$5.9 million as of December 31, 2016 and 2015, respectively. Other invested assets were carried at \$843.6 million and \$903.7 million as of December 31, 2016 and 2015, respectively, reflecting no gross unrealized appreciation or depreciation.

A summary of the Company's held for trading and fair value option portfolios as of December 31, 2016 and 2015 is as follows (in thousands):

	<u>2016 Fair Value</u>	<u>2015 Fair Value</u>
Fixed income securities:		
United States government, government agencies and authorities	\$ 189,672	\$ 799,270
States, municipalities and political subdivisions	960,243	1,200,819
Foreign governments	416,591	248,127
Corporate	328,900	344,353
Total fixed income securities	1,895,406	2,592,569
Preferred stocks	—	54,155
Common stocks	1,033,399	1,307,077
Short-term investments	1,742,357	708,749
Cash and cash equivalents	604,861	460,267
Cash collateral for borrowed securities	218,660	200,717
Total	<u>\$ 5,494,683</u>	<u>\$ 5,323,534</u>

(a) Fixed Income Maturity Schedule

The amortized cost and fair value of fixed income securities as of December 31, 2016, by contractual maturity, are shown below (in thousands):

	<u>At December 31, 2016</u>					
	<u>Available for Sale</u>			<u>Held for Trading</u>		
	<u>Cost or Amortized Cost</u>	<u>Fair Value</u>	<u>% of Total Fair Value</u>	<u>Cost or Amortized Cost</u>	<u>Fair Value</u>	<u>% of Total Fair Value</u>
Due in one year or less	\$ 11,814	\$ 11,814	1.2%	\$ 144,331	\$ 137,089	7.2%
Due after one year through five years	25,008	25,018	2.6	360,228	320,508	16.9
Due after five years through ten years	41,604	46,186	4.8	36,931	41,701	2.2
Due after ten years	776,591	875,646	91.4	1,421,519	1,396,108	73.7
Total fixed income securities	<u>\$ 855,017</u>	<u>\$ 958,664</u>	<u>100.0%</u>	<u>\$ 1,963,009</u>	<u>\$ 1,895,406</u>	<u>100.0%</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Actual maturities may differ from the contractual maturities shown in the table above due to the existence of call or put options. In the case of securities containing call options, the actual maturity will be the same as the contractual maturity if the issuer elects not to exercise its call option. Total securities subject to call options represent approximately 42.2% of the total fair value. In the case of securities containing put options, the actual maturity will be the same as the contractual maturity if the Company elects not to exercise its put option. Total securities containing a put option represent approximately 0.8% of the total fair value.

(b) Net Investment Income and Realized Investment Gains (Losses)

The following table sets forth the sources and components of net investment income for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Interest on fixed income securities	\$ 189,520	\$ 176,320	\$ 194,570
Dividends on preferred stocks	6,112	7,398	14,229
Dividends on common stocks	25,954	40,258	17,350
Net income of common stocks, at equity	22,890	9,940	27,287
Interest on cash and short-term investments	6,049	4,048	4,862
Net income from other invested assets	24,489	51,806	35,664
Gross investment income	<u>275,014</u>	<u>289,770</u>	<u>293,962</u>
Less: investment expenses	59,941	72,610	77,111
Net investment income	<u>\$ 215,073</u>	<u>\$ 217,160</u>	<u>\$ 216,851</u>

The following table summarizes the Company's net realized investment gains and losses for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Available for sale:			
From sales	\$ 58,547	\$ 96,045	\$ 62,258
Other-than-temporary impairments	<u>(16,227)</u>	<u>(65,120)</u>	<u>(103,887)</u>
Total available for sale	<u>42,320</u>	<u>30,925</u>	<u>(41,629)</u>
Held for trading:			
From sales and settlements	(264,734)	236,280	140,445
From mark to market adjustments	<u>20,499</u>	<u>(383,713)</u>	<u>258,306</u>
Total held for trading	<u>(244,235)</u>	<u>(147,433)</u>	<u>398,751</u>
Total net realized investment (losses) gains	<u>\$ (201,915)</u>	<u>\$ (116,508)</u>	<u>\$ 357,122</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table sets forth the components of net realized investment gains and losses on the Company's available for sale securities for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Fixed income securities:			
Realized investment gains.....	\$ 68,081	\$ 173,615	\$ 26,881
Realized investment losses	(9,905)	(2,931)	(12,954)
Other-than-temporary impairments.....	—	(1,052)	(1,704)
Net realized investment gains	<u>58,176</u>	<u>169,632</u>	<u>12,223</u>
Preferred stock:			
Realized investment gains.....	—	—	2,075
Equity securities:			
Realized investment gains.....	724	2,722	46,656
Realized investment losses	(353)	(57,501)	(400)
Other-than-temporary impairments.....	(16,227)	(64,068)	(102,183)
Net realized investment losses	<u>(15,856)</u>	<u>(118,847)</u>	<u>(55,927)</u>
Common stocks, at equity:			
Realized investment losses	—	(19,860)	—
Total available for sale securities:			
Realized investment gains.....	68,805	176,337	75,612
Realized investment losses	(10,258)	(80,292)	(13,354)
Other-than-temporary impairments.....	(16,227)	(65,120)	(103,887)
Net realized investment gains (losses)	<u>\$ 42,320</u>	<u>\$ 30,925</u>	<u>\$ (41,629)</u>

For those fixed income securities that were determined to be other-than-temporarily impaired, the Company determined that such impairments were related to credit, requiring the recognition of an impairment charge to income, and not related to other factors (e.g., interest rates and market conditions) which would have required charges to other comprehensive income.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The net realized investment gains or losses on disposal of held for trading securities in the table below represent the total gains or losses from the purchase dates of the investments and have been reported in net realized investment gains in the consolidated statements of operations. The change in fair value presented below consists of two components: (i) the reversal of the gain or loss recognized in previous years on securities sold and (ii) the change in fair value resulting from mark-to-market adjustments on contracts still outstanding. The following table sets forth the total net realized investment gains and losses on held for trading securities for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Fixed income securities:			
Net realized investment gains on disposal.....	\$ 75,991	\$ 47,669	\$ 121,531
Change in fair value.....	<u>47,776</u>	<u>(234,665)</u>	<u>222,401</u>
Net realized investment gains (losses)	<u>123,767</u>	<u>(186,996)</u>	<u>343,932</u>
Preferred stock:			
Net realized investment (losses) gains on disposal.....	(41,989)	33,816	(32,063)
Change in fair value.....	<u>34,719</u>	<u>(45,223)</u>	<u>(21,498)</u>
Net realized investment losses	<u>(7,270)</u>	<u>(11,407)</u>	<u>(53,561)</u>
Equity securities:			
Net realized investment (losses) gains on disposal.....	(20,756)	28,637	117,148
Change in fair value.....	<u>(15,490)</u>	<u>(221,497)</u>	<u>(58,060)</u>
Net realized investment (losses) gains	<u>(36,246)</u>	<u>(192,860)</u>	<u>59,088</u>
Derivative securities:			
Net realized investment (losses) gains on disposal/ settlement	(327,402)	142,350	(53,249)
Change in fair value.....	<u>(79,779)</u>	<u>87,794</u>	<u>94,188</u>
Net realized investment (losses) gains	<u>(407,181)</u>	<u>230,144</u>	<u>40,939</u>
Other securities:			
Net realized investment gains (losses) on disposal.....	49,422	(16,192)	(12,922)
Change in fair value.....	<u>33,273</u>	<u>29,878</u>	<u>21,275</u>
Net realized investment gains	<u>82,695</u>	<u>13,686</u>	<u>8,353</u>
Total held for trading securities:			
Net realized investment (losses) gains on disposal.....	(264,734)	236,280	140,445
Change in fair value.....	<u>20,499</u>	<u>(383,713)</u>	<u>258,306</u>
Net realized investment (losses) gains	<u>\$ (244,235)</u>	<u>\$ (147,433)</u>	<u>\$ 398,751</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(c) *Unrealized (Depreciation) Appreciation*

The following table sets forth the changes in net unrealized appreciation (depreciation) of investments, and the related tax effect, reflected in accumulated other comprehensive income for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Fixed income securities	\$ (88,131)	\$ (210,885)	\$ 177,565
Preferred stock	—	—	(2,049)
Equity securities.....	(13,578)	(115,097)	56,113
Other.....	<u>(244)</u>	<u>270</u>	<u>—</u>
(Decrease) increase in unrealized net appreciation of investments	(101,953)	(325,712)	231,629
Deferred income tax benefit (provision).....	<u>35,664</u>	<u>113,755</u>	<u>(80,914)</u>
Change in net unrealized (depreciation) appreciation of investments included in other comprehensive (loss) income.....	<u>\$ (66,289)</u>	<u>\$ (211,957)</u>	<u>\$ 150,715</u>

On a quarterly basis, the Company reviews its investment portfolio classified as available for sale for declines in value and specifically evaluates securities with fair values that have declined to less than 80% of their cost or amortized cost at the time of review. Declines in the fair value of investments that are determined to be temporary are recorded as unrealized depreciation, net of tax, in accumulated other comprehensive income. If the Company determines that a decline relating to credit issues is “other-than-temporary,” the cost or amortized cost of the investment will be written down to the fair value, and a realized loss will be recorded in the Company’s consolidated statements of operations. If the Company determines that a decline related to other factors (e.g., interest rates or market conditions) is “other-than-temporary,” the cost or amortized cost of the investment will be written down to the fair value within other comprehensive income.

In assessing the value of the Company’s debt and equity securities that are classified as available for sale and possible impairments of such securities, the Company reviews (i) the issuer’s current financial position and disclosures related thereto, (ii) general and specific market and industry developments, (iii) the timely payment by the issuer of its principal, interest and other obligations, (iv) the outlook and expected financial performance of the issuer, (v) current and historical valuation parameters for the issuer and similar companies, (vi) relevant forecasts, analyses and recommendations by research analysts, rating agencies and investment advisors, and (vii) other information the Company may consider relevant. Generally, a change in the market or interest rate environment would not, of itself, result in an impairment of an investment. In addition, the Company considers its ability and intent to hold the security to recovery when evaluating possible impairments.

The facts and circumstances involved in making a decision regarding an other-than-temporary impairment are those that exist at that time. Should the facts and circumstances change such that an other-than-temporary impairment is considered appropriate, the Company will recognize the impairment by reducing the cost, amortized cost or carrying value of the investment to its fair value, and recording the loss in its consolidated statements of operations. Upon the disposition of a security where an other-than-temporary impairment has been taken, the Company will record a gain or loss based on the adjusted cost or carrying value of the investment.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table reflects the fair value and gross unrealized depreciation of the Company's fixed income securities and common stocks, at fair value classified as available for sale, aggregated by investment category for individual securities that have been in a continuous unrealized depreciation position for less than 12 months, as of December 31, 2016 and 2015 (in thousands):

	Fair Value	Gross Unrealized Depreciation	Number of Securities
December 31, 2016			
Fixed income securities:			
United States government, government agencies and authorities	\$ 975	\$ 48	1
States, municipalities and political subdivisions	12,535	320	5
Total fixed income securities	13,510	368	6
Common stocks, at fair value	80,296	6,902	2
Total temporarily impaired securities	\$ 93,806	\$ 7,270	8

	Fair Value	Gross Unrealized Depreciation	Number of Securities
December 31, 2015			
Fixed income securities:			
States, municipalities and political subdivisions	\$ 2,895	\$ 134	1
Total fixed income securities	2,895	134	1
Common stocks, at fair value	8,179	5,326	1
Total temporarily impaired securities	\$ 11,074	\$ 5,460	2

The Company did not own any fixed income or common stocks, at fair value classified as available for sale, that have been in a continuous unrealized loss position for more than 12 months as of December 31, 2016 or 2015.

The Company believes the gross unrealized depreciation for securities classified as available for sale is temporary in nature and has not recorded a realized investment loss related to these securities. Given the size of the Company's investment portfolio and capital position, the Company believes it is likely that it will not be required to sell or liquidate these securities before the fair value recovers the gross unrealized depreciation.

(d) Common Stocks, at Equity

The following table sets forth the components of common stocks, at equity, as of December 31, 2016 and 2015 (in thousands):

	Carrying Value		Goodwill and Other included in Carrying Value		Quoted Market Value		Relative Economic Ownership
	2016	2015	2016	2015	2016	2015	2016
Cara Operations Limited	\$ 161,594	\$ 119,425	\$ 106,306	\$ 102,104	\$ 152,421	\$ 158,397	13.7%
Fairfax India Holdings Corp.	90,907	79,587	—	—	100,476	85,850	8.3%
Apple Bidco Limited	51,608	—	(1,690)	—	n/a	n/a	14.8%
Zenith National Insurance Corp.	39,859	44,888	3,928	3,928	n/a	n/a	6.1%
Boat Rocker Media Inc.	24,051	10,798	14,877	8,975	n/a	n/a	27.3%
Other	30,000	27	—	—	n/a	n/a	0.0%
Total common stocks, at equity	\$ 398,019	\$ 254,725	\$ 123,421	\$ 115,007			

Zenith is a wholly-owned subsidiary of Fairfax, while Fairfax is the controlling or largest shareholder of Cara (38.9%), Fairfax India (29.4%), Apple Bidco (54.2%) and Boat Rocker (58.2%).

During 2015, the Company exchanged its interest in Fairfax Asia with a note receivable from an affiliate, and later exchanged this note (plus warrants and preferred shares of Cara) for common stock of Cara.

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(e) *Other Invested Assets*

The following table shows the components of other invested assets as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Investment funds and partnerships, at fair value.....	\$ 509,065	\$ 533,234
Investment funds and partnerships, at equity	182,794	185,211
Derivatives, at fair value	82,641	167,425
Affiliate loans	50,069	—
Benefit plan funds, at fair value.....	12,257	11,108
Other.....	6,730	6,730
Total other invested assets	<u>\$ 843,556</u>	<u>\$ 903,708</u>

The Company's investment funds and partnership investments may be subject to restrictions on redemptions or sales, which are determined by the governing documents thereof, and may limit the Company's ability to liquidate these investments in the short term. Due to a time lag in reporting by a majority of investment fund and partnership fund managers, valuations for these investments are recorded by the Company on a one month or one quarter lag. For the years ended December 31, 2016, 2015 and 2014, the Company recognized net investment income of \$20.0 million, \$46.0 million and \$17.5 million, respectively, from its investment funds and partnership investments. For the years ended December 31, 2016, 2015 and 2014, the Company recognized net realized investment gains of \$67.7 million, \$24.8 million and \$34.8 million, respectively, from its investment funds and partnerships that are held as trading securities. With respect to the Company's \$691.9 million in investments in investment funds and partnerships, the Company has commitments that may require additional funding of up to \$118.7 million.

(f) *Derivative Investments*

The Company has utilized CPI-linked derivative contracts, total return swaps, forward currency contracts, U.S. Treasury bond forward contracts and various other contracts, to manage against adverse changes in the values of assets and liabilities. These products are typically not directly linked to specific assets or liabilities on the consolidated balance sheets or a forecasted transaction. The following tables set forth the Company's derivative positions, which are included in other invested assets or other liabilities in the consolidated balance sheets, as of December 31, 2016 and 2015, respectively (in thousands):

<u>As of December 31, 2016</u>	<u>Exposure/ Notional Amount</u>	<u>Cost</u>	<u>Fair Value Asset</u>	<u>Fair Value Liability</u>
CPI-linked derivative contracts.....	\$ 32,902,540	\$ 229,779	\$ 13,616	\$ —
U.S. Treasury bond forward contracts.....	913,950	—	—	13,866
Forward currency contracts.....	729,430	—	62,311	53,469
Short total return swaps.....	117,819	—	1,010	9,254
Long total return swaps.....	78,729	—	5,704	2,951
Other.....	—	6,623	—	—
Total		<u>\$ 236,402</u>	<u>\$ 82,641</u>	<u>\$ 79,540</u>

<u>As of December 31, 2015</u>	<u>Exposure/ Notional Amount</u>	<u>Cost</u>	<u>Fair Value Asset</u>	<u>Fair Value Liability</u>
CPI-linked derivative contracts.....	\$ 33,793,251	\$ 228,494	\$ 61,025	\$ —
Short total return swaps.....	1,924,566	—	73,769	1,654
Forward currency contracts.....	967,195	—	31,630	7,889
Long total return swaps.....	62,027	—	940	3,469
Other.....	—	83,250	61	—
Total		<u>\$ 311,744</u>	<u>\$ 167,425</u>	<u>\$ 13,012</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

In the normal course of affecting its economic hedging strategy with respect to equity risk, the Company expects that there may be periods where the notional value of the derivative instruments may exceed or be less than the exposure item. This situation may arise when management compensates for imperfect correlations between the exposed item and the derivative instruments used to manage change in the value of the item, due to the timing of opportunities related to the Company's ability to exit and enter markets at attractive prices or when management desires to only partially manage an exposure.

The Company held long position common stock total return swaps, with a total notional value of \$78.7 million and \$62.0 million as of December 31, 2016 and 2015, respectively, as replications of investments in publicly-listed common stocks. The common stock total return swaps, which are carried at fair value, are recorded in other invested assets or other liabilities based on the positive or negative value of the underlying contracts as of the financial statement date. Changes in the fair value of common stock total return swaps are recorded as realized investment gains or losses in the consolidated statements of operations in the period in which they occur.

As of December 31, 2016 and 2015, the Company held short position common stock total return swaps with a notional value of \$117.8 million and \$176.7 million, respectively. The common stock total return swaps are recorded at fair value in other invested assets or other liabilities based on the positive or negative value of the underlying contracts as of the financial statement date. Changes in the fair value of the swaps are recorded as realized investment gains or losses in the consolidated statements of operations in the period in which they occur.

Due to volatility in the equity markets, the Company had entered into U.S. equity index total return swap contracts to protect against a potential significant market downturn. As a result of fundamental changes in the U.S. in the fourth quarter of 2016 that may bolster economic growth and business development in the future, the Company closed all of its U.S. equity index total return swap contracts. The aggregate notional value of these contracts was \$1.7 billion as of December 31, 2015. The equity index total return swaps were recorded at fair value in other invested assets or other liabilities based on the positive or negative value of the underlying contracts as of financial statement date, with the related changes in the fair values recorded as realized investment gains or losses in the consolidated statements of operations in the period in which they occurred.

The following tables summarize the effect of the derivative instruments used to manage adverse changes in equity investment values and related items on the Company's financial position, results of operations and cash flows as of and for the years ended December 31, 2016 and 2015 (in thousands):

	Exposure (a)	Carrying Value	Effect on Pre-tax:			
			Other Comprehensive Income	Net Investment Income / Realized Gains (Losses)	Net Equity Impact	Net Cash Flow from Disposals
As of and for the year ended December 31, 2016						
Equity risk exposures:						
Common stocks, at fair value.....	\$ 1,119,079	\$1,119,079	\$ (21,201)	\$ (48,523)	\$ (69,724)	\$ (20,737)
Preferred stocks.....	—	—	—	(7,270)	(7,270)	(41,989)
Bonds – convertible.....	233,790	233,790	—	(18,150)	(18,150)	10,589
Partnerships.....	670,467	670,467	—	86,621	86,621	34,481
Total return swaps – long.....	81,482	2,753	—	6,956	6,956	1,674
Total equity exposure.....	<u>\$ 2,104,818</u>	<u>\$2,026,089</u>	<u>(21,201)</u>	<u>19,634</u>	<u>(1,567)</u>	<u>(15,982)</u>
Hedging instruments included in other invested assets:						
Total return swaps - short.....	\$ 126,063	\$ (8,244)	—	(388,988)	(388,988)	(308,629)
Total equity hedging instruments.....	<u>\$ 126,063</u>	<u>\$ (8,244)</u>	<u>—</u>	<u>(388,988)</u>	<u>(388,988)</u>	<u>(308,629)</u>
Net equity impact.....			<u>\$ (21,201)</u>	<u>\$ (369,354)</u>	<u>\$ (390,555)</u>	<u>\$ (324,611)</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	Exposure (a)	Carrying Value	Effect on Pre-tax:			
			Other Comprehensive Income	Net Investment Income / Realized Gains (Losses)	Net Equity Impact	Net Cash Flow from Disposals
As of and for the year ended December 31, 2015						
Equity risk exposures:						
Common stocks, at fair value	\$ 1,038,529	\$1,038,529	\$ (125,494)	\$ (285,778)	\$ (411,272)	\$ (32,271)
Preferred stocks	54,155	54,155	—	(13,649)	(13,649)	33,816
Bonds – convertible	268,055	268,055	—	(45,152)	(45,152)	—
Partnerships	698,653	698,653	—	67,934	67,934	2,511
Total return swaps – long	59,498	(2,529)	—	(16,915)	(16,915)	(22,473)
Other	—	—	—	6,014	6,014	6,460
Total equity exposure	<u>\$ 2,118,890</u>	<u>\$2,056,863</u>	<u>(125,494)</u>	<u>(287,546)</u>	<u>(413,040)</u>	<u>(11,957)</u>
Hedging instruments included in other invested assets:						
Total return swaps - short	\$ 1,852,451	\$ 72,116	—	162,013	162,013	71,894
Total equity hedging instruments	<u>\$ 1,852,451</u>	<u>\$ 72,116</u>	<u>—</u>	<u>162,013</u>	<u>162,013</u>	<u>71,894</u>
Net equity impact			<u>\$ (125,494)</u>	<u>\$ (125,533)</u>	<u>\$ (251,027)</u>	<u>\$ 59,937</u>

(a) The exposure for hedging instruments represents the notional value stated in the underlying contracts plus or minus the current carrying value of the derivative investment.

As a result of fundamental changes to the macroeconomic outlook for the U.S. during the fourth quarter of 2016 and the ensuing potential for a significant increase in market interest rates, the Company reduced its exposure to interest rate risk by selling certain U.S. state and municipal bonds and long dated U.S. Treasury bonds. To further reduce its exposure to interest rate risk (specifically exposure to U.S. state and municipal bonds and any remaining long dated U.S. Treasury bonds held in its fixed income portfolio), the company entered into forward contracts to sell long dated U.S. Treasury bonds. These contracts have an average term to maturity of less than one year and may be renewed at market rates. The U.S. Treasury bond forward contracts are recorded at fair value in other invested assets or in other liabilities based on the positive or negative value of the underlying contracts as of the financial statement date, with the related changes in fair value recognized as realized investment gains or losses in the consolidated statements of operations in the period in which they occur.

As an economic hedge against the potential adverse impact on the Company of decreasing price levels in the economy, the Company has purchased derivative contracts referenced to consumer price indices (“CPI”) in various geographic regions in which the Company operates. These contracts had a remaining average life of 5.1 years and 6.1 years as of December 31, 2016 and 2015, respectively. As the remaining life of a contract declines, the fair value of the contract (excluding the impact of CPI changes) will generally decline. The initial premium paid for the contracts is recorded as a derivative asset and subsequently adjusted for changes in the unrealized fair value of the contracts at each balance sheet date. Changes in the unrealized fair value of the contracts are recorded as realized gains or losses on investments in the Company’s consolidated statements of operations with a corresponding adjustment to the carrying value of the derivative asset. In the event of a sale, expiration or early settlement of one of the Company’s CPI-linked derivative contracts, the Company would receive the fair value of that contract on the date of the transaction. The Company’s maximum potential cash loss is limited to the premiums paid to enter into the derivative contracts.

The Company has entered into forward currency contracts to manage its foreign currency exchange rate risk on a macro basis. Under a forward currency contract, the Company and the counterparty are obligated to purchase or sell an underlying currency at a specified price and time. Forward currency contracts are recorded at fair value in other invested assets or other liabilities based on the positive or negative value of the underlying contracts as of the financial statement date, with the related changes in fair value recognized as realized investment gains or losses in the consolidated statements of operations in the period in which they occur.

Pursuant to the agreements governing various derivative contracts, the fair value of collateral deposited by the Company with the contracts’ counterparties totaled \$46.8 million and \$118.3 million as of December 31, 2016 and 2015, respectively, while the fair value of collateral deposited by various counterparties for the benefit of the Company was \$11.6 million and \$91.6 million as of December 31, 2016 and 2015, respectively.

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Counterparties to the derivative instruments expose the Company to credit risk in the event of non-performance. The Company believes this risk is low, given the diversification among various highly rated counterparties. The credit risk exposure is reflected in the fair value of the derivative instruments.

The net realized investment gains or losses on disposal of derivatives in the table below represent the total gains or losses for the years ended December 31, 2016, 2015 and 2014 from the purchase dates of the investments and have been reported in net realized investment gains in the consolidated statements of operations; the change in fair value presented consists of two components: (i) the reversal of the gain or loss recognized in previous years on securities sold and (ii) the change in fair value resulting from mark-to-market adjustments on contracts still outstanding (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
CPI-linked derivative contracts:			
Net realized investment losses on disposal	\$ —	\$ —	\$ (33,116)
Change in fair value.....	<u>(48,695)</u>	<u>(17)</u>	<u>6,748</u>
Net realized investment losses	<u>(48,695)</u>	<u>(17)</u>	<u>(26,368)</u>
U.S. Treasury bond forward contracts:			
Net realized investment gains on disposal.....	33,143	—	—
Change in fair value.....	<u>(13,866)</u>	<u>—</u>	<u>—</u>
Net realized investment gains.....	<u>19,277</u>	<u>—</u>	<u>—</u>
Forward currency contracts:			
Net realized investment gains on disposal.....	23,037	100,666	25,835
Change in fair value.....	<u>(18,707)</u>	<u>(19,312)</u>	<u>52,855</u>
Net realized investment gains.....	<u>4,330</u>	<u>81,354</u>	<u>78,690</u>
Short total return swaps:			
Net realized investment (losses) gains on disposal.....	(308,629)	71,894	(103,516)
Change in fair value.....	<u>(80,359)</u>	<u>90,119</u>	<u>73,070</u>
Net realized investment (losses) gains.....	<u>(388,988)</u>	<u>162,013</u>	<u>(30,446)</u>
Long total return swaps:			
Net realized investment gains (losses) on disposal.....	1,674	(22,473)	25,050
Change in fair value.....	<u>5,282</u>	<u>5,558</u>	<u>(10,757)</u>
Net realized investment gains (losses).....	<u>6,956</u>	<u>(16,915)</u>	<u>14,293</u>
Other:			
Net realized investment (losses) gains on disposal.....	(76,627)	(7,737)	32,498
Change in fair value.....	<u>76,566</u>	<u>11,446</u>	<u>(27,728)</u>
Net realized investment (losses) gains.....	<u>(61)</u>	<u>3,709</u>	<u>4,770</u>
Total derivatives:			
Net realized investment (losses) gains on disposal.....	(327,402)	142,350	(53,249)
Change in fair value.....	<u>(79,779)</u>	<u>87,794</u>	<u>94,188</u>
Net realized investment (losses) gains.....	<u>\$ (407,181)</u>	<u>\$ 230,144</u>	<u>\$ 40,939</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(g) *Assets on Deposit*

The Company is required to maintain assets on deposit with various regulatory authorities to support its insurance and reinsurance operations. These requirements are generally promulgated in the statutes and regulations of the individual jurisdictions. The assets on deposit are available to settle insurance and reinsurance liabilities. For certain reinsurance contracts, derivative contracts and affiliate guarantees, the Company utilizes trust funds to collateralize its obligations or potential obligations to the ceding companies and counterparties. As of December 31, 2016, restricted assets supporting these deposits and trust fund requirements totaled \$1.0 billion, as depicted in the following table (in thousands):

	Restricted Assets Relating to:				
	Cash				
	Fixed Income Securities	Cash Equivalents Short-term Investments	Common Stocks	Partnerships	Total
	\$	\$	\$	\$	\$
U.S. regulatory requirements	82,457	—	—	—	82,457
Foreign regulatory requirements	76,744	210,654	43,494	—	330,892
Derivative collateral requirements	14,241	34,829	—	—	49,070
Reinsurance collateral requirements	331,984	87,441	97,335	5,869	522,629
Guarantee collateral requirements	29,763	19,485	—	—	49,248
Total	<u>535,189</u>	<u>352,409</u>	<u>140,829</u>	<u>5,869</u>	<u>1,034,296</u>

5. **Accumulated Other Comprehensive Income**

The following table shows the components of the change in accumulated other comprehensive income, net of deferred income taxes, for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	2016	2015	2014
Beginning balance of unrealized net appreciation on securities	\$ 153,147	\$ 365,104	\$ 214,389
Ending balance of unrealized net appreciation on securities	<u>86,858</u>	<u>153,147</u>	<u>365,104</u>
Current period change in unrealized net (depreciation) appreciation on securities	<u>(66,289)</u>	<u>(211,957)</u>	<u>150,715</u>
Beginning balance of foreign currency translation adjustments	26,562	44,168	29,015
Ending balance of foreign currency translation adjustments	<u>10,854</u>	<u>26,562</u>	<u>44,168</u>
Current period change in foreign currency translation adjustments	<u>(15,708)</u>	<u>(17,606)</u>	<u>15,153</u>
Beginning balance of benefit plan liabilities	(28,545)	(27,604)	(12,347)
Ending balance of benefit plan liabilities	<u>(30,131)</u>	<u>(28,545)</u>	<u>(27,604)</u>
Current period change in benefit plan liabilities	<u>(1,586)</u>	<u>(941)</u>	<u>(15,257)</u>
Other comprehensive (loss) income	<u>\$ (83,583)</u>	<u>\$ (230,504)</u>	<u>\$ 150,611</u>
Beginning balance of accumulated other comprehensive income ..	\$ 151,164	\$ 381,668	\$ 231,057
Other comprehensive (loss) income	<u>(83,583)</u>	<u>(230,504)</u>	<u>150,611</u>
Ending balance of accumulated other comprehensive income ..	<u>\$ 67,581</u>	<u>\$ 151,164</u>	<u>\$ 381,668</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table shows the components of accumulated other comprehensive income and the related deferred income taxes on each component, as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Gross:		
Unrealized appreciation on securities.....	\$ 133,459	\$ 235,412
Foreign currency translation adjustments	16,701	40,867
Benefit plan liabilities.....	<u>(46,356)</u>	<u>(43,916)</u>
Total accumulated other comprehensive income, gross of deferred income taxes.....	<u>\$ 103,804</u>	<u>\$ 232,363</u>
Deferred taxes:		
Unrealized appreciation on securities.....	\$ (46,601)	\$ (82,265)
Foreign currency translation adjustments	(5,847)	(14,305)
Benefit plan liabilities.....	<u>16,225</u>	<u>15,371</u>
Total deferred taxes on accumulated other comprehensive income	<u>\$ (36,223)</u>	<u>\$ (81,199)</u>

The following table shows the changes in the balances of each component of accumulated other comprehensive income (loss), for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>Unrealized Gains and Losses on Securities</u>	<u>Foreign Currency Items</u>	<u>Benefit Plan Items</u>	<u>Total</u>
Balance, January 1, 2014	\$ 214,389	\$ 29,015	\$ (12,347)	\$ 231,057
Amounts arising during the period	126,221	11,055	(15,641)	121,635
Reclassification adjustment included in net income	<u>24,494</u>	<u>4,098</u>	<u>384</u>	<u>28,976</u>
Net other comprehensive income (loss)	<u>150,715</u>	<u>15,153</u>	<u>(15,257)</u>	<u>150,611</u>
Balance, December 31, 2014	<u>365,104</u>	<u>44,168</u>	<u>(27,604)</u>	<u>381,668</u>
Amounts arising during the period	(189,574)	(20,123)	(2,301)	(211,998)
Reclassification adjustment included in net (loss) income	<u>(22,383)</u>	<u>2,517</u>	<u>1,360</u>	<u>(18,506)</u>
Net other comprehensive loss.....	<u>(211,957)</u>	<u>(17,606)</u>	<u>(941)</u>	<u>(230,504)</u>
Balance, December 31, 2015	<u>153,147</u>	<u>26,562</u>	<u>(28,545)</u>	<u>151,164</u>
Amounts arising during the period	(34,497)	(24,229)	(3,017)	(61,743)
Reclassification adjustment included in net (loss) income	<u>(31,792)</u>	<u>8,521</u>	<u>1,431</u>	<u>(21,840)</u>
Net other comprehensive (loss)	<u>(66,289)</u>	<u>(15,708)</u>	<u>(1,586)</u>	<u>(83,583)</u>
Balance, December 31, 2016	<u>\$ 86,858</u>	<u>\$ 10,854</u>	<u>\$ (30,131)</u>	<u>\$ 67,581</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table shows the significant amounts reclassified out of each component of accumulated other comprehensive income for the years ended of December 31, 2016, 2015 and 2014 (in thousands):

Details about Accumulated Other Comprehensive Income Components	Amount Reclassified from Accumulated Other Comprehensive Income (a)			Affected Line Item in the Consolidated Statement of Operations Where Net Income is Presented
	2016	2015	2014	
Unrealized net depreciation (appreciation) of securities:				
	\$ 48,910	\$ 34,436	\$ (37,683)	Net realized investment gains (loss)
	(17,118)	(12,053)	13,189	Total federal and foreign income (benefit) provision
	<u>\$ 31,792</u>	<u>\$ 22,383</u>	<u>\$ (24,494)</u>	Net income (loss)
Foreign currency translations:				
	\$ (13,109)	\$ (3,873)	\$ (6,304)	Net realized investment losses
	4,588	1,356	2,206	Total federal and foreign income provision
	<u>\$ (8,521)</u>	<u>\$ (2,517)</u>	<u>\$ (4,098)</u>	Net loss
Amortization of benefit plan items:				
Net actuarial loss.....	\$ (2,239)	\$ (2,129)	\$ (608)	Other underwriting expenses (b)
Prior service costs	<u>37</u>	<u>37</u>	<u>19</u>	Other underwriting expenses (b)
	(2,202)	(2,092)	(589)	Loss before federal and foreign income tax benefit
	771	732	205	Total federal and foreign income tax provision
	<u>\$ (1,431)</u>	<u>\$ (1,360)</u>	<u>\$ (384)</u>	Net loss
Total reclassifications	<u>\$ 21,840</u>	<u>\$ 18,506</u>	<u>\$ (28,976)</u>	

(a) Amounts in parentheses indicate decreases to the indicated line item of the consolidated statement of operations.

(b) These accumulated other comprehensive income components are included in the computation of net periodic benefit plan costs (see Note 14 for additional details).

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

6. Unpaid Losses and Loss Adjustment Expenses

The following table sets forth the activity in the liability for unpaid losses and loss adjustment expenses for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Gross unpaid losses and loss adjustment expenses, beginning of year	\$ 5,002,422	\$ 5,317,465	\$ 5,569,515
Less: Ceded unpaid losses and loss adjustment expenses, beginning of year	<u>690,884</u>	<u>726,196</u>	<u>790,642</u>
Net unpaid losses and loss adjustment expenses, beginning of year	<u>4,311,538</u>	<u>4,591,269</u>	<u>4,778,873</u>
Add: Net incurred losses and loss adjustment expenses related to:			
Current year	1,438,311	1,419,132	1,473,125
Prior years	<u>(266,486)</u>	<u>(233,358)</u>	<u>(189,128)</u>
Total net incurred losses and loss adjustment expenses	<u>1,171,825</u>	<u>1,185,774</u>	<u>1,283,997</u>
Less: Net paid losses and loss adjustment expenses related to:			
Current year	264,582	275,728	275,305
Prior years	<u>972,915</u>	<u>1,048,267</u>	<u>1,010,103</u>
Total net paid losses and loss adjustment expenses	<u>1,237,497</u>	<u>1,323,995</u>	<u>1,285,408</u>
Effect of exchange rate changes.....	<u>(27,625)</u>	<u>(141,510)</u>	<u>(186,193)</u>
Net unpaid losses and loss adjustment expenses, end of year	4,218,241	4,311,538	4,591,269
Add: Ceded unpaid losses and loss adjustment expenses, end of year	<u>658,607</u>	<u>690,884</u>	<u>726,196</u>
Gross unpaid losses and loss adjustment expenses, end of year	<u>\$ 4,876,848</u>	<u>\$ 5,002,422</u>	<u>\$ 5,317,465</u>

Estimates of reserves for unpaid losses and loss adjustment expenses, which relate to loss events that have occurred on or before the balance sheet date, are contingent on many assumptions that may or may not occur in the future. These assumptions include loss estimates attributable to a variety of loss events, including earthquakes, hurricanes, windstorms and floods. The eventual outcome of these loss events may be different from the assumptions underlying the Company's reserve estimates. When the business environment and loss trends diverge from expected trends, the Company may have to adjust its reserves accordingly, potentially resulting in adverse or favorable effects to the Company's financial results. The Company believes that the recorded estimate represents the best estimate of unpaid losses and loss adjustment expenses based on the information available as of December 31, 2016. The estimate is reviewed on a quarterly basis and the ultimate liability may be greater or less than the amounts provided; any changes in the estimated ultimate liability are reported in the periods in which they become known.

Net incurred losses and loss adjustment expenses related to the current year were \$1,438.3 million, \$1,419.1 million and \$1,473.1 million for the years ended December 31, 2016, 2015 and 2014, respectively. The increase in incurred losses and loss adjustment expenses for the year ended December 31, 2016 was principally attributable to an increase in current year catastrophe losses largely offset by a decrease in non-catastrophe losses in the EuroAsia division. The decrease in incurred losses and loss adjustment expenses for the year ended December 31, 2015 was principally attributable to improved results on crop business in the U.S. Insurance division. For the years ended December 31, 2016, 2015 and 2014, current year property catastrophe losses were \$190.3 million, \$108.5 million and \$148.5 million, respectively. For the year ended December 31, 2016, current year property catastrophe losses included \$30.8 million related to Hurricane Matthew. For the year ended December 31, 2014, current year property catastrophe losses included \$39.0 million related to windstorm Ela. For the year ended December 31, 2015, current year losses included \$55.9 million for the Port of Tianjin explosion.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Net incurred losses and loss adjustment expenses related to prior years included reductions in loss estimates of \$266.5 million, \$233.4 million and \$189.1 million for the years ended December 31, 2016, 2015 and 2014, respectively. The reductions in prior years' incurred losses and loss adjustment expenses were attributable to decreased loss estimates due to loss emergence lower than expectations in all divisions.

Net paid losses and loss adjustment expenses related to the current year were \$264.6 million, \$275.7 million and \$275.3 million for the years ended December 31, 2016, 2015 and 2014, respectively. The decrease in paid losses and loss adjustment expenses for the year ended December 31, 2016 was principally due to a decrease in payments on crop business in the U.S. Insurance division.

The effects of exchange rate changes on net unpaid losses and loss adjustment expenses resulted in decreases of \$27.6 million, \$141.5 million and \$186.2 million for the years ended December 31, 2016, 2015, and 2014, respectively, and were attributable to the North America, Latin America, EuroAsia, and London Market divisions.

Ceded unpaid losses and loss adjustment expenses were \$658.6 million, \$690.9 million and \$726.2 million as of December 31, 2016, 2015 and 2014, respectively. The decrease in ceded unpaid losses and loss adjustment expenses for the year ended December 31, 2016 was principally attributable to decrease in ceded unpaid reinsurance recoverables in the U.S. Insurance division. The decrease in ceded unpaid losses and loss adjustment expenses for the year ended December 31, 2015 was principally attributable to decreases in ceded unpaid reinsurance recoverables in the London Market and U.S. Insurance divisions.

The Company uses tabular reserving for workers' compensation indemnity loss reserves, which are considered to be fixed and determinable, and discounts such reserves using an interest rate of 3.5%. Workers' compensation indemnity loss reserves have been discounted using the Life Table for Total Population: United States, 2009. Reserves reported at the discounted value were \$54.3 million and \$59.4 million as of December 31, 2016 and 2015, respectively. The amount of case reserve discount was \$18.5 million and \$21.0 million as of December 31, 2016 and 2015, respectively. The amount of incurred but not reported reserve discount was \$20.6 million and \$21.6 million as of December 31, 2016 and 2015, respectively.

The Company is not materially exposed to asbestos and environmentally-related liabilities and does not establish a specific reserve for such exposures.

7. Reinsurance and Retrocessions

The Company utilizes reinsurance and retrocessional agreements to reduce and spread the risk of loss on its insurance and reinsurance business and to limit exposure to multiple claims arising from a single occurrence. The Company is subject to accumulation risk with respect to catastrophic events involving multiple treaties, facultative certificates and insurance policies. To protect against these risks, the Company purchases catastrophe excess of loss protection. The retention, the level of capacity purchased, the geographical scope of the coverage and the costs vary from year to year. Additionally, the Company purchases specific protections related to the insurance business underwritten by its London Market and U.S. Insurance divisions.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

There is credit risk with respect to reinsurance, which would result in the Company recording a charge to earnings in the event that such reinsuring companies are unable, at some later date, to meet their obligations under the reinsurance agreements in force. Reinsurance recoverables are recorded as assets and a reserve for uncollectible reinsurance recoverables is established based on the Company's evaluation of each reinsurer's or retrocessionaire's ability to meet its obligations under the agreements. Premiums written and earned are stated net of reinsurance ceded in the consolidated statements of operations. Direct, reinsurance assumed, reinsurance ceded and net amounts for the years ended December 31, 2016, 2015 and 2014 follow (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Premiums Written			
Direct	\$ 1,086,119	\$ 1,089,892	\$ 1,185,239
Add: assumed	1,294,628	1,314,093	1,554,272
Less: ceded	<u>280,570</u>	<u>309,000</u>	<u>345,678</u>
Net	<u>\$ 2,100,177</u>	<u>\$ 2,094,985</u>	<u>\$ 2,393,833</u>
Premiums Earned			
Direct	\$ 1,070,553	\$ 1,108,264	\$ 1,132,357
Add: assumed	1,303,878	1,416,857	1,562,517
Less: ceded	<u>300,335</u>	<u>321,051</u>	<u>338,297</u>
Net	<u>\$ 2,074,096</u>	<u>\$ 2,204,070</u>	<u>\$ 2,356,577</u>

The total amount of reinsurance recoverable on paid and unpaid losses as of December 31, 2016 and 2015 was \$700.7 million and \$732.4 million, respectively. The reserve for uncollectible reinsurance recoverable was \$15.0 million and \$18.4 million, as of December 31, 2016 and 2015, respectively, and has been netted against reinsurance recoverables on loss payments in the consolidated balance sheets.

In accordance with the terms of certain reinsurance agreements, the Company has recorded interest expense associated with its ceded reinsurance agreements of less than \$0.1 million for each of the years ended December 31, 2016, 2015 and 2014.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

8. Reinsurance Recoverables

The Company's ten largest reinsurers represent 60.1% of its total reinsurance recoverables as of December 31, 2016. Amounts due from all other reinsurers are diversified, with no other individual reinsurer representing more than \$25.1 million, or 3.6%, of reinsurance recoverables as of December 31, 2016, and the average balance is less than \$1.9 million. The Company held total collateral of \$134.7 million as of December 31, 2016, representing 19.2% of total reinsurance recoverables. The following table shows the total amount as of December 31, 2016 that is recoverable from each of the Company's ten largest reinsurers for paid and unpaid losses, the amount of collateral held and each reinsurer's A.M. Best rating (in thousands):

<u>Reinsurer</u>	<u>Reinsurance Recoverable</u>	<u>% of Total</u>	<u>Collateral</u>	<u>A.M. Best Rating</u>
Lloyd's Syndicates (excluding Brit PLC Syndicate 2987)	\$ 102,820	14.7%	\$ 1,264	A
Chubb Tempest Reinsurance Ltd	46,488	6.6	21,212	A++
Federal Crop Insurance Corporation	45,071	6.4	—	NR
Markel CatCo Reinsurance Ltd	39,325	5.6	39,325	NR
CRC Reinsurance Limited	38,285	5.5	38,285	NR
National Indemnity Company	31,248	4.5	—	A++
Markel Global Reinsurance Co.	30,420	4.3	—	A
Berkley Insurance Company	30,267	4.3	—	A+
Brit Limited (Lloyd's Syndicate 2987).....	29,993	4.3	—	A
Everest Reinsurance (Bermuda) Ltd	27,424	3.9	—	A+
Sub-total.....	421,341	60.1	100,086	
All other	279,347	39.9	34,581	
Total	<u>\$ 700,688</u>	<u>100.0%</u>	<u>\$ 134,667</u>	

Several individual reinsurers are part of the same corporate group. The following table shows the five largest aggregate amounts that are recoverable from all individual entities that form part of the same corporate group as of December 31, 2016 and the amount of collateral held from each group (in thousands):

<u>Reinsurer</u>	<u>Reinsurance Recoverable</u>	<u>% of Total</u>	<u>Collateral</u>
Lloyd's Syndicates (excluding Brit PLC Syndicate 2987)	\$ 102,820	14.7%	\$ 1,264
Markel Corporation	96,175	13.7	41,241
Fairfax Financial Holdings Ltd.	90,765	13.0	40,539
Chubb Limited.....	48,016	6.8	21,212
Federal Crop Insurance Corporation	45,071	6.4	—
Sub-total.....	382,847	54.6	104,256
All other	317,841	45.4	30,411
Total	<u>\$ 700,688</u>	<u>100.0%</u>	<u>\$ 134,667</u>

Reinsurance recoverables were \$732.4 million and collateral was \$97.4 million, or 13.3% of the reinsurance recoverable balance, as of December 31, 2015.

The Company is the beneficiary of letters of credit, cash and other forms of collateral to secure certain amounts due from its reinsurers. Collateral held by the Company as of December 31, 2016 was comprised of the following forms (in thousands):

<u>Form of Collateral</u>	<u>Collateral</u>	<u>% of Recoverables</u>
Letters of credit	\$ 38,782	5.5%
Funds withheld from reinsurers	42,286	6.0
Trust agreements.....	53,599	7.7
Total	<u>\$ 134,667</u>	<u>19.2%</u>

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Each reinsurance contract between the Company and the reinsurer describes the losses that are covered under the contract and terms upon which payments are to be made. The Company generally has the ability to utilize collateral to settle unpaid balances due under its reinsurance contracts when it determines that the reinsurer has not met its contractual obligations. Letters of credit are for the sole benefit of the Company to support the obligations of the reinsurer, providing the Company with the unconditional ability, in its sole discretion, to draw upon the letters of credit in support of any unpaid amounts due under the relevant contracts. Cash and investments supporting funds withheld from reinsurers are included in the Company's invested assets. Funds withheld from reinsurers are typically used to automatically offset payments due to the Company in accordance with the terms of the relevant reinsurance contracts. Amounts held under trust agreements are typically comprised of cash and investment grade fixed income securities and are not included in the Company's invested assets. The ability of the Company to draw upon funds held under trust agreements to satisfy any unpaid amounts due under the relevant reinsurance contracts is typically unconditional and at the sole discretion of the Company.

9. Debt Obligations, Common Shares, Preferred Shares and Non-Controlling Interest

Debt Obligations

The amortized cost by component of the Company's debt obligations as of December 31, 2016 and 2015 were as follows (in thousands):

	December 31, 2016	December 31, 2015
Series A Floating Rate Senior Debentures due 2021	\$ 49,890	\$ 49,863
Series C Floating Rate Senior Debentures due 2021	39,925	39,910
Total debt obligations	<u>\$ 89,815</u>	<u>\$ 89,773</u>

On November 28, 2006, the Company completed the private sale of \$40.0 million aggregate principal amount of floating rate senior debentures, Series C, due December 15, 2021 (the "Series C Notes"). Interest on the Series C Notes accrues at a rate per annum equal to the three-month London Interbank Offer Rate ("LIBOR"), reset quarterly, plus 2.50%, and is payable quarterly in arrears on March 15, June 15, September 15 and December 15 of each year. The Company has the option to redeem the Series C Notes at par, plus accrued and unpaid interest, in whole or in part on any interest payment date. For the years ended December 31, 2016 and 2015, the average annual interest rate on the Series C Notes was 3.18% and 2.80%, respectively.

On February 22, 2006, the Company issued \$100.0 million aggregate principal amount of floating rate senior debentures, pursuant to a private placement. The net proceeds from the offering, after fees and expenses, were \$99.3 million. The debentures were sold in two tranches: \$50.0 million of Series A, due March 15, 2021 (the "Series A Notes"), and \$50.0 million of Series B, due March 15, 2016 (the "Series B Notes"). Interest on each series of debentures is due quarterly in arrears on March 15, June 15, September 15 and December 15 of each year. The interest rate on each series of debentures is equal to the three-month LIBOR, reset quarterly, plus 2.20%. The Series A Notes are callable by the Company on any interest payment date at their par value, plus accrued and unpaid interest. For the years ended December 31, 2016 and 2015, the average annual interest rate on Series A Notes was 2.88% and 2.50%, respectively. The Series B Notes were called by the Company on December 15, 2014.

During the second quarter of 2005, the Company issued \$125.0 million aggregate principal amount of senior notes due May 1, 2015. The issue was sold at a discount of \$0.8 million, which was amortized over the life of the notes. Interest accrued on the senior notes at a fixed rate of 6.875% per annum and was due semi-annually on May 1 and November 1. On May 1, 2015, the 6.875% Senior Notes matured with \$125.0 million distributed to the noteholders.

As of December 31, 2016 and 2015, the estimated fair value of the Company's debt obligations was \$94.1 million and \$92.0 million, respectively. The estimated fair value is based on quoted market prices of the Company's debt, where available, for debt similar to the Company's, and discounted cash flow calculations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Common Shares

The Company did not issue any common shares during the year ended December 31, 2016.

The Company issued 1,502 common shares to a Fairfax affiliate during the second quarter of 2015 in exchange for a \$125.0 million capital contribution to fund the payment of the Company's \$125.0 million Senior Notes 6.875%, which matured on May 1, 2015.

The Company issued 15,555 common shares during the year ended December 31, 2014, of which 15,518 shares related to the reorganization of the Company's ownership structure discussed in Note 1. The Company redeemed and retired 21,327 common shares during the year ended December 31, 2014 as a result of the reorganization of the Company's ownership structure.

The Company declared and paid \$200.0 million common share dividends during each of the years ended December 31, 2016 and 2015. The Company did not declare or pay any common share dividends during the year ended December 31, 2014.

Preferred Shares

As discussed in Note 1, a reorganization of the ownership structure of the Company by Fairfax during the year ended December 31, 2014 resulted in the redemption of all of the Company's Series A and Series B preferred shares.

The Company's 8.125% Series A preferred shares (253,599 shares outstanding as of December 31, 2013) had a liquidation preference of \$25.00 per share and were redeemable at \$25.00 per share at the Company's option, in whole or in part at any time. Dividends on the Company's floating rate Series B preferred shares (70,000 shares outstanding as of December 31, 2013) were payable at an annual rate equal to 3.25% above the three-month LIBOR on the applicable quarterly determination date. The Series B preferred shares had a liquidation preference of \$25.00 per share and were redeemable at \$25.00 per share at the Company's option, in whole or in part, at any time.

Dividends on each series of preferred shares were deferrable on a non-cumulative basis, provided that no dividends or other distributions had been declared or paid or set apart for payment on any other class or series of the Company's capital shares ranking junior to or equal with the preferred shares. Dividends on Series A and Series B preferred shares were each payable when, as and if declared by the Company's Board of Directors, quarterly on the 20th day of January, April, July, and October of each year. Deferred dividends on either series did not accrue interest prior to the date of redemption. The Company declared and paid Series A and Series B preferred dividends for the year ended December 31, 2014 as follows (in thousands):

<u>Preferred dividends</u>	<u>2014</u>
	<u>Declared and Paid</u>
Series A	\$ 515
Series B	61
Total dividends paid and declared	<u>\$ 576</u>

Non-Controlling Interest – Preferred Shares of Subsidiaries

On September 30, 2016, Clearwater Insurance Company ("Clearwater") merged with and into TIG Insurance Company ("TIG"), a Fairfax affiliate. Clearwater held all 23,807 shares of Hudson's 5.5% Series A preferred stock with a liquidation preference of \$1,000 per share and an aggregate book value of \$23.8 million, and all 5,492 shares of Clearwater Select's 5.5% Series A preferred stock, with a liquidation preference of \$1,000 per share and an aggregate book value of \$5.5 million. On October 6, 2016, Clearwater Select's Board of Directors declared a preferred dividend to TIG in the amount of \$0.3 million and Hudson's Board of Directors declared a preferred dividend to TIG in the amount of \$1.3 million. Both dividends were paid on October 20, 2016. The aggregate amount of the preferred shares of Hudson and Clearwater Select owned by TIG is presented on the balance sheet as non-controlling interest in the amount of \$29.3 million.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

10. Federal and Foreign Income Taxes

The components of the federal and foreign income tax provision included in the consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Current:			
United States	\$ 5,593	\$ 200,240	\$ 168,768
Foreign	22,915	28,027	53,499
Total current income tax provision.....	<u>28,508</u>	<u>228,267</u>	<u>222,267</u>
Deferred:			
United States	(19,766)	(99,636)	95,102
Foreign	<u>(4,327)</u>	<u>(8,957)</u>	<u>(7,874)</u>
Total deferred income tax (benefit) provision.....	<u>(24,093)</u>	<u>(108,593)</u>	<u>87,228</u>
Total federal and foreign income tax provision	<u>\$ 4,415</u>	<u>\$ 119,674</u>	<u>\$ 309,495</u>

Deferred federal and foreign income taxes reflect the tax impact of temporary differences between the amount of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws and regulations. Components of federal and foreign income tax assets and liabilities as of December 31, 2016 and 2015 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Unpaid losses and loss adjustment expenses.....	\$ 80,352	\$ 94,576
Unearned premiums.....	42,424	41,039
Reserve for potentially uncollectible balances.....	6,838	6,192
Pension and benefit accruals.....	34,505	32,971
Investments	161,174	138,460
Alternative minimum tax credit.....	1,561	2,331
Foreign tax credit.....	97,345	115,062
Other.....	<u>2,688</u>	<u>598</u>
Total deferred tax assets.....	<u>426,887</u>	<u>431,229</u>
Deferred acquisition costs.....	55,160	52,192
Foreign deferred items.....	20,182	24,509
Subsidiary net operating loss.....	<u>7,754</u>	<u>34,831</u>
Total deferred tax liabilities	<u>83,096</u>	<u>111,532</u>
Net deferred tax assets.....	343,791	319,697
Deferred income taxes on accumulated other comprehensive income	<u>(36,223)</u>	<u>(81,199)</u>
Deferred federal and foreign income tax asset.....	307,568	238,498
Current federal and foreign income tax receivable (payable)	<u>93,214</u>	<u>(31,127)</u>
Federal and foreign income taxes receivable.....	<u>\$ 400,782</u>	<u>\$ 207,371</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table reconciles federal and foreign income taxes at the statutory federal income tax rate to the Company's tax provision and effective tax rate for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	2016		2015		2014	
	Amount	% of Pre-tax Income	Amount	% of Pre-tax Income	Amount	% of Pre-tax Income
Income before income taxes	<u>\$ 165,323</u>		<u>\$ 418,968</u>		<u>\$ 900,179</u>	
Income tax provision computed at the						
U.S. statutory tax rate on income	\$ 57,863	35.0%	\$ 146,639	35.0%	\$ 315,063	35.0%
(Decrease) increase in income taxes resulting from:						
Dividend received deduction	(3,259)	(2.0)	(1,506)	(0.4)	(193)	(0.0)
Tax-exempt income.....	(23,353)	(14.1)	(30,827)	(7.4)	(36,398)	(4.0)
Foreign tax expense	—	—	209	0.0	33,670	3.7
Release of tax sharing liability.....	(32,999)	(20.0)	—	(0.0)	—	(0.0)
Other, net.....	<u>6,163</u>	<u>3.7</u>	<u>5,159</u>	<u>1.4</u>	<u>(2,647)</u>	<u>(0.3)</u>
Total federal and foreign income tax provision.....	<u>\$ 4,415</u>	<u>2.6%</u>	<u>\$ 119,674</u>	<u>28.6%</u>	<u>\$ 309,495</u>	<u>34.4%</u>

Pre-tax (loss) income generated in the United States was \$(3.3) million, \$340.5 million and \$636.6 million for the years ended December 31, 2016, 2015 and 2014, respectively. Foreign pre-tax income was \$168.6 million, \$78.5 million and \$263.6 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The Company has claimed the benefit of a foreign tax credit in the tax years ended December 31, 2016 and 2015. The Company had elected to expense foreign taxes in its federal income tax returns for the year ended December 31, 2014.

During 2016, the Company released the deferred tax liability relating to a contingent contractual obligation to a former subsidiary of the Company as a result of the Company's utilization of the former subsidiary's net operating losses in years prior to the sale of the former subsidiary, pursuant to tax sharing agreements in effect for those years, following the determination that such liability will not be realized.

The Company is included in the United States tax group of Fairfax (US). The method of allocation among the companies is subject to a written agreement. Tax payments are made to, or refunds received from, Fairfax (US) in amounts equal to the amounts as if separate tax returns were filed with federal taxing authorities.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company paid federal and foreign income taxes of \$152.8 million, \$298.0 million and \$87.4 million for the years ended December 31, 2016, 2015 and 2014, respectively. As of December 31, 2016, the Company had a current tax receivable of \$93.2 million, which included \$88.0 million receivable from Fairfax (US) and a net receivable of \$5.2 million from various foreign governments. As of December 31, 2015, the Company had a current tax payable of \$31.1 million, which included \$24.7 million payable to Fairfax (US) and a net payable of \$6.4 million to various foreign governments. The Company files income tax returns with various federal, state and foreign jurisdictions.

The Company's U.S. federal income tax returns for tax years prior to 2014 are closed. The Internal Revenue Service ("IRS") is expected to complete their audit of the Company's 2014 returns during 2017. Effective for 2014 through 2017 tax years, the Company participates in the IRS's Compliance Assurance Program ("CAP"). Under CAP, the IRS begins their examination of the tax year before the tax return is filed. The goal of CAP is to expedite the exam process and reduce the level of uncertainty regarding a taxpayer's filing positions by examining significant transactions and events as they occur. The IRS has not proposed any material adjustments as part of the Company's ongoing examinations. Income tax returns filed with various state and foreign jurisdictions remain open to examination in accordance with individual statutes.

The Company has elected to recognize accrued interest and penalties associated with uncertain tax positions as part of the income tax provision. The Company does not have any material unrecognized tax benefits and, accordingly, has not recognized any accrued interest or penalties associated with uncertain tax positions.

The Company has recorded foreign tax credits of \$97.3 million, of which \$2.6 million, \$0.9 million and \$13.3 million expire in 2020, 2025 and 2026, respectively, the remainder of which the carryforward period has not yet begun.

11. Commitments and Contingencies

(a) Contingencies

The Company participates in Lloyd's through its 100% ownership of the capital provider for Newline Syndicate (1218), for which the Company directly or indirectly provides 100% of the capacity. The results of Newline Syndicate (1218) are consolidated in the financial statements of the Company. In support of Newline Syndicate (1218)'s capacity at Lloyd's, the Company has pledged securities and cash with a fair value of \$276.6 million as of December 31, 2016 in a deposit trust account in favor of the Society and Council of Lloyd's. The securities may be substituted with other securities at the discretion of the Company, subject to approval by Lloyd's. The securities are carried at fair value and are included in investments and cash in the Company's consolidated balance sheets. Interest earned on the securities is included in investment income. The pledge of assets in support of Newline Syndicate (1218) provides the Company with the ability to participate in writing business through Lloyd's, which remains an important part of the Company's business. The pledged assets effectively secure the contingent obligations of Newline Syndicate (1218) should it not meet its obligations. The Company's contingent liability to the Society and Council of Lloyd's is limited to the aggregate amount of the pledged assets. The Company has the ability to remove funds at Lloyd's annually, subject to certain minimum amounts required to support outstanding liabilities as determined under risk-based capital models and approved by Lloyd's. The funds used to support outstanding liabilities are adjusted annually and the obligations of the Company to support these liabilities will continue until they are settled or the liabilities are reinsured by a third party approved by Lloyd's. The Company expects to continue to actively operate Newline Syndicate (1218) and support its requirements at Lloyd's. The Company believes that Newline Syndicate (1218) maintains sufficient liquidity and financial resources to support its ultimate liabilities and the Company does not anticipate that the pledged assets will be utilized.

ORC agreed to guarantee the performance of all the insurance and reinsurance contract obligations of Compagnie Transcontinentale de Réassurance ("CTR"), a subsidiary of Fairfax, in the event CTR became insolvent and CTR was not otherwise indemnified under its guarantee agreement with a Fairfax affiliate. Fairfax has agreed to indemnify ORC for all its obligations incurred under its guarantee. The Company's potential exposure in connection with this agreement stems from CTR's remaining gross reserves, which are estimated to be \$54.6 million as of December 31, 2016. The Company believes that the financial resources of the Fairfax subsidiaries that have assumed CTR's liabilities provide adequate protection to satisfy the obligations that are

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subject to this guarantee. The Company does not expect to make payments under this guarantee and does not consider its potential exposure under this guarantee to be material to its consolidated financial position.

ORC agreed, as of April 1, 2002, to guarantee the payment of all of the insurance contract obligations (the “Subject Contracts”), whether incurred before or after the agreement, of Falcon Insurance Company (Hong Kong) Limited (“Falcon”), a subsidiary of Fairfax Asia, in the event Falcon becomes insolvent. The guarantee by ORC was made to assist Falcon in writing business through access to ORC’s financial strength ratings and capital resources. ORC is paid a fee for this guarantee of one quarter of one percent of all gross premiums earned associated with the Subject Contracts on a quarterly basis. For the years ended December 31, 2016, 2015 and 2014, Falcon paid \$0.1 million, \$0.1 million and \$0.2 million, respectively, to ORC in connection with this guarantee. ORC’s potential exposure in connection with this agreement is estimated to be \$112.6 million, based on Falcon’s loss reserves at December 31, 2016. Fairfax has agreed to indemnify ORC for any obligation under this guarantee. The Company believes that the financial resources of Falcon provide adequate protection to support its liabilities in the ordinary course of business. The Company anticipates that Falcon will meet all of its obligations in the normal course of business and does not expect to make any payments under this guarantee. The Company does not consider its potential exposure under this guarantee to be material to its consolidated financial position.

During 2015, in consideration for an appropriate fee, ORC agreed to guarantee the payment of all of the obligations of Clearwater with respect to a certain contract of reinsurance of asbestos, pollution and health hazard claims (the “APH contract”) entered into by Clearwater with an unrelated third party. The guarantee was made to enable Clearwater, an unrated company, to access ORC’s financial strength ratings and capital resources for securing the APH Contract. On September 30, 2016, Clearwater merged with and into TIG. ORC’s maximum exposure in connection with this guarantee is \$350.0 million; as of December 31, 2016, the Company’s estimated exposure under the guarantee is \$83.4 million, based on TIG’s loss reserves for the APH Contract at December 31, 2016. The Company i) believes that the financial resources of TIG provide adequate protection to support its liabilities in the ordinary course of business; ii) anticipates that TIG will meet all of its obligations in the normal course of business and iii) does not expect to make any payments under this guarantee.

The Company and its subsidiaries are involved from time to time in ordinary litigation and arbitration proceedings as part of the Company’s business operations. In the Company’s opinion, the outcome of these suits, individually or collectively, is not likely to result in judgments that would be material to the financial condition or results of operations of the Company.

(b) *Commitments*

The Company and its subsidiaries lease office space and furniture and equipment under long-term operating leases expiring through the year 2028. Minimum annual rentals follow (in thousands):

	<u>Amount</u>
2017	\$ 11,185
2018	10,710
2019	9,974
2020	7,874
2021	7,383
2022 and thereafter	19,081
Total	<u>\$ 66,207</u>

Rental expense, before sublease income under these operating leases, was \$12.1 million, \$12.2 million and \$11.7 million for the years ended December 31, 2016, 2015 and 2014, respectively. The Company recovered \$0.1 million for the year ended December 31, 2016 and less than \$0.1 million for each of the years ended December 31, 2015 and 2014 from subleases.

12. Statutory Information and Dividend Restrictions

ORC, the Company’s principal operating subsidiary, is subject to state regulatory restrictions that limit the maximum amount of dividends payable. In any 12-month period, ORC may pay dividends equal to the greater of (i) 10% of statutory capital and surplus as of the prior year end or (ii) net income for such prior year, without prior approval of the Insurance Commissioner of the State of Connecticut (the “Connecticut Commissioner”).

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Connecticut law further provides that (i) ORC must report to the Connecticut Commissioner, for informational purposes, all dividends and other distributions within five business days after the declaration thereof and at least ten days prior to payment and (ii) ORC may not pay any dividend or distribution in excess of its earned surplus, defined as the insurer's "unassigned funds surplus" reduced by 25% of unrealized appreciation in value or revaluation of assets or unrealized profits on investments, as reflected in its most recent statutory annual statement on file with the Connecticut Commissioner, without the Connecticut Commissioner's approval. The maximum ordinary dividend capacity available during 2017, without prior approval, is \$319.4 million. ORC declared and paid to ORH dividends of \$200.0 million, \$300.0 million and \$325.0 million during the years ended December 31, 2016, 2015 and 2014, respectively. The dividends paid in 2014 included an extraordinary dividend of \$100.0 million, which was approved by the Connecticut Department. Hudson declared and paid dividends on its preferred shares owned by TIG of \$1.3 million during the year ended December 31, 2016. Clearwater Select declared and paid dividends on its preferred shares owned by TIG of \$0.3 million during each of the year ended December 31, 2016. Hudson declared and paid dividends on its preferred shares owned by Clearwater of \$1.3 million during each of the years ended December 31, 2015 and 2014. Clearwater Select declared and paid dividends on its preferred shares owned by Clearwater of \$0.3 million during each of the years ended December 31, 2015 and 2014.

The following is the consolidated statutory basis net income and policyholders' surplus of ORC and its subsidiaries, for each of the years ended and as of December 31, 2016, 2015 and 2014 (in thousands):

	2016	2015	2014
Net income	\$ 145,455	\$ 534,723	\$ 275,714
Policyholders' surplus	3,223,232	3,317,809	3,277,963

13. Related Party Transactions

The Company has entered into various reinsurance arrangements with Fairfax and its affiliates. The amounts included in or deducted from income, expense, assets and liabilities in the accompanying consolidated financial statements with respect to reinsurance assumed and ceded from and to affiliates as of and for the years ended December 31, 2016, 2015 and 2014, follow (in thousands):

	2016	2015	2014
Assumed:			
Premiums written	\$ 25,267	\$ 22,702	\$ 35,814
Premiums earned	23,148	25,963	33,339
Losses and loss adjustment expenses	8,278	12,689	14,698
Acquisition costs	1,722	3,164	9,352
Reinsurance payable on paid losses.....	667	2,474	2,952
Reinsurance balances receivable	4,604	5,117	4,288
Unpaid losses and loss adjustment expenses	57,896	60,684	59,190
Unearned premiums	8,826	6,692	9,960
Ceded:			
Premiums written	\$ 32,661	\$ 28,622	\$ 33,925
Premiums earned	32,566	33,565	23,609
Losses and loss adjustment expenses	22,066	19,057	7,761
Acquisition costs	3,253	4,409	5,957
Ceded reinsurance balances payable.....	2,705	2,579	2,199
Reinsurance recoverables on paid losses.....	1,299	680	(437)
Reinsurance recoverables on unpaid losses	99,585	83,550	49,203
Unearned premiums	10,588	10,617	12,179

The Company's subsidiaries have entered into investment management agreements with Fairfax and its wholly-owned subsidiary, Hamblin Watsa Investment Counsel Ltd. These agreements provide for an annual base fee of 0.20% (20 basis points), calculated and paid quarterly based upon each subsidiary's average invested assets for the preceding three months. The agreements also include incentive fees of 0.10% (10 basis points), which are payable if realized gains exceed 1% of the average investment portfolio in any given year, subject to cumulative

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realized gains on investments exceeding 1% of the average investment portfolio. Additional incentive fees are paid based upon the performance of the subsidiary's equity portfolio equal to 10% of the return on equities (subject to an annual maximum) in excess of the Standard & Poor's 500 index plus 200 basis points, provided that the equity portfolio has achieved such excess on a cumulative basis. If the performance of the equity portfolio does not equal or exceed this benchmark in a given year, the annual base fee, on the equity portion of the portfolio, is reduced to 0.18% (18 basis points). The aggregate annual investment management fee payable by each subsidiary, including incentive fees, is capped at 0.40% (40 basis points) of its investment portfolio, with any excess amounts carried into the following year. These agreements may be terminated by either party on 30 days' notice. For the years ended December 31, 2016, 2015 and 2014, total fees, including incentive fees, of \$21.5 million, \$14.5 million and \$22.8 million, respectively, are included in the consolidated statements of operations.

Included in other expense, net, for the years ended December 31, 2016, 2015 and 2014, are charitable contributions expenses of \$1.6 million, \$4.0 million and \$6.6 million, respectively, primarily representing amounts to be funded by ORH to the OdysseyRe Foundation, a not-for-profit entity through which the Company provides funding to charitable organizations active in the communities in which the Company operates.

Due to expense sharing and investment management agreements with Fairfax and its affiliates, the Company has accrued, on its consolidated balance sheet, amounts receivable from affiliates of \$4.0 million and \$2.1 million as of December 31, 2016 and 2015, respectively, and amounts payable to affiliates of \$7.1 million and \$1.2 million as of December 31, 2016 and 2015, respectively.

Effective May 1, 2012, Hudson entered into an agreement with Northbridge Indemnity Insurance Company and Commonwealth Insurance Company ("Commonwealth"), which are Fairfax subsidiaries, to acquire the renewal rights for certain insurance business underwritten by Commonwealth in the U.S. market (the "CW Business"). The purchase price for these renewal rights was \$4.0 million in cash plus a contingent obligation to pay up to \$5.0 million in additional consideration based upon the underwriting profitability of the CW Business for the ensuing five years. The total consideration for the contract of \$8.5 million (which consisted of the \$4.0 million cash payment plus the net present value of expected contingent payments as of the acquisition date) has been recorded as an intangible asset and is included in other assets as of December 31, 2016 and 2015; the asset is being amortized over five years. As of December 31, 2016 and 2015, the net present value of the contingent consideration obligation was \$0.1 million and \$2.9 million, respectively, and was included in other liabilities. In 2016, the contingent consideration was reduced to reflect the revised underwriting performance of the business.

On December 6, 2016, the Company loaned an affiliate, 9938982 Canada Inc., \$50.1 million, the proceeds of which were used to fund a debtor in possession loan to a Canadian retail company. The loan to 9938982 Canada Inc. bears interest at 8.0% and is due on February 28, 2017.

In the ordinary course of the Company's investment activities, the Company makes investments in investment funds, limited partnerships and other investment vehicles in which Fairfax or its affiliates may also be investors.

14. Employee Benefits

The Company provides its employees with benefits through various plans as described below.

Defined Benefit Pension Plan

The Company maintains a qualified, non-contributory, defined benefit pension plan (the "Pension Plan") covering substantially all employees in the United States hired prior to August 1, 2011 who have reached age twenty-one. Employer contributions to the Pension Plan are in accordance with the minimum funding requirements of the Employee Retirement Income Security Act of 1974, as amended.

The amortization period for unamortized pension costs and credits, including prior service costs, if any, and actuarial gains and losses, is based on the remaining service period for those employees expected to receive pension benefits. Actuarial gains and losses result when actual experience differs from that assumed or when actuarial assumptions are changed.

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The following tables set forth the Pension Plan's unfunded status and accrued pension cost recognized in the Company's consolidated financial statements as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Change in projected benefit obligation:		
Benefit obligation at beginning of year	\$ 159,624	\$ 152,601
Service cost	8,819	9,260
Interest cost	6,935	6,257
Actuarial loss (gain)	6,366	(5,507)
Benefits paid	<u>(2,445)</u>	<u>(2,987)</u>
Benefit obligation at end of year	<u>179,299</u>	<u>159,624</u>
Change in Plan assets:		
Fair value of Pension Plan assets at beginning of year	112,722	115,727
Actual appreciation (depreciation) on Pension Plan assets	12,186	(7,818)
Actual contributions during the year	7,800	7,800
Benefits paid	<u>(2,445)</u>	<u>(2,987)</u>
Fair value of Pension Plan assets at end of year	<u>130,263</u>	<u>112,722</u>
Funded status and accrued pension cost	<u>\$ (49,036)</u>	<u>\$ (46,902)</u>

The net amount reported in the consolidated balance sheets related to the accrued pension cost for the Pension Plan of \$49.0 million and \$46.9 million, as of December 31, 2016 and 2015, respectively, is included in other liabilities. The unamortized amount of accumulated other comprehensive loss related to the Pension Plan is \$28.0 million and \$28.7 million, before taxes, as of December 31, 2016 and 2015, respectively.

As of December 31, 2016 and 2015, the fair value and percentage of fair value of the total Pension Plan assets by type of investment are as follows (in thousands):

	<u>As of December 31,</u>			
	<u>2016</u>		<u>2015</u>	
Equity securities	\$ 79,782	61.3%	\$ 32,282	28.6%
Mutual funds - fixed income securities	38,699	29.7	—	0.0
Money market	11,782	9.0	17,331	15.4
Fixed income securities	<u>—</u>	<u>0.0</u>	<u>63,109</u>	<u>56.0</u>
Fair value of Plan assets	<u>\$ 130,263</u>	<u>100.0%</u>	<u>\$ 112,722</u>	<u>100.0%</u>

The Pension Plan seeks to maximize the economic value of its investments by applying a long-term, value-oriented approach to optimize the total investment returns of the Pension Plan's invested assets. Assets are transferred and allocated among various investment vehicles, when appropriate. The long-term rate of return assumption is based on this flexibility to adjust to market conditions. The actual return on assets has historically been in line with the Company's assumptions of expected returns. During the years ended December 31, 2016, 2015 and 2014, the Company contributed \$7.8 million, \$7.8 million, and \$8.3 million, respectively, to the Pension Plan. The Company currently expects to make a contribution to the Pension Plan of \$7.8 million during 2017.

The Company accounts for its Pension Plan assets at fair value as required by GAAP. The Company has categorized its Pension Plan assets, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy, using the three-level hierarchy approach described in Note 3.

For determining the fair value of the Company's Level 1 Pension Plan assets, quoted market prices are used. The majority of these Pension Plan assets are common stocks that are actively traded in a public market. The Pension Plan's money market account, for which the cost basis approximates fair value, is also classified as a Level 1 investment.

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The Company's Level 2 Pension Plan assets, the majority of which are in government, corporate and municipal fixed income securities, are priced using publicly traded over-the-counter prices and broker-dealer quotes. Observable inputs such as benchmark yields, reported trades, broker-dealer quotes, issuer spreads and bids are available for these investments.

As of December 31, 2016 and 2015, there were no Level 3 assets in the Pension Plan.

The following tables present the fair value hierarchy for those Pension Plan assets measured at fair value on a recurring basis as of December 31, 2016 and 2015 (in thousands):

	Assets Measured at Fair Value December 31, 2016	Fair Value Measurements as of December 31, 2016	
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Equity securities.....	\$ 79,782	\$ 79,782	\$ —
Mutual funds - fixed income securities	38,699	38,699	—
Money market	11,782	11,782	—
Total Pension Plan assets measured at fair value	\$ 130,263	\$ 130,263	\$ —

	Assets Measured at Fair Value December 31, 2015	Fair Value Measurements as of December 31, 2015	
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Fixed income securities	\$ 63,109	\$ —	\$ 63,109
Equity securities.....	32,282	32,282	—
Money market	17,331	17,331	—
Total Pension Plan assets measured at fair value	\$ 112,722	\$ 49,613	\$ 63,109

The following table presents the targeted asset allocation percentages for the Pension Plan's assets by type:

	Targeted Asset Allocation %
Equities	61.00
Mutual funds - fixed income securities	30.00
Money market	9.00
Total target asset allocations	100.00

The weighted average assumptions used to calculate the benefit obligation as of December 31, 2016 and 2015 are as follows:

	2016	2015
Discount rate	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%

The discount rate represents the Company's estimate of the interest rate at which the Pension Plan's benefits could be effectively settled. The discount rates are used in the measurement of the expected and accumulated Pension Plan benefit obligations and the service and interest cost components of net periodic Pension Plan benefit cost.

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The net periodic benefit cost included in the Company's consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 is comprised of the following (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net Periodic Benefit Cost:			
Service cost	\$ 8,819	\$ 9,261	\$ 8,579
Interest cost	6,935	6,257	5,483
Return on Plan assets	(6,582)	(6,833)	(6,030)
Recognized actuarial loss	1,504	569	—
Recognized prior service cost	—	—	18
Net periodic benefit cost	<u>\$ 10,676</u>	<u>\$ 9,254</u>	<u>\$ 8,050</u>
Change in accumulated other comprehensive loss (income):			
Beginning balance	\$ 28,729	\$ 20,155	\$ 7,074
Actuarial loss arising during the year	762	9,143	13,099
Amortization of actuarial loss recognized in net periodic costs	(1,504)	(569)	—
Amortization of prior service costs recognized in net periodic costs	—	—	(18)
Accumulated other comprehensive loss at end of year	<u>\$ 27,987</u>	<u>\$ 28,729</u>	<u>\$ 20,155</u>

The Company estimates that the net periodic benefit cost for the Pension Plan will be \$10.0 million for the year ended December 31, 2017. The Company does not expect any refunds of Pension Plan assets during the year ended December 31, 2017.

The weighted average assumptions used to calculate the net periodic benefit cost for the years ended December 31, 2016, 2015 and 2014 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Discount rate	4.50%	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%	3.80%
Expected long term rate of return on Pension Plan assets	6.00%	6.00%	6.00%

The accumulated benefit obligation for the Pension Plan was \$153.7 million and \$135.2 million as of the December 31, 2016 and 2015 measurement dates, respectively.

The Pension Plan's expected future benefit payments for the next 10 years are shown below (in thousands):

<u>Year</u>	<u>Amount</u>
2017	\$ 8,671
2018	8,354
2019	7,915
2020	9,585
2021	10,940
2022 – 2026	57,567

The amortization of actuarial losses and of prior service costs (currently reflected in accumulated other comprehensive income) as components of net periodic cost are expected to be \$1.3 million and \$0.0 million, respectively, for the year ended December 31, 2017.

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Excess Benefit Plans

The Company maintains two non-qualified excess benefit plans (the “Excess Plans”) that provide more highly compensated officers and employees in the United States hired prior to August 1, 2011 with defined retirement benefits in excess of qualified plan limits imposed by federal tax law. The following tables set forth the combined amounts recognized for the Excess Plans in the Company’s consolidated financial statements as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Change in projected benefit obligation:		
Benefit obligation at beginning of year	\$ 23,813	\$ 22,644
Service cost	1,232	1,121
Interest cost	1,046	941
Actuarial loss	985	119
Benefits paid	<u>(476)</u>	<u>(1,012)</u>
Benefit obligation at end of year	<u>26,600</u>	<u>23,813</u>
Change in Excess Plans’ assets:		
Fair value of Excess Plans’ assets at beginning of year	—	—
Actual contributions during the year	476	1,012
Benefits paid	<u>(476)</u>	<u>(1,012)</u>
Fair value of Excess Plans’ assets at end of year	<u>—</u>	<u>—</u>
Funded status and accrued pension cost	<u>\$ (26,600)</u>	<u>\$ (23,813)</u>

The net amount reported in the consolidated balance sheets related to the accrued pension cost for the Excess Plans of \$26.6 million and \$23.8 million, as of December 31, 2016 and 2015, respectively, is included in other liabilities. The unamortized amount of accumulated other comprehensive loss related to the Excess Plan is \$5.5 million and \$4.7 million, before taxes, as of December 31, 2016 and 2015, respectively.

The weighted average assumptions used to calculate the benefit obligation as of December 31, 2016 and 2015 are as follows:

	<u>2016</u>	<u>2015</u>
Discount rate	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%

The discount rate represents the Company’s estimate of the interest rate at which the Excess Plans’ benefits could be effectively settled. The discount rates are used in the measurement of the expected and accumulated Excess Plans’ benefit obligations and the service and interest cost components of net periodic Excess Plans’ benefit cost.

Net periodic benefit cost included in the Company’s consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 is comprised of the following (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net Periodic Benefit Cost:			
Service cost	\$ 1,232	\$ 1,121	\$ 944
Interest cost	1,046	941	834
Recognized net actuarial loss	242	251	27
Recognized prior service cost	<u>(37)</u>	<u>(37)</u>	<u>(37)</u>
Net periodic benefit cost	<u>\$ 2,483</u>	<u>\$ 2,276</u>	<u>\$ 1,768</u>
Change in accumulated other comprehensive loss (income):			
Beginning balance	\$ 4,740	\$ 4,835	\$ 1,964
Actuarial loss arising during the year	985	119	2,861
Amortization of actuarial loss recognized in net periodic costs	(243)	(251)	(27)
Amortization of prior service costs recognized in net periodic costs	<u>37</u>	<u>37</u>	<u>37</u>
Accumulated other comprehensive loss at end of year	<u>\$ 5,519</u>	<u>\$ 4,740</u>	<u>\$ 4,835</u>

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The Company estimates that the net periodic benefit cost for the Excess Plans will be \$2.8 million for the year ended December 31, 2017.

The weighted average assumptions used to calculate the net periodic benefit cost for the years ended December 31, 2016, 2015 and 2014 are as follows:

	2016	2015	2014
Discount rate	4.50%	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%	3.80%

The accumulated benefit obligation for the Excess Plans was \$19.8 million and \$18.1 million as of December 31, 2016 and 2015, respectively.

The Excess Plans' expected benefit payments for the next 10 years are shown below (in thousands):

Year	Amount
2017	\$ 1,210
2018	1,971
2019	2,006
2020	1,266
2021	7,706
2022 – 2026	11,801

The amortization of actuarial losses and of prior service costs (currently reflected in accumulated other comprehensive income) as components of net periodic costs are expected to be \$0.3 million and less than \$0.1 million, respectively, for the year ended December 31, 2017.

As of December 31, 2016 and 2015, respectively, there are no assets held directly by the Excess Plans, as a trust fund established for the Excess Plans was liquidated and closed during 2015. Following the liquidation and closing of this trust, all Excess Plan benefits realized by the participants are paid by the Company.

The Company expects to contribute \$1.2 million to the Excess Plans during the year ended December 31, 2017, which represents the amount necessary to fund the 2017 expected benefit payments.

Postretirement Benefit Plan

The Company provides certain health care and life insurance ("postretirement") benefits for retired employees in the United States. Substantially all employees in the United States hired prior to August 1, 2011 may become eligible for these benefits if they reach retirement age while working for the Company. The Company's cost for providing postretirement benefits other than pensions is accounted for in accordance with ASC 715, "Compensation – Retirement Benefits." The following tables set forth the amounts recognized for the postretirement benefit plan in the Company's consolidated financial statements as of December 31, 2016 and 2015 (in thousands):

	2016	2015
Change in accumulated postretirement obligation:		
Accumulated postretirement obligation at beginning of year	\$ 66,087	\$ 64,801
Service cost	4,181	5,114
Interest cost	2,947	2,735
Actuarial loss (gain)	2,896	(5,723)
Benefits paid	(853)	(935)
Participant contributions	82	95
Retiree Drug Subsidy receipts	91	—
Accumulated postretirement obligation at end of year	75,431	66,087
Funded status and accrued prepaid pension cost	\$ (75,431)	\$ (66,087)

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The net amount reported in the consolidated balance sheets related to the accrued benefit cost for the postretirement plan of \$75.4 million and \$66.1 million, as of December 31, 2016 and 2015, respectively, is included in other liabilities. The unamortized amount of accumulated other comprehensive loss related to the postretirement plan is \$12.9 million and \$10.4 million, before taxes, as of December 31, 2016 and 2015, respectively.

The weighted average assumptions used to calculate the benefit obligation as of December 31, 2016 and 2015 are as follows:

	<u>2016</u>	<u>2015</u>
Discount rate	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%

The discount rate represents the Company's estimate of the interest rate at which the postretirement benefit plan benefits could be effectively settled. The discount rates are used in the measurement of the expected and accumulated postretirement benefit obligations and the service and interest cost of net periodic postretirement benefit cost.

Net periodic benefit cost included in the Company's consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 is comprised of the following (in thousands):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net Periodic Benefit Cost:			
Service cost	\$ 4,181	\$ 5,114	\$ 4,236
Interest cost	2,947	2,735	2,268
Recognized actuarial loss	492	1,309	581
Net periodic benefit cost	<u>\$ 7,620</u>	<u>\$ 9,158</u>	<u>\$ 7,085</u>
Change in accumulated other comprehensive loss (income):			
Beginning balance	\$ 10,447	\$ 17,479	\$ 9,957
Actuarial loss (gain) arising during the year	2,896	(5,723)	8,103
Amortization of actuarial loss recognized in net periodic costs.....	<u>(492)</u>	<u>(1,309)</u>	<u>(581)</u>
Accumulated other comprehensive loss at end of year	<u>\$ 12,851</u>	<u>\$ 10,447</u>	<u>\$ 17,479</u>

The Company estimates that the net periodic benefit costs relating to this plan will be \$8.5 million for the year ended December 31, 2017.

The weighted average assumptions used to calculate the net periodic benefit cost for the years ended December 31, 2016, 2015 and 2014 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Discount rate	4.50%	4.25%	4.50%
Rate of compensation increase	3.80%	3.80%	4.00%

The postretirement plan's expected benefit payments for the next 10 years are shown below (in thousands):

<u>Year</u>	<u>Amount</u>
2017	\$ 1,396
2018	1,603
2019	1,957
2020	2,289
2021	2,590
2022 - 2026	17,958

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The amortization of actuarial losses and of prior service costs (currently reflected in accumulated other comprehensive income) as components of net periodic costs are expected to be \$0.7 million and \$0.0 million, respectively, for the year ended December 31, 2017.

The annual assumed rate of increase in the per capita cost of covered benefits (i.e., health care cost trend rate) is assumed to be 6.5% in 2017, gradually decreasing to 4.5% in 2038 and remaining constant thereafter. The health care cost trend rate assumption has a significant effect on the amounts reported. For example, increasing the assumed health care cost trend rates by one percentage point in each year would increase the accumulated postretirement benefit obligation by \$14.9 million (19.8% of the benefit obligation as of December 31, 2016) and the service and interest cost components of net periodic postretirement benefit costs by \$1.6 million for the year ended December 31, 2016. Decreasing the assumed health care cost trend rates by one percentage point in each year would decrease the accumulated postretirement benefit obligation and the service and interest cost components of net periodic postretirement benefit cost for the year ended December 31, 2016 by \$11.9 million and \$1.3 million, respectively.

Other Plans

The Company also maintains a defined contribution profit sharing plan for all eligible employees. Each year, the Board of Directors may authorize payment of an amount equal to a percentage of each participant's basic annual earnings based on the results of the Company for that year. These amounts are credited to the employee's account maintained by a third party, which has contracted to provide benefits under the plan. No contributions were authorized for the years ended December 31, 2016, 2015 or 2014.

The Company maintains a qualified deferred compensation plan pursuant to Section 401(k) of the Internal Revenue Code of 1986, as amended. Employees may contribute up to 50% of base salary on a pre-tax basis, subject to annual maximum contributions set by law (\$18,000 in 2016 plus an additional \$6,000 if an employee is age 50 or older). The Company contributes an amount equal to 100% of each employee's pre-tax contribution up to certain limits. The maximum matching contribution is 4.0% of annual base salary, with certain government-mandated restrictions on contributions to highly compensated employees. The Company also maintains a non-qualified deferred compensation plan to allow for contributions in excess of qualified plan limitations. The Company's contributions to both of these plans, which totaled \$3.1 million, \$3.0 million, and \$2.7 million for the years ended December 31, 2016, 2015 and 2014, respectively, are included primarily in other underwriting expenses in the consolidated statements of operations.

All employees in the United States hired on or after August 1, 2011 are eligible for an annual profit sharing contribution, subject to Plan limitations. The Company makes this contribution regardless of whether or not elective deferrals were made during the year. The profit sharing contribution is paid each January and uses the prior year's 401(k) compensation (base pay, short-term disability earnings and any overtime earnings) to determine the actual contribution for each employee. These profit sharing contributions are calculated as a percentage of earnings at the end of each year and allocated to participant accounts in January of the following year.

The profit sharing contribution percentages are based upon each employee's years of service as follows:

<u>Years of Service</u>	<u>Percent</u>
Less than or equal to 5 years	6%
More than 5 years but less than or equal to 15	7%
More than 15 years	8%

The profit sharing contribution amounts vest based upon the following vesting schedule:

<u>Years of Service</u>	<u>Percent</u>
Less than 2 years	0%
2 years but less than 3	20%
3 years but less than 4	40%
4 years but less than 5	60%
5 years but less than 6	80%
6 years or more.....	100%

ODYSSEY RE HOLDINGS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

15. Stock-Based Compensation Plans

Fairfax Restricted Share Plan and Share Option Plan

In 1999, Fairfax established the Fairfax Financial 1999 Restricted Share Plan (the “Fairfax Restricted Share Plan”) and the Share Option Plan (the “Option Plan”) (collectively, the “Fairfax Plans”), in which the Company participates. The Fairfax Plans generally provide officers, key employees and directors who were employed by or provided services to the Company with awards of restricted shares or stock options (with a grant price of zero) of Fairfax common stock (collectively, “Restricted Share Awards”). The Restricted Share Awards generally vest over five years. The Company had 219,552 Restricted Share Awards outstanding as of December 31, 2016.

The fair value of the Restricted Share Awards is estimated on the date of grant based on the market price of Fairfax’s stock and is amortized to compensation expense on a straight-line basis over the related vesting periods. The Company purchases Fairfax common stock on the open market to cover the grant of a Restricted Share Award and reflects such purchase as a reduction in the Company’s additional paid-in capital. As of December 31, 2016, there was \$50.3 million of unrecognized compensation cost related to unvested Restricted Share Awards granted from the Fairfax Plans that was netted against additional paid-in capital, which is expected to be recognized over a remaining weighted-average vesting period of 2.6 years. The total fair values of the Restricted Share Awards granted for the years ended December 31, 2016, 2015 and 2014 were \$14.2 million, \$21.1 million and \$17.3 million, respectively. As of December 31, 2016, the aggregate fair value of the Restricted Share Awards outstanding was \$51.0 million. For the years ended December 31, 2016, 2015 and 2014, the Company recognized expense related to the Fairfax Plans of \$14.2 million, \$12.9 million and \$9.7 million, respectively.

The following table summarizes activity for the Fairfax Plans for the year ended December 31, 2016:

	Shares / Options	Weighted- Average Value at Grant Date
Awards outstanding as of December 31, 2015.....	201,905	\$ 428.51
Granted	30,653	464.78
Vested	(39,149)	392.20
Forfeited.....	(2,895)	432.27
Unallocated	29,038	476.83
	<u>219,552</u>	<u>\$ 446.39</u>
Awards outstanding as of December 31, 2016.....		
	<u>2,164</u>	<u>\$ 362.87</u>

Employee Share Purchase Plans

Under the terms of the Odyssey Re Holdings Corp. (Non-Qualified) 2010 Employee Share Purchase Plan (the “2010 ESPP”), eligible employees are given the election to purchase Fairfax common shares in an amount up to 10% of their annual base salary. The Company matches these contributions by purchasing, on the employee’s behalf, a number of Fairfax’s common shares equal in value to 30% of the employee’s contribution. In the event that the Company achieves a net combined ratio in any calendar year that is less than the lesser of i) 100% or ii) the average of the reported net combined ratios of the ten (10) most recent calendar years prior to the current calendar year, additional shares are purchased by the Company for the employee’s benefit, in an amount equal in value to 20% of the employee’s contribution during that year. During the year ended December 31, 2016, the Company purchased 12,753 Fairfax common shares on behalf of employees pursuant to the 2010 ESPP, at an average purchase price of \$566.22. The compensation expense recognized by the Company for purchases of Fairfax’s common shares under the 2010 ESPP was \$2.7 million, \$1.8 million and \$1.0 million for the years ended December 31, 2016, 2015 and 2014, respectively.



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